CENTRAL BANK OF LESOTHO

QUARTERLY REVIEW

JUNE, 2013

VOLUME XXXII, NO. 2

MASERU
KINGDOM OF LESOTHO

Table of Contents

List of Tables

List of Figures

I. Overview

Generally, economic performance in the emerging market economies continued to outpace performance in the advanced economies. In the US, Economic activity picked up modestly despite continued fiscal tightening. Real GDP growth was 1.7 per cent compared to 1.1 per cent rise in the first quarter of 2013. Growth continued to be driven by personal consumption expenditures, exports, non-residential fixed investment, private inventory investment and residential investment while a surge in imports and a slowdown in federal government spending slightly dampened the increase.

Euro zone, the second largest economy in the world after the US, remained mired in recession during the second quarter of 2013. Real GDP deteriorated by 0.7 per cent in the second quarter of 2013 compared with a decline of 1.1 per cent in the previous quarter. The fiscal austerity continued to hold back most economies mostly the periphery economies. Nonetheless, Euro zones largest economies, Germany and France, posted positive performance. Growth in exports, robust consumer and business spending were the key drivers of economic activity.

Economic growth in South Africa grew at a pace of 2.0 per cent in the second quarter of 2013 compared with 1.9 per cent in the previous quarter. Growth continued to be fuelled by a strong growth in manufacturing output, real estate, finance and business services. In line with lacklustre economic performance globally, inflation remained under control. In the US and the Euro zone, the inflation rate was 1.8 per cent in the second quarter compared with 1.5 per cent in the inflation rate remained below 2.0 per cent. In South Africa the inflation rate dropped from 5.9 per cent to 5.5 per cent. However, the movement in the exchange rate and the prices of food and oil will determine the trajectory of inflation.

Lesotho's economy displayed positive performance, based on a number of economic indicators, during the second quarter of 2013. Production by the diamond mining industry picked up again following a temporary production stoppage in the previous quarter. Activity in the textiles and clothing industry, measured by exports of textile and clothing to the US, continued on an upward trend. The number of imported motor vehicles a measure general consumer demand also increased. Electricity consumption a measure of the performance of the manufacturing industry increased while water consumption contracted. Employment by both LNDC assisted companies and Government increased during the second quarter of 2013, and this was consistent with the growth exports of textile and clothing to the US.

Money supply (M2) expanded by 2.0 per cent during the quarter under review following a 3.2 per cent decrease observed in the first quarter of 2013 , and it was driven by the expansion in net foreign assets and domestic credit. Short-term interest rates remained unchanged reflective of an unchanged monetary policy stance by South Africa since July 2012. Government registered a surplus for the second quarter 2013. The surplus continued to reflect more revenues which outweigh expenditures, despite a strong growth in expenditures. The expansion in total public debt reflected higher external debt which was driven by the depreciation of the rand vis-à-vis the US dollar. As a share of GDP, the current account balance registered a deficit of 13.0 per cent in the second quarter, compared with a deficit of 19.7 per cent in the previous quarter. The narrowing of the current account balance reflected a fall in both exports and imports.

II. International Economic Developments

Developments in the second quarter of 2013 reflected weak global economic activity. Economic activity continued to weaken in advanced economies, particularly in the Euro Area, amid continuing recession. Japan's GDP improved marginally to 0.9 per cent from 0.3 per cent recorded in the previous quarter aided by Japan's massive monetary stimulus. Real GDP in the United States (US) picked up moderately portraying the economy's resilience to the weak global economic activity. For emerging economies, growth also remained feeble mainly due to the effects of the slow global demand.

On the commodity front, international crude oil prices continued to fall in line with a slowdown in energy demand worldwide. The price of gold continued to decline due to worries about the narrowing of the monetary stimulus by the US Federal Reserve, which led to a fall in investment on precious metals mainly gold. The price of platinum also fell due to weak global demand, particularly in Europe. Regarding agricultural products, prices moved in different directions, with maize price declining while the price of wheat increased.

Table 1: Key World Economic Indicators

	Real GDP Growth		Inflation Rate		Key Interest Rate		Unemployment Rate	
	QI: 2013	QII: 2013	QI: 2012	QII: 2013	QI: 2012	QII: 2013	QI: 2013	QII: 2013
US	1.1	1.7	1.5	1.8	0.25	0.25	7.6	7.6
Euro Area	-1.1	-0.7	1.7	1.7	0.75	0.75	12.1	12.1
Japan	0.3	0.9	-0.7	0.2	0.00	0.00	4.1	3.9
SA	1.9	n/a	5.9	5.5	5.00	5.00	25.2	25.6
China	7.7	7.5	2.1	2.7	6.00	6.00	4.1	n/a
India	4.8	n/a	5.7	4.9	7.50	7.25	n/a	n/a

Source: Bloomberg, The Economist, STATSSA and SARB, OECD National Accounts Statistics (database), US Bureau of Economic Analysis, National Bureau of Statistics of China, Statistics Bureau of Japan, Government of India Department of labour

Advanced Economies

United States (US)

Real GDP growth picked up moderately during the second quarter of 2013, despite the austerity measures[1] undertaken by the US government. It recorded a 1.7 per cent increase against a 1.1 per cent rise in the first quarter of 2013. The faster growth was largely attributed to improvements in personal consumption expenditures, exports, non-residential fixed investment, private inventory

[1] Austerity refers to measures taken by the governments to cut expenditure in an attempt to reduce growing budget deficits, especially during adverse economic conditions.

investment and residential investment while a surge in imports and a slowdown in federal government spending slightly dampened the increase.

The US inflation rate accelerated to 1.8 per cent in June 2013, from 1.5 per cent in March 2013, largely due to a sharp rise in the price of gasoline. In addition, the price of clothing, shelter and medical care also contributed to the increase. The US Federal Open Markets Committee (FOMC) continued to keep its benchmark lending rate unchanged at 0.25 per cent in order to boost the economy.

Unemployment rate remained unchanged at 7.6 per cent in June 2013 despite an increase of 188,000 in US nonfarm employment. This development was largely driven by an increase in job losers and persons who completed temporary jobs. Moreover, this showed that people remained in the labour market rather than giving up the search for work. The sectors that recorded an increase were leisure and hospitality, professional and business services, retail trade, health care and financial activities.

Euro-Area[2]

Economic activity in the Euro Area continued to weaken due to ongoing economic and fiscal problems in the peripheral countries. Real GDP deteriorated by 0.7 per cent in the second quarter of 2013 compared with a decline of 1.1 per cent in the previous quarter. Nonetheless, an improvement was realized in the core countries, specifically Germany and France with the growth rates of 0.5 per cent and 0.3 per cent, respectively. This improvement was brought by increased business and consumer spending, improvements in inventories as well as increased exports.

Inflation decelerated to 1.6 per cent in June 2013 from 1.7 per cent in March 2013. The largest contributor was fuel for transport followed by telecommunication. The moderation was slightly offset by a rise in electricity and food, particularly fruits and vegetables. The European Central Bank's (ECB's) Monetary Policy Committee kept its key interest rate at 0.50 percent in June 2013. The rate was cut by 25 basis points in March 2013 in an effort to continue to stimulate economic growth and employment creation.

Unemployment rate remained unchanged at 12.1 percent in June 2013 relative to the previous quarter, amid weak economic activity. Amongst the member states, the lowest unemployment rates were recorded in Austria, Germany and Luxemburg, with 4.6 per cent, 5.4 per cent and 5.7 per cent, respectively while Spain and Greece recorded the highest unemployment rates of 26.3 per cent and 26.9 per cent, respectively, during the period.

Japan

The performance of the Japanese economy improved slightly during the quarter under review. Real GDP grew by 0.9 per cent in the quarter ending in June 2013 compared with an increase of 0.3 per cent in the previous quarter. The increase was ascribed to a rise in private consumption, public investment and net exports. Japan's economic performance is however clouded by

[2] Euro Area: Austria, Belgium, Cyprus, Estonia, Germany, Greece, Finland, France, Ireland, Italy, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.

uncertainties regarding the planned increase in sales tax[3] (from 5 per cent to 8 per cent from April 2014 and subsequently 10 per cent in 2015) in an attempt to reduce public debt which is currently more than 200 per cent of Japan's annual GDP. This could negatively affect the economy through reduced consumption spending.

Inflation picked-up to 0.2 per cent from a long period of deflation giving signals that there could be a recovery in economic activity. The increase was due to a surge in electricity bills as well as the increased cost of gasoline imports due to a weak yen. The Bank of Japan decided to keep the key interest rate constant at 0.0 per cent in an effort to encourage borrowing to stimulate economic growth.

The unemployment rate fell to 3.9 percent in the quarter ending in June 2013 from 4.1 per cent in the previous quarter, its lowest since October 2008. The observed improvement was registered in medical and health care, finance and insurance, information and communication, as well as scientific research.

Emerging Market Economies

China

Real GDP grew at a slower rate of 7.5 per cent in the second quarter compared to an increase of 7.7 per cent in the previous quarter. The slowdown was largely attributed to weaker external demand, which implied a decline in Chinese exports. Also, growth in factory output as well as in fixed-asset investment weakened.

Inflation accelerated to 2.7 per cent in June 2013 compared to an increase of 2.1 per cent in March 2013, on account of food prices which increased by 4.9 per cent during the period. The key interest rate was kept unchanged at 6.0 per cent by the People's Bank of China's MPC. This was done to promote a stable and relatively faster economic growth. The government of China has introduced a number of measures in an attempt to stabilize and boost the economy. These include tax breaks meant to boost small and micro sized enterprises, reduced fees for exporters and opening up of railway construction. Further, the government continues to increase financial support for the real economy as well as promote stable and healthy development of the real estate sector.

India

Industrial production fell at an annual rate of 2.2 per cent in June 2013 compared to an increase of 3.4 per cent in March 2013. The decline was ascribed to weak manufacturing and mining performance. Output of capital goods as well as utilities also fell during the period.

Inflation decelerated to 4.9 per cent in June 2013 following a 5.7 per cent increase in March 2013. The moderation was due to a decline in items such as coal, aviation turbine fuel and petrol while an increase in the price of food and the increased costs of electricity slightly offset the decline.

[3] The government of Japan is expected to make a decision later in the year on whether to go ahead with the planned tax hike (of increasing the sales tax from 5 per cent to 8 per cent from April 2014 and subsequently increase it to 10 per cent in 2015).

In an attempt to stimulate economic growth, the Reserve Bank of India decided to cut the repo rate by 25 basis points in May 2013, which was subsequently left unchanged in June 2013. The decision was based on measures put in place since January 2012, which were meant to support growth. These measures included a shift in policy stance by the Reserve Bank towards addressing growth, which had decelerated continuously and steeply. Moreover, the Bank had also indicated that the monetary policy would guard against the risks to inflation while at the same time ensuring adequate credit flow to the productive sectors of the economy.

South Africa

The leading indicator of economic output, industrial production, increased by 0.4 per cent in June 2013 compared to a decrease of 1.4 per cent in March 2013. This growth was attributed to an increase in manufacturing production as well as vehicle sales. The increase in manufacturing production arose from higher production in basic iron and steel, non-ferrous metal products, and food and beverages. The increase in these two components was, however, moderated by the decline in production in the mining sector. This was as a result of the negative growth rates in both the gold and platinum production, due to the on-going labour unrest and sluggish growth of the economy.

Inflation decelerated to 5.5 per cent in June 2013 from 5.9 per cent in March 2013, in line with the moderating price of gasoline. However, there were concerns that the recent depreciation of the rand and higher wages could push the inflation rate above the target range of 3 – 6 per cent. The combination of high inflation rate and low economic growth has however left the Reserve Bank with limited room for policy action. South African Reserve Bank's (SARB's) Monetary Policy Committee decided to keep the repo rate unchanged at 5.0 per cent in an effort to support growth as the Euro Area crisis continued to weigh heavily on South Africa's economic activity.

Unemployment accelerated to 25.6 percent in the second quarter of 2013 compared to an increase of 25.2 per cent in the previous quarter. The observed unemployment rate was the highest in 2 years. The number of unemployed persons increased by 5.7 percent, undermining the observed improvements in employed persons which registered an increase of 2.0 per cent. Employment gains were more pronounced in Finance and Other Business Services, Agriculture, and Construction industries while job losses were recorded in Private households and Trade industries.

Commodities

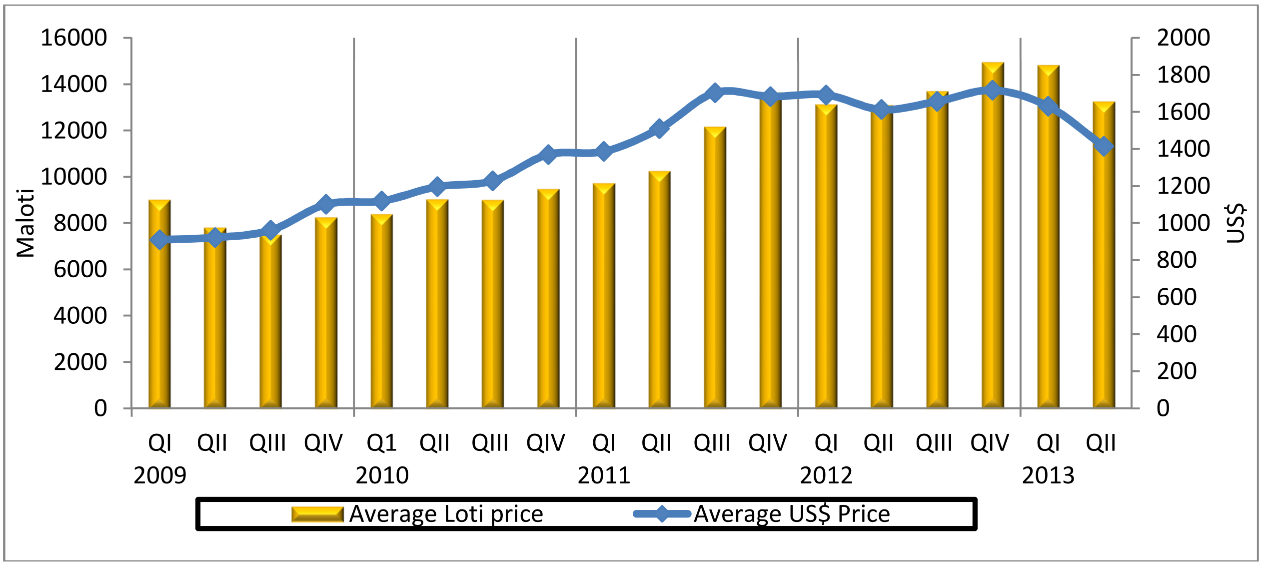
Minerals

Gold

In US dollar terms, the average price of gold declined by 13.2 per cent to US$1 414.7 per ounce during the second quarter of 2013, compared with a fall of 5.0 per cent in the previous quarter. In terms of Maloti, it declined by 10.5 per cent to M13 246.6 per ounce compared to a decrease of 0.9 per cent in the quarter ending in March 2013. The drop was driven by slower global demand, in particular, China as it is a more important player in the international commodity markets. Moreover, the decline in global demand was attributed to investors' concerns that the US Federal Reserve Bank may cut down its monetary stimulus for American economy this year. The quantitative easing triggers consumption and investment which in turn increase inflation.

Given that gold is used to hedge against inflation, any move towards quantitative easing taper will lead to a fall in demand for gold and hence its price.

Figure 1: Average Price of Gold

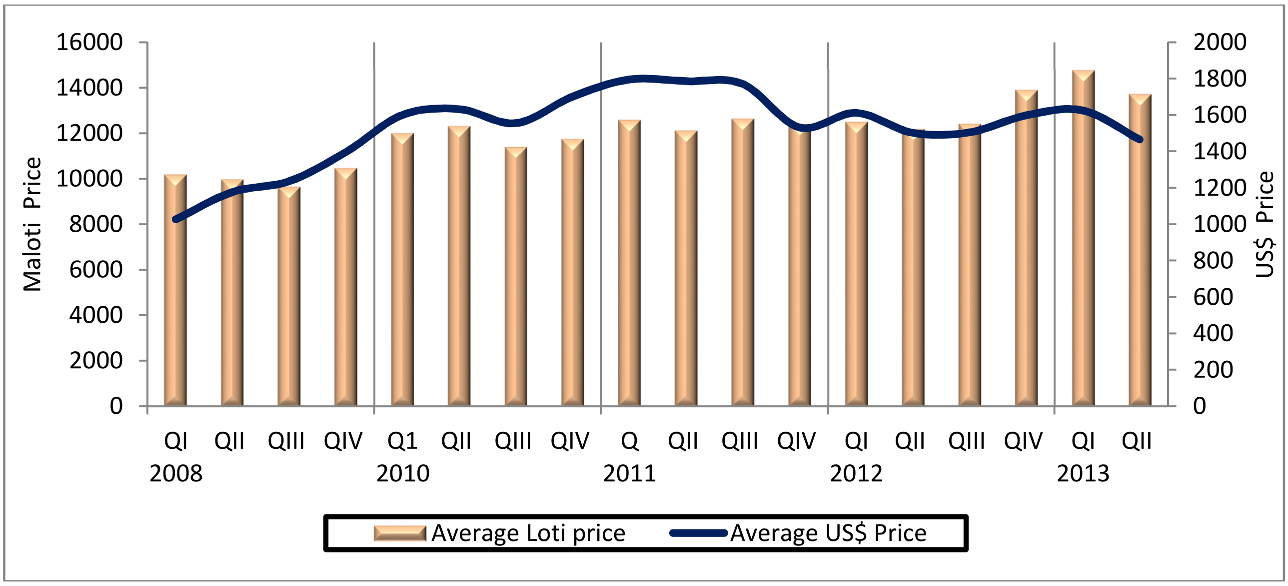


Source: Bloomberg

Platinum

During the second quarter of 2013, the average price of platinum in US Dollar terms decreased by 9.8 per cent to US$1 465.3 per ounce relative to an increase of 1.7 per cent in the quarter ending in March 2013. In terms of Maloti, it declined by 7.0 per cent to M13 714.9 per ounce compared to a rise of 6.1 per cent in the previous quarter. This decline was attributed to lower production of vehicles, which mainly uses platinum. This led to reduced demand for platinum which resulted in a fall in global price of platinum.

Figure 2: Average of Price of Platinum



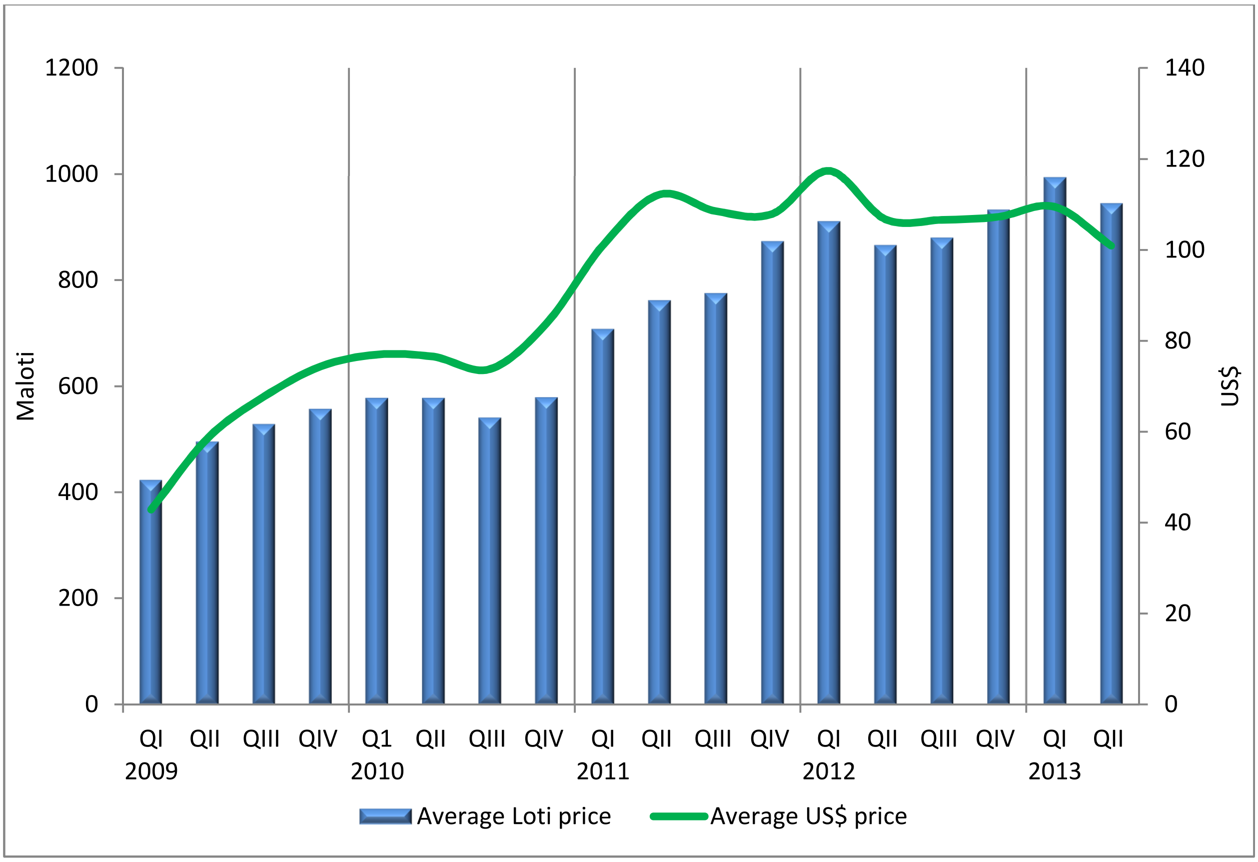
Source: Bloomberg

Energy

Oil

The average price of crude oil in US Dollar terms decreased during the quarter ending in June 2013. It recorded a drop of 7.8 per cent to US$100.9 per barrel compared to an increase of 2.1 per cent in the previous quarter. In Maloti terms, the price declined by 5.0 per cent to M944.9 per barrel. The slowdown was ascribed to a weakening demand for heavy machinery and a fall in energy demand worldwide.

Figure 3: Average Price of Oil



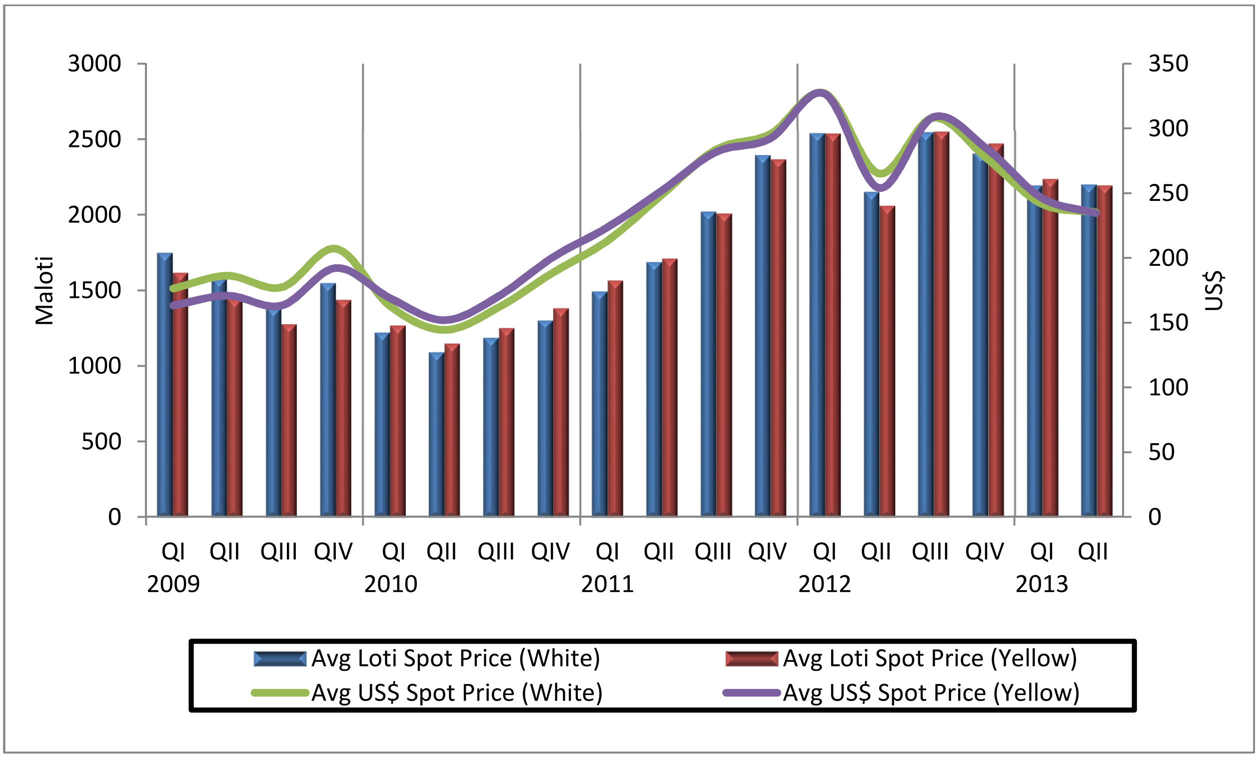
Source: Bloomberg

Agricultural Products

Maize

The average prices of white and yellow maize continued to decrease during the second quarter of 2013. In US Dollar terms, prices fell by 2.7 per cent to US$235 per tonne and 4.8 per cent to US$235 per tonne, respectively. In Maloti terms, the average price of white maize decreased by 0.3 per cent to M2 202.2 per tonne while that of yellow maize declined by 1.9 per cent to M2 195.27 per tonne. This slowdown was attributed to increased harvest in Argentina and Brazil, which augmented market supplies.

Figure 4: Average Spot Price of Maize

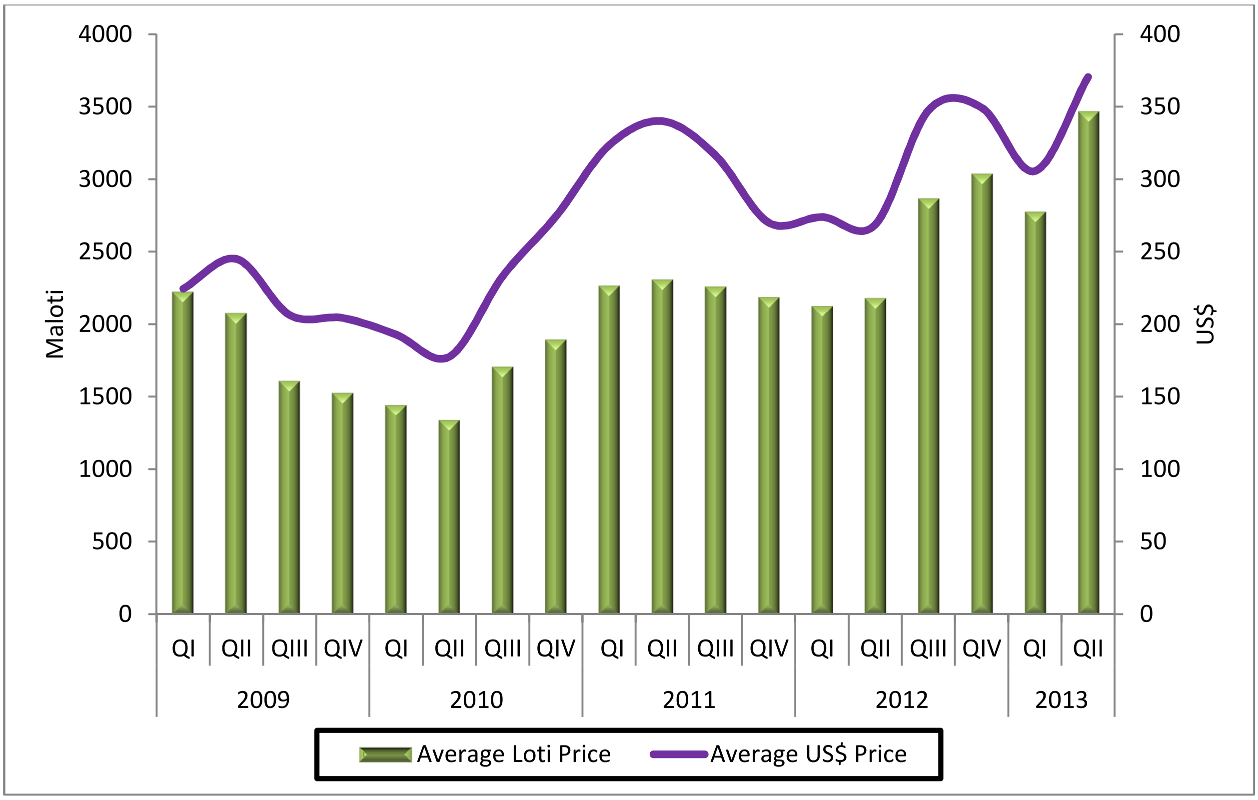


Source: Bloomberg

Wheat

During the review period, the average price of wheat surged by 21.3 per cent to US$370.5 per tonne, while in Maloti terms it increased by 25 per cent to M3 467 per tonne. The increase is ascribed to a rise in demand for wheat to meet livestock feed needs. Lower supplies of wheat from key producing countries also contributed to the hike in prices.

Figure 5: Average Spot Price of Wheat



III. Real Sector, Employment and Price Developments

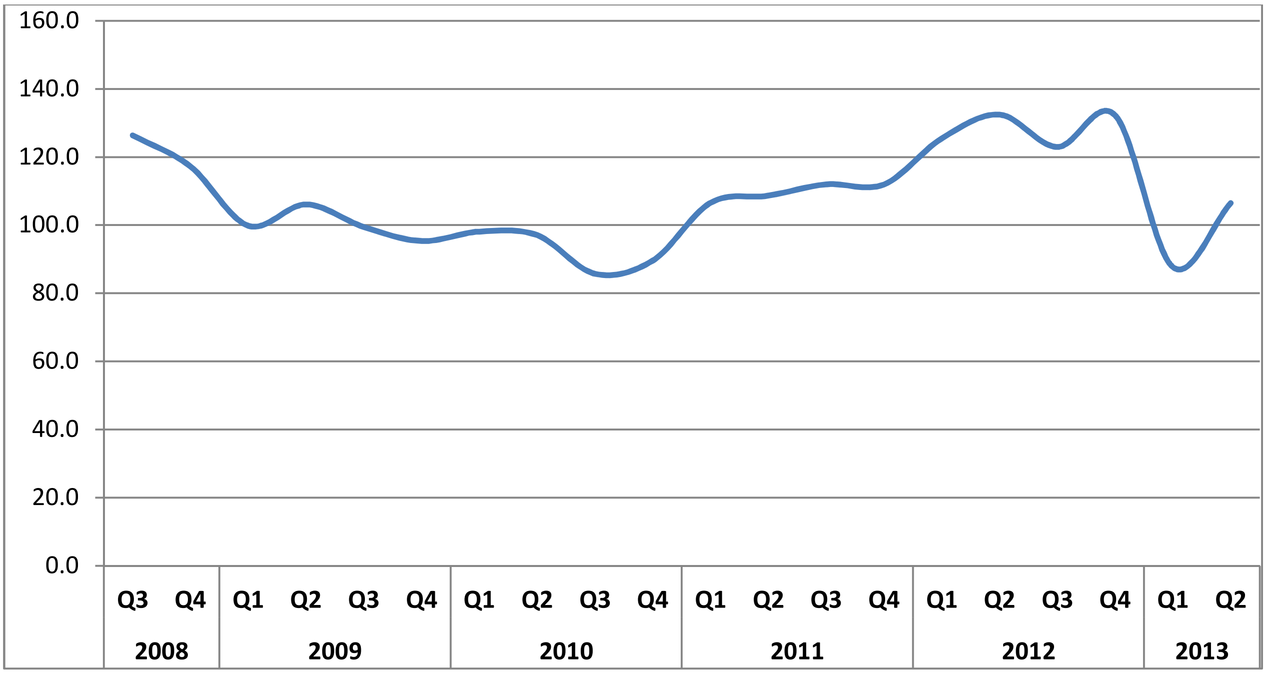
Overview

Lesotho's economy displayed positive performance during the second quarter of 2013. Production by the diamond mining industry increased following a decline related to temporary production stoppage in the previous quarter. Activity in the textiles and clothing industry continued on an upward trend. The number of imported motor vehicles also increased. Electricity consumption rose owing to increased economic activity in the economy while water consumption and sales turnover declined. Employment by the LNDC assisted companies and by Government also increased during the period under review.

Primary Sector Developments

The weighted Diamond Production Index (WDPI) rose by 21.5 per cent during the quarter ending in June 2013, following a decline of 31.7 per cent in the first quarter of 2013. This increase resulted mainly from the recovery of Let'seng mine's production following temporary stoppage in the first quarter of 2013 while some test work was being undertaken to establish diamond damage profiles and new crushers were being installed with the objective of reducing diamond damage. Production by Liqhobong mine also increased during the review quarter.

Figure 6: Weighted Diamond Production Index



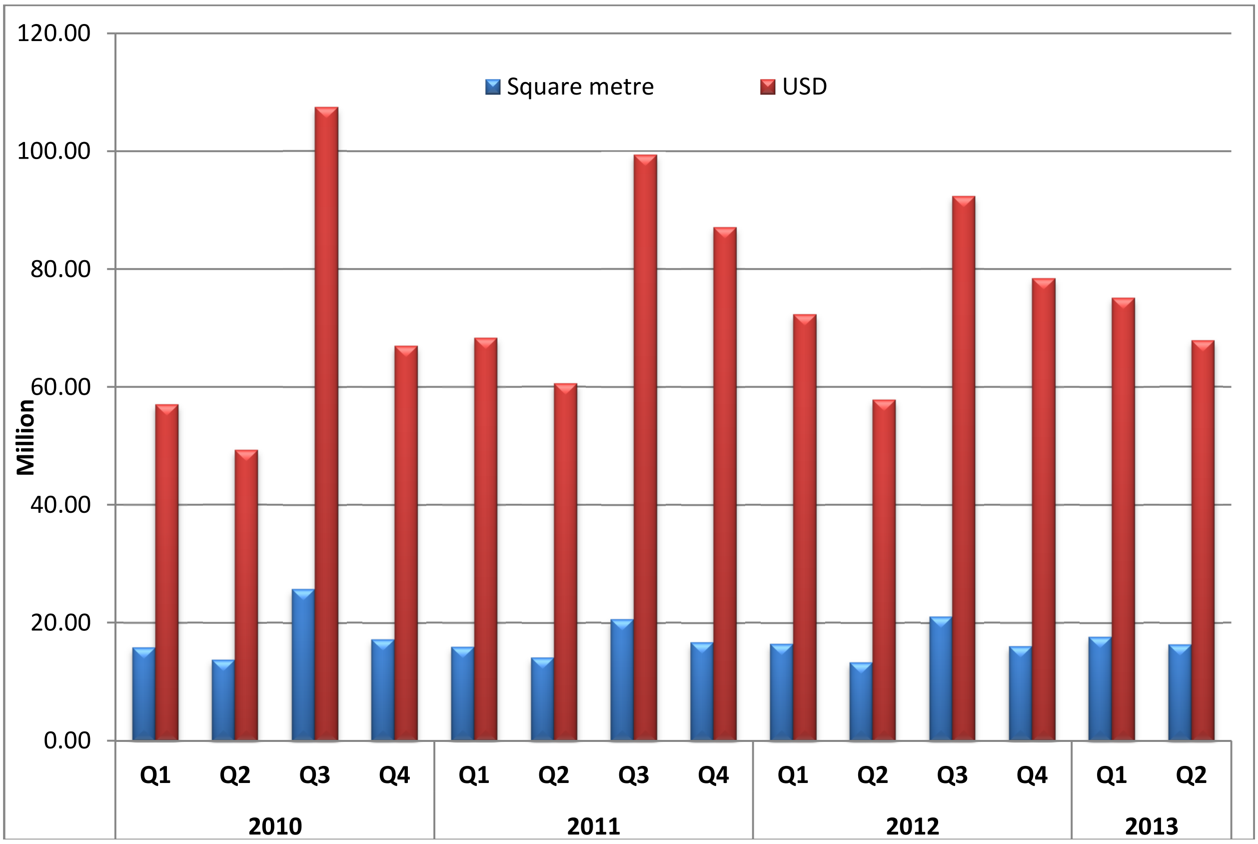
Source: Department of Mines and Geology

Secondary Sector Developments

Textiles and Clothing Manufacturing

The volume of Lesotho's exports of textiles and clothing to the US, measured in square meters, a proxy for Lesotho's textiles and clothing industry's performance, registered a quarterly decline of 7.2 per cent in the quarter ending in June 2013 following a 10.0 per cent increase in the previous quarter. Lesotho's textiles and clothing industry remained under pressure due to relatively higher production costs that were exacerbated by the rise in electricity tariffs during the review quarter coupled with increasing completion from Asian producers for the US market, notably Vietnam and Bangladesh. However, on an annual basis, the volume of exports of textiles and clothing increased by 22.7 per cent during the review period compared with 6.9 per cent in the quarter ending in March 2013 reflecting higher demand for Lesotho's textiles and clothing products by US buyers associated with the recovery in their confidence on Lesotho's producers following the extension of the third country fabric provision under the Africa Growth and Opportunity Act (AGOA). Further impetus came from the strengthening consumer spending in the US due to increasing household wealth, which, in turn, is being supported by the recovery of the US housing market coupled with the depreciation of the loti against the US Dollar during the review period.

Figure 7: Lesotho's Exports of Textiles and Clothing to the US



Source: Website of U.S. Department of Commerce, Office of Textiles and Apparel

Electricity Consumption

Overall electricity consumption, measured in kilowatt hour (kwh) rose by 17.4 per cent in the second quarter of 2013 following a decline of 10.1 per cent in the previous quarter. All electricity consumption categories registered increases during the review period. The general purpose, domestic, and the commercial and industrial categories registered increases of 13.1 per cent, 21.6 per cent and 16.1 per cent, respectively. The increase in overall electricity consumption reflected high electricity usage as the winter season began during the review period. Consumption rose despite the increase in electricity tariffs from the 1st of June 2013. The increase in electricity consumption by the commercial and industrial category was in line with the rise in production by both the mining and textiles and clothing industries.

Table 2: Electricity Consumption

(Units in Million Kilowatt Hours and Value in Million Maloti)

	2012				2013			
	Q3		Q4		Q1		Q2*	
	Kwh	Value	Kwh	Value	Kwh	Value	Kwh	Value
General Purpose	25.46	25.32	21.92	21.72	21.67	21.44	24.51	25.57
Domestic	61.50	45.59	54.85	49.89	53.32	50.84	64.86	66.26
Commercial & Industrial	91.65	57.34	96.99	52.06	81.30	49.94	94.37	60.20
Total	**184.61**	**128.25**	**173.76**	**123.67**	**156.30**	**122.22**	**183.75**	**152.03**

Source: Lesotho Electricity Authority and Lesotho Electricity Company
* Preliminary estimates

Water consumption

Total water consumption declined by a marginal 1.0 per cent in the quarter ending in June 2013 compared with an increase of 2.3 per cent in the previous quarter. Both the domestic and industrial categories registered lower consumption. This mainly reflected lower water usage by households and businesses during the cold winter season.

Table 3: Water Consumption

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

		Domestic	Industrial	Other	Total
2012					
Q2	Units	1.08	1.2	0.62	2.89
	Value	6.02	10.87	5.42	22.31
	Units*		1.22		2.94
Q3	Units	1.04	1.37	0.6	3.02
	Value	6.34	11.54	5.67	23.54
	Units*		1.31		2.87
Q4	Units	1.27	1.14	0.62	3.03
	Value	8	9.86	5.59	23.44
	Units*		1.03		2.74
2013					
Q1	Units	1.27	1.25	0.59	3.10
	Value	6.51	10.28	5.33	22.12
	Units*		1.46		3.63
Q2	Units	1.22	1.20	0.64	3.05
	Value	7.03	11.15	5.76	23.94
	Units*		1.22		3.10

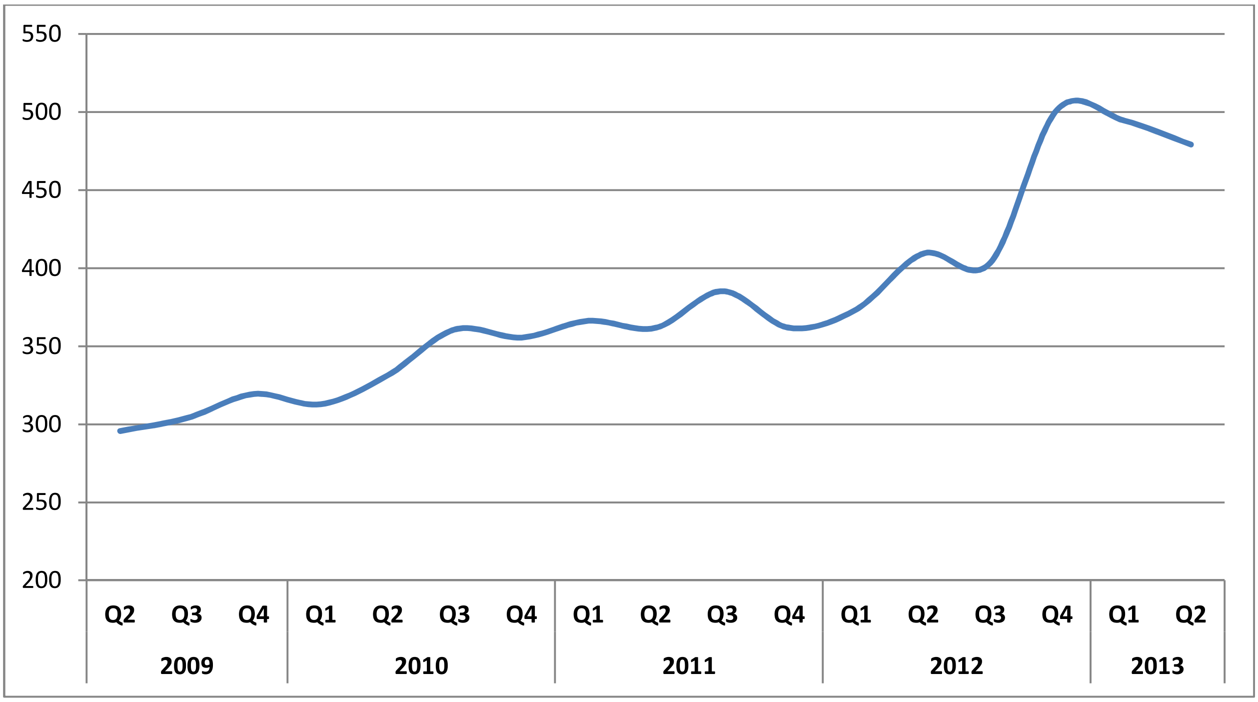
Source: Water and Sewerage Authority
* denotes seasonally adjusted figures

Tertiary Sector Developments

Sales Turnover

The value of sales turnover registered a quarterly decline of 3.1 per cent and an annual increase of 17.0 per cent during the period under review. This was the second consecutive quarterly decline in the value of sales turn over. This decline reflected lower demand in the economy during the review quarter and could be related to the winding down of some construction projects such as those related to the Millennium Challenge Account (MCA), some components of the Metolong dam project and some office buildings.

Figure 8: Value of Sales Turnover
(Million Maloti)



Source: Lesotho Revenue Authority

Investment Expenditure

Imported Motor Vehicles

The number of imported motor vehicles increased by 51.7 per cent in seasonally adjusted terms during the review quarter. The major increases were observed in the imports of trucks, buses, cars and tractors. The government purchased a higher number of trucks for construction of village roads. The increase in the total number of imported motor vehicles coupled with the purchase of high value vehicles like trucks resulted in an increase in the value of imported motor vehicles during the review quarter.

Table 4: Motor Vehicle Imports⁺

(Value in Million Maloti)

		Cars	Vans	Trucks	Buses	Tractors	M/ Cycles	Trailers	Total
2012 Q2	Value	52.77	49.78	12.68	8..27	0.41	0.00	6.27	130.18
	Units*								999
	Units	444	384	35	41	7	0	34	945
Q3	Value	66.03	83.47	13.76	7.77	3.09	0.21	3.09	177.42
	Units*								968
	Units	452	498	29	40	20	3	22	1064
Q4	Value	56.95	46.89	20.33	837	3.58	0.28	1.47	137.88
	Units*								912
	Units	374	309	39	29	40	3	20	814
2013 Q1	Value	38.53	30.21	4.71	2.27	0.44	0.12	0.96	77.24
	Units*								478
	Units	235	212	18	20	9	2	12	508
Q2	Value	56.69	48.63	18.89	7.33	8.99	0.03	2.57	125.21
	Units*								725
	Units	278	284	44	34	28	1	17	686

Source: Avis Fleet Services Lesotho and Customs Department
*denotes seasonally adjusted figures
+Includes imports of second hand cars

Employment Developments

Employment by LNDC assisted companies increased by 1.4 per cent during the second quarter of 2013, following a 1.3 per cent increase in the quarter ending in March 2013. On an annual basis, an increase of 3.6 per cent was observed compared with that of 7.7 per cent in the first quarter of 2013. The major increases were registered in the textiles and clothing manufacturing industry, particularly the woven garments manufacturing firms. This was in line with the increase in Lesotho's exports of textile and clothing to the US.

Table 5: Employment Trend of LNDC-Assisted Companies

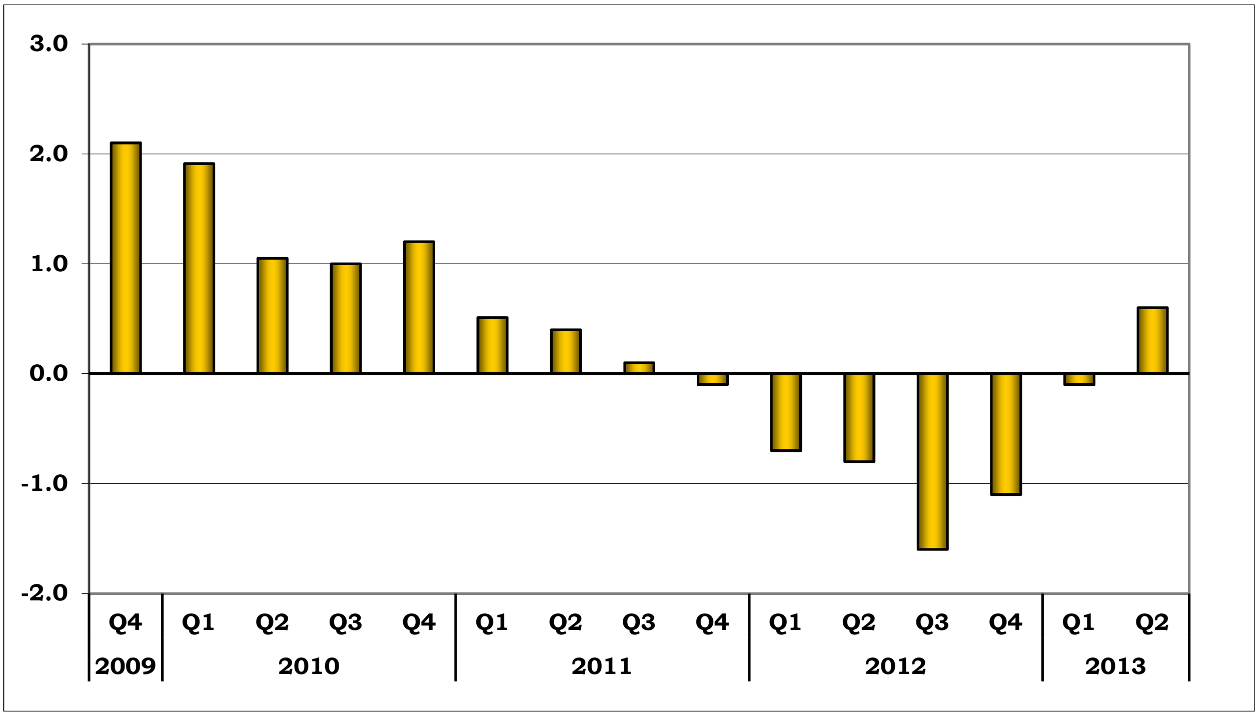
Industry	2012			2013	
	Q2	Q3	Q4	Q1	Q2*
Knit Garments	22451	22337	22824	23706	23760
Woven Garments	15243	15671	15220	14 580	15787
Footwear	2907	2895	2885	2686	2691
Fabrics, Yarn etc.	1627	1725	1714	1688	1669
Construction	295	299	295	302	294
Food & Beverages	853	857	878	888	545
Electronics	1363	1359	1290	1376	1354
Retail	135	136	136	128	128
Hotel & Accommodation	400	408	398	765	405
Other	231	264	237	350	405
TOTAL	**45 505**	**45 951**	**45 877**	**46 469**	**47 136**

Source: Lesotho National Development Corporation
*Preliminary estimates

The number of government employees increased by 0.6 per cent in June 2013 compared with a marginal decline of 0.1 per cent in March 2013. The number of civil servants and teachers increased by 0.3 per cent and 0.9 per cent, respectively while the number of daily paid workers declined by 1.7 per cent. This was the first increase in government employment since September 2011. The government created 370 new positions for teachers in July 2012 and 6 new schools were opened in January 2013 and the related on-going recruitment contributed to the observed increase in government employment. Some of the positions of civil servants that became vacant since September 2011 were also filled during the review quarter.

Figure 9: **Government Employment**

(Annual Percentage Change)

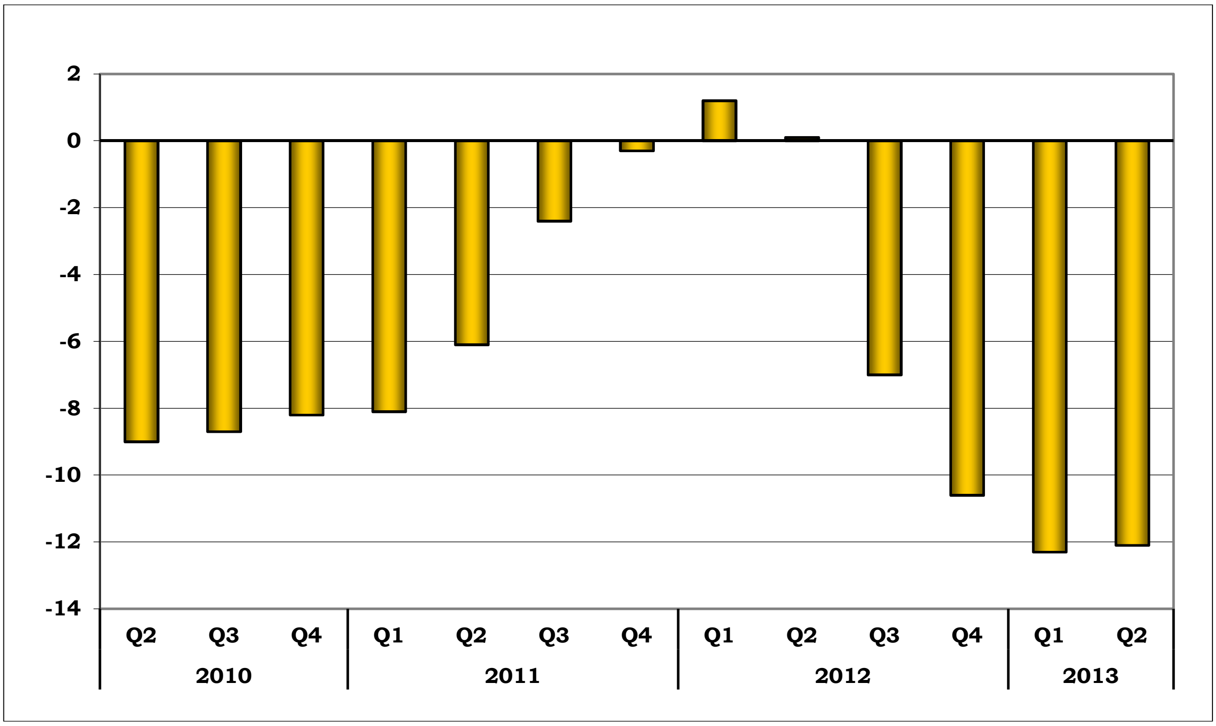


Source: Ministry of Finance

The number of Basotho migrant mineworkers declined further by 12.1 per cent in the second quarter of 2013 following a decline of 12.3 per cent in the first quarter of 2013. This was in line with the decline in employment by SA's mining and quarrying industry. According to the Statistics SA's Quarterly Employment Statistics report employment by SA's mining and quarrying industry has been registering quarterly and annual declines since the third quarter of 2012 to the first quarter of 2013. SA's mining production also declined in response to the fall in the international price of gold and platinum during the review quarter.

Figure 10: Migrant Mineworkers Employment

(Annual Percentage Change)



Source: The Employment Bureau of Africa (TEBA) and CBL estimates

Price Developments

Lesotho's inflation rate measured as a percentage change in the consumer Price Index (CPI) decelerated to 4.6 per cent in June 2013 from 5.0 per cent in March 2013. The fall in the inflation rate was mainly due to slower increases in the prices of food and non-alcoholic beverages, housing, electricity, gas and other fuels, alcoholic beverages and tobacco, clothing and footwear, and furniture, households' equipment and routine maintenance of house. The major factors behind the decline in inflation during the second quarter of 2013 were international food and crude oil prices. According to the Food and Agricultural Organization (FAO), the global food prices have recently fallen. Maize prices have been declining as favourable weather boosted hopes of a significant production increase in several leading maize producing countries. The domestic pump prices of oil products were revised downwards in line with the decline in the price of crude oil during the review period. This contributed to the deceleration in the housing, electricity, gas and other fuels category despite the increase in the domestic electricity tariffs during the review quarter.

Table 6: Inflation Rate

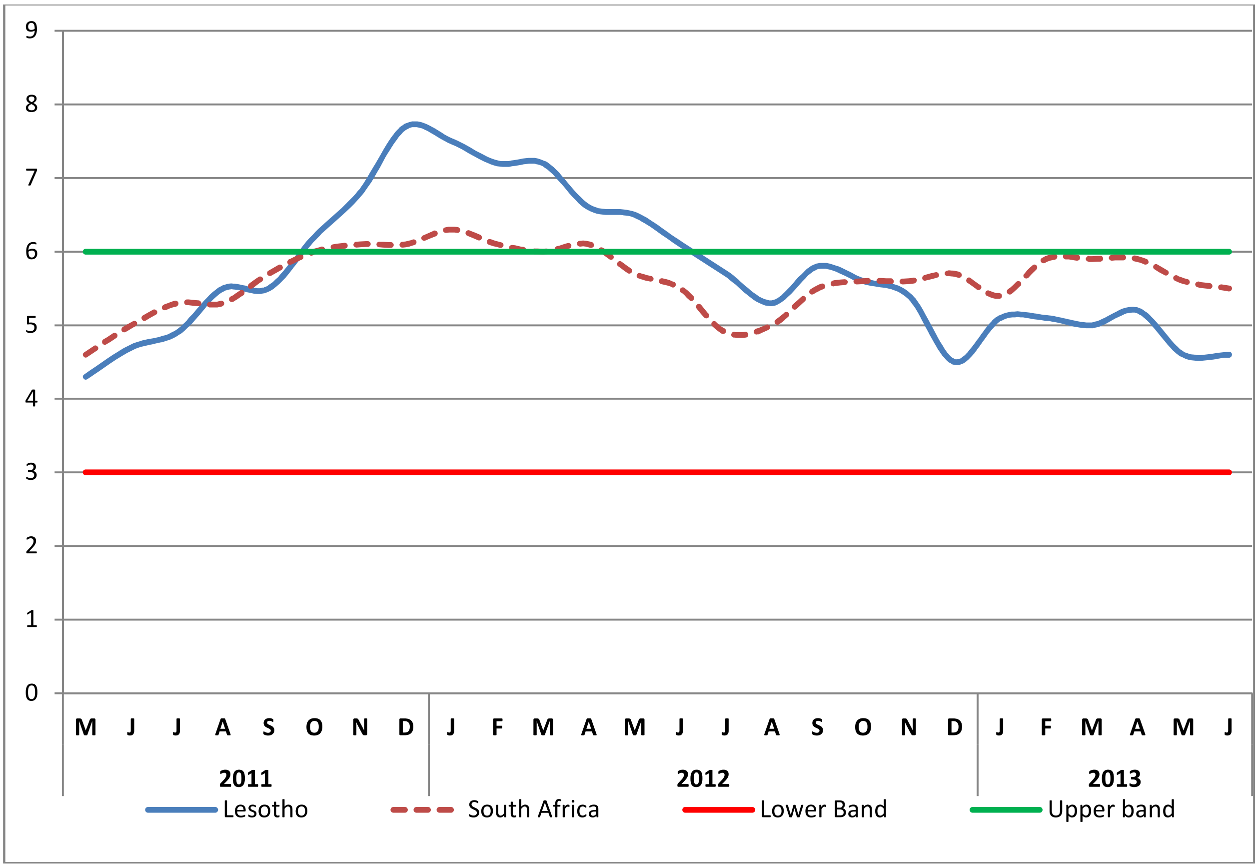
(Annual Percentage Change: March 2010 =100)

	Weight	2013				
		Feb	**Mar**	**Apr**	**May**	**Jun**
All items	**100.0**	**5.1**	**5.0**	**5.2**	**4.6**	**4.6**
Food and non-alcoholic beverages	38.1	7.2	6.5	6.4	6.1	5.7
Alcoholic beverages & Tobacco	1.2	6.9	5.8	5.6	5.5	5.6
Clothing & footwear	17.4	1.2	1.5	1.4	1.6	1.6
Housing, electricity gas & other fuels	10.6	7.2	9.8	10.4	6.6	8.1
Furniture, households equipment & routine maintenance of house	9.4	4.0	4.4	4.2	3.8	3.6
Health	1.9	0.5	0.5	0.5	0.5	0.5
Transport	8.5	0.8	0.9	0.6	0.6	0.7
Communication	1.2	0.0	0.0	0.0	0.0	0.0
Leisure, entertainment & Culture	2.4	1.3	1.2	0.9	0.9	0.8
Education	2.7	13.7	13.4	13.4	13.4	13.4
Restaurant & Hotels	0.7	0.7	1.0	1.1	1.4	1.4
Miscellaneous goods & services	5.8	2.2	2.3	2.5	2.6	2.8

Source: Bureau of Statistics, Lesotho

Lesotho's inflation rate continued to track that of South Africa (SA), reflecting Lesotho's high reliance on imports from SA. SA's CPI decelerated from 5.9 per cent in March 2013 to 5.5 per cent in June 2013. Both countries' inflation rates remained within the 3-6 per cent band. Upside risks to inflation continued to emanate from the weak Rand and the volatile crude oil prices.

Figure 11: Annual Inflation Rate for Households



Source: Bureau of Statistics Lesotho, Statistics South Africa

IV. Monetary and Financial Developments

Determinants of Money Supply

Broadly defined money supply (M2) expanded by 2.0 per cent during the quarter under review following a 3.2 per cent decrease observed in the first quarter of 2013. On an annual basis, money supply increased by 3.4 per cent compared with an increase by 6.8 per cent observed in the previous quarter. The quarterly increase in money supply was as a result of an increase in net foreign assets and domestic credit (excluding net claims on government) by 7.7 per cent and 1.8 per cent respectively.

Figure 12: Overview of Recent Monetary Developments

(Million Maloti: End of Period)

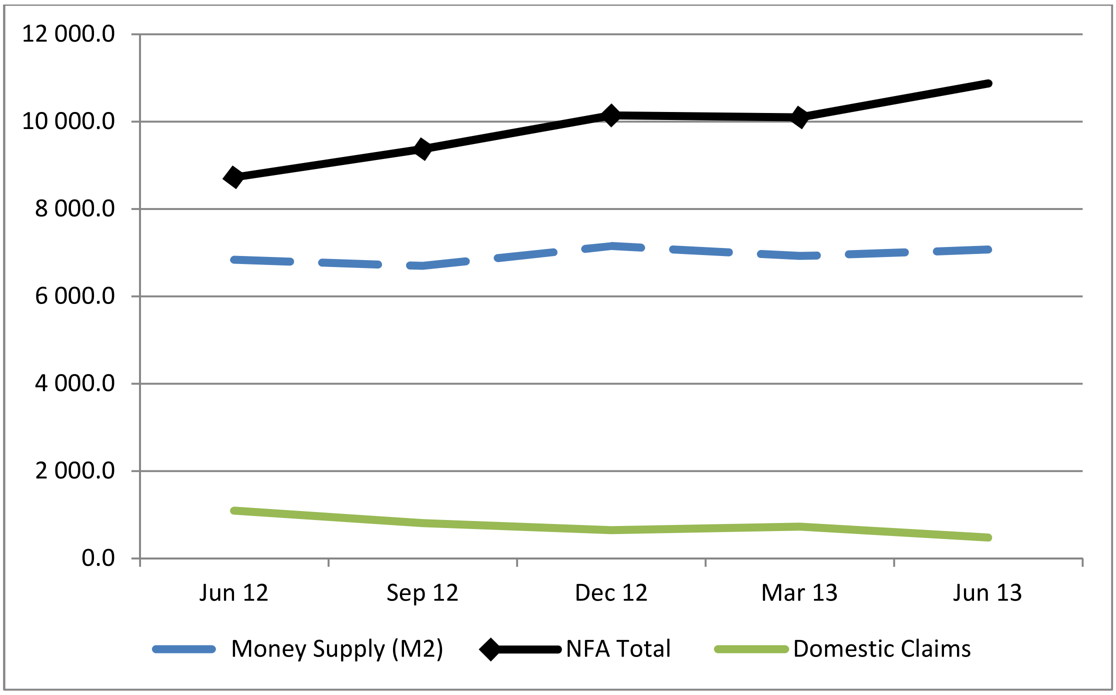


Table 7: Determinants of Money Supply

(Million Maloti: Changes)

	2012				2013	
	Q1	Q2	Q3	Q4	Q1	Q2
Net Foreign Assets	**-1 104.3**	**-74.1**	**646.8**	**766.9**	**-43.9**	**780.7**
Domestic Claims	**1 065.2**	**-82.4**	**-285.4**	**-164.8**	**85.2**	**-252.3**
Net Claims on Central Government	842.8	-317.2	-612.8	-469.1	-274.0	-328.9
Claims on other Sectors	0.3	0.5	-2.1	-0.9	1.2	0.0
Claims on Private Sector	222.1	234.3	329.5	305.2	358.0	76.6
Shares and other equity	-41.0	373.5	73.9	170.7	579.6	106.2
Other Items (NET)	177.6	-874.4	426.9	-28.2	-311.4	281.6
Broad Money Liabilities (M2)	**-175.7**	**344.5**	**-139.4**	**459.7**	**-226.4**	**140.2**

Components of Money Supply

With regard to the major components of broad money, the expansion in M2 was as a result of a 9.8 per cent increase in narrow money moderated by a 5.3 per cent decline in quasi money. The increase in narrow money was due to increases in currency outside depository corporations and transferrable deposits. The fall in quasi money was as a result of decreases in other deposits of commercial banks and other deposits held at the central bank.

Table 8: Money Supply

(Million Maloti; End of Period)

	2012			2013	
	Q2	**Q3**	**Q4**	**Q1**	**Q2**
Broad Money (M2)	**6828.4**	**6689.0**	**7148.7**	**6922.3**	**7062.5**
Narrow Money (M1)	**2789.2**	**2865.6**	**3476.3**	**3337.8**	**3666.4**
Currency Outside DCs	721.6	733.8	769.0	791.8	807.7
Transferable Deposits	2067.6	2131.7	2707.2	2546.0	2858.7
Quasi Money	**4039.1**	**3823.4**	**3672.4**	**3584.5**	**3396.1**
Other Deposits Commercial Banks	4006.8	3797.9	3652.1	3566.0	3380.6
Other Deposits Central Bank	32.3	25.6	20.3	18.5	15.5

Figure 13: Components of Money Supply

(Percentage shares)

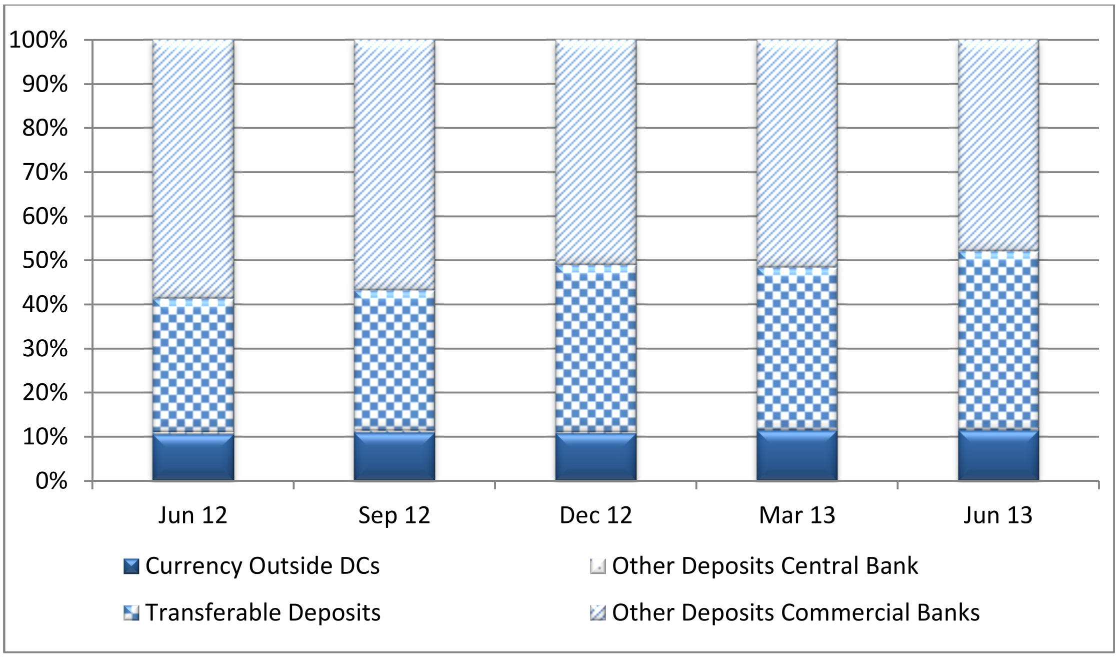


Table 9: Commercial Banks; Deposits by Holder

(Million Maloti: End of Period)

	2012			2013	
	Q2	Q3	Q4	Q1	Q2
Transferable Deposits Incl. in BM	**2067.6**	**2131.7**	**2707.2**	**2546.0**	**2858.7**
Other Financial Corporations	13.9	0.0	0.0	0.0	0.0
Public Nonfinancial Corporations	51.9	48.3	38.6	5.6	3.1
Private Sector	2001.9	2066.1	2649.9	2522.4	2837.7
Other NFCs	1391.5	1415.1	2065.7	1699.6	1974.8
Other Sectors (Households)	610.4	651.0	584.3	822.8	862.8
Other Deposits Incl. in BM	**4006.8**	**3797.9**	**3652.1**	**3566.0**	**3380.6**
Other Financial Corporations	0.0	0.0	0.0	0.0	0.0
Public Nonfinancial Corporations	25.6	22.4	20.3	3.0	3.0
Private Sector	3981.2	3775.4	3631.8	3563.0	3377.6
Other NFCs	2393.6	2363.9	2261.7	1973.7	1758.2
Other Sectors (Households)	1587.5	1411.5	1370.1	1589.3	1619.4
Total Deposits	**6074.4**	**5929.6**	**6359.3**	**6112.0**	**6239.3**

NB: Totals may not tally due to rounding off

Commercial banks deposits by holder

The quantity of deposits held with the local commercial banks increased by 2.1 per cent at the end of June 2013 following a 3.9 per cent decrease registered in at the end of March 2013. The increase in deposits was driven by a 12.3 per cent increase in transferable deposits moderated by a 5.2 per cent reduction in other deposits included in broad money. The increase in transferable deposits was mainly driven by an increase in private sector deposits (business and household deposits). Business enterprises deposits increased by 16 per cent and household deposits increased by 5 per cent. The increase in deposits may generally be attributed to the increase in public servants' salaries that was effected in May.

Table 10: Commercial Banks' Liquidity
(Million Maloti: End of Period)

	2012			2013	
	Q2	Q3	Q4	Q1	Q2
Credit to Deposit Ratio	**51.1%**	**57.9%**	**58.7%**	**66.9%**	**66.7%**
Private Sector Credit	3 106.3	3 431.8	3 735.9	4 091.1	4 163.8
Total Deposits	6 074.4	5 929.6	6 359.3	6 112.0	6 239.3
Liquidity Ratio	**77%**	**75%**	**70.8%**	**82.6%**	**79.9%**
Notes and Coins	191.3	188.1	342.9	250.5	201.2
Balances Due from Banks in Lesotho	753.6	990.6	931.3	1 428.4	1 497.4
Balances Due from Banks in SA	2 884.0	2 421.4	2 397.3	2 528.2	2 307.8
Surplus funds	(4.9)	(41.3)	(5.7)	23.5	189.5
Government Securities	864.0	877.0	839.1	815.9	791.5
Total	**4 688.2**	**4 435.8**	**4 504.9**	**5 046.4**	**4 987.3**

Liquidity of Commercial Banks

The liquidity of commercial banks declined to 79.9 per cent in the second quarter of 2013 from 82.6 per cent recorded in the first quarter of 2013. The ratio of liquid assets to deposit liabilities and placements with other banks was 2.6 percentage points lower due to the reductions in liquid assets and an increase in deposit liabilities of the banking industry. The credit deposit ratio also declined albeit marginally. It declined from 66.9 per cent recorded in the previous quarter to 66.7 per cent in the review period. This slight decline in credit to deposit ratio was as a result of an increase in deposits which outweighed the increase in credit.

Demand for Money

Domestic Claims

Domestic credit, excluding net claims on government, expanded by 1.6 per cent during the quarter under review following a 9.5 per cent expansion realised during the first quarter of 2013. On an annual basis, domestic credit continued to register a double digit growth of 33.5 per cent following an expansion of 41.9 per cent recorded in the previous quarter. The deceleration in domestic claims is as a result of a slowdown in new acquired loans worsened by repayments toward existing loans in the quarter ending June compared with the quarter ending in March. Domestic credit is largely held by the private sector while other institutional sectors hold negligible amounts of credit.

Table 11: **Domestic Credit Excluding Net Claims on Government***

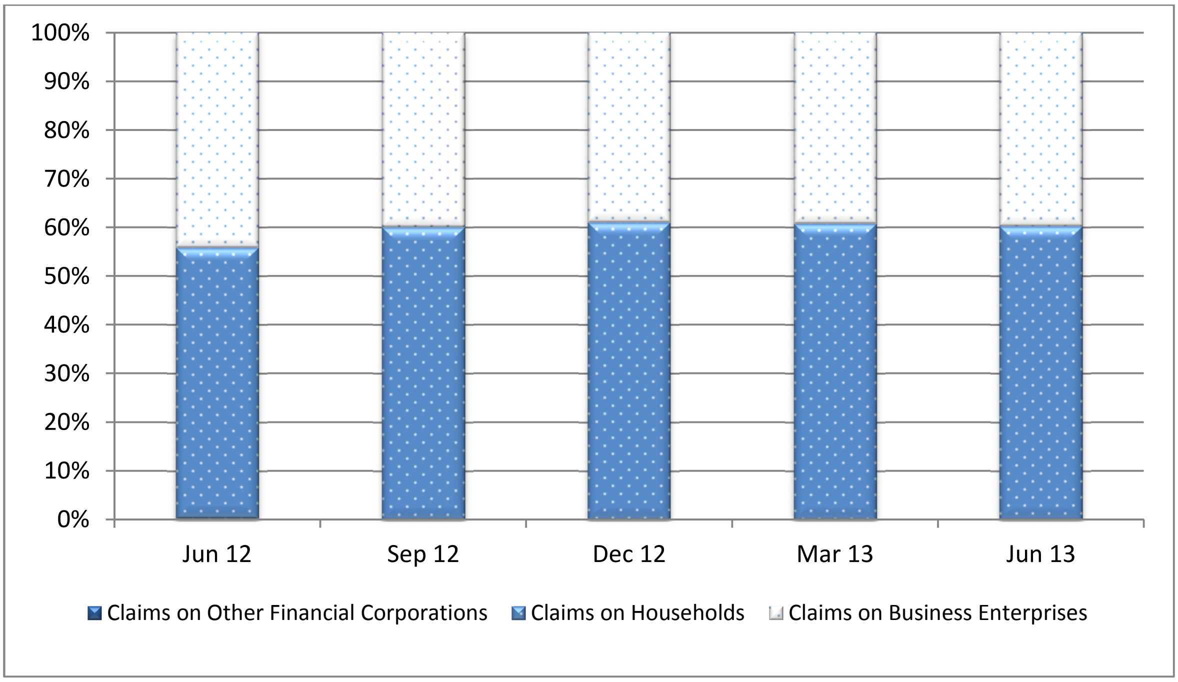
(Million Maloti: End of Period)

	2012			2013	
	Q2	**Q3**	**Q4**	**Q1**	**Q2**
Claims on Other Sectors	**3156.8**	**3484.3**	**3788.6**	**4147.8**	**4224.4**
Claims on Other Financial Corporations	11.0	11.3	10.6	11.7	11.6
Claims on State and Local Government	0.0	0.0	0.0	0.0	0.0
Claims on Private Sector	**3143.4**	**3473.0**	**3778.2**	**4136.1**	**4212.8**
Claims on Business Enterprises	1391.0	1385.7	1470.8	1619.4	1671.3
Claims on Households	1752.4	2087.3	2307.3	2516.7	2541.4

*includes non-performing loans

Figure 14: **Distribution of Credit by Holder**

(Percentage shares)



Credit to Private Sector

During the second quarter of 2013, credit extended to the private sector increased by 1.6 per cent, following a 9.5 per cent increase in the previous quarter. The increase in private sector credit on a quarterly basis was driven by a rise of 0.5 per cent and 3.2 per cent in credit extended to households and business enterprises respectively as compared to a 9.1 per cent and 10.1 per cent increase in the previous quarter.

Sectoral Distribution of Credit to Enterprises

During the second quarter of 2013, the mining sector had the highest increase in credit allocation followed by manufacturing, construction and real estate sectors. Growth in credit to mining is in line with the recovery in diamond mining output as reported under the real sector. As for manufacturing, the growth in credit mirrors better performance in the sector. As a result of increased activity in the textiles manufacturing, several firms resorted to acquiring bank overdrafts in order to finance their working capital. This facility is denominated in dollars therefore credit was further inflated by depreciation of the loti. Credit growth allocated to the construction sector was in line with the preparatory work for the commencement of the Metolong dam wall construction and the recent surge in construction of houses and business complexes.

Table 12: Sectoral Distribution of Credit to Enterprises*

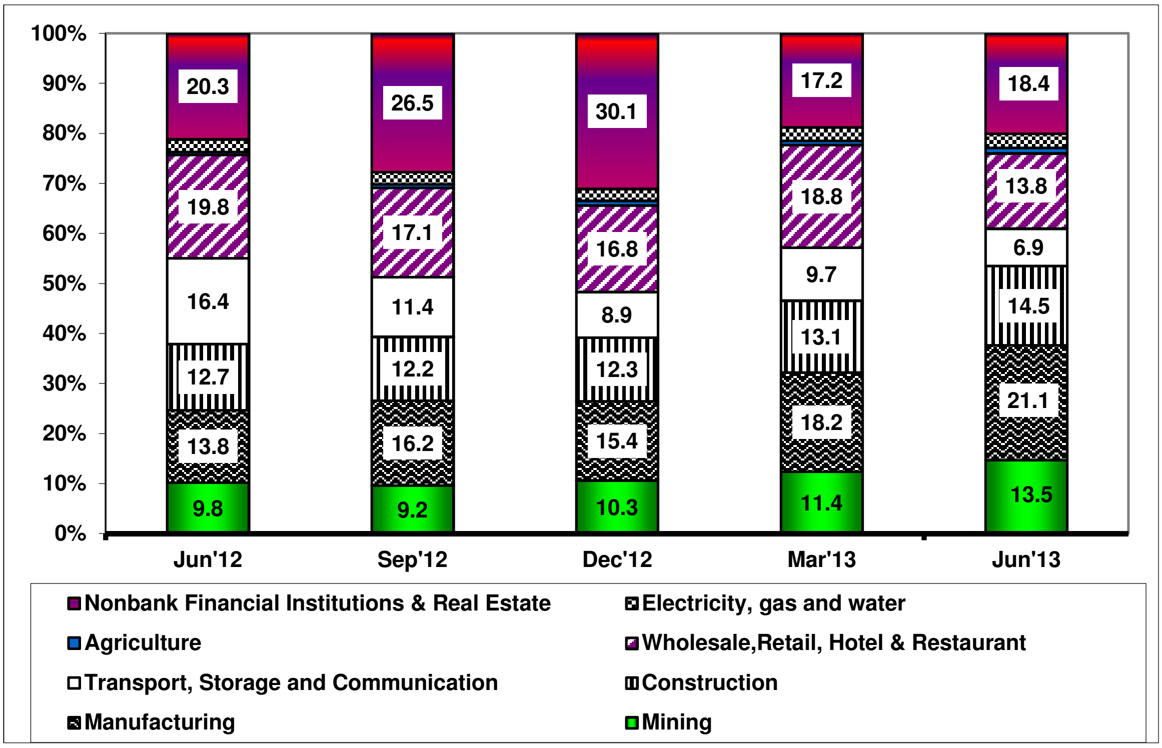
(Million Maloti: End of period)

Sector	**2012**			**2013**	
	Q2	**Q3**	**Q4**	**Q1**	**Q2**
Agriculture	9.0	12.3	11.3	16.5	18.1
Mining	136.8	128.0	152.0	184.3	226.0
Manufacturing	192.9	224.8	226.0	294.1	352.8
Construction	176.5	169.1	181.4	212.8	243.1
Transport, storage and communication	228.5	158.3	130.2	157.2	114.6
Electricity, gas and water	33.5	32.4	33.9	39.9	43.1
Wholesale, retail, hotel and restaurant	275.7	236.6	246.9	304.3	230.9
Real estate and business services	282.5	367.7	443.3	278.6	308.1
Community, social and personal services	58.0	56.4	45.7	131.8	134.6
All sectors	**1393.5**	**1385.7**	**1470.7**	**1619.5**	**1671.3**

* includes non-performing loans

Figure 15: Commercial Bank's Credit to Business Enterprises

(Percentage shares)



Net Claims on Government

The net claims on government by the banking system decreased by 9.6 per cent during the second quarter of 2013, following a decrease of 8.7 per cent observed in the previous quarter. This decrease in total net claims by the banking sector was mainly driven by a 7.2 per cent decrease in net claims on Government by the Central Bank and a 3.0 per cent decrease in net claims on Government by the commercial banks. The decrease in net claims on government by Central Bank is as a result of an increase in liabilities to central government due to an increase in government revenue and slow implementation of government expenditure, especially capital expenditure. The decrease in net claims on government by the commercial banks is as a result of a fall in claims on central government which resulted from low issuance of treasury bills during the second quarter as compared to the first quarter.

Table 13: Banking System's Net Claims on Government

(Million Maloti: End of Period)

	2012			2013	
	Jun	**Sep**	**Dec**	**Mar**	**Jun**
Commercial Banks Net Claims	**840.6**	**875.1**	**837.1**	**814.6**	**790.4**
Claims on Central Government	864.0	877.0	839.1	815.9	791.5
Liabilities to Central Government	23.4	2.0	2.0	1.3	1.1
Central Bank Net Claims	**-2907.6**	**-3554.9**	**-3986.1**	**-4237.5**	**-4542.2**
Claims on Central Government	474.5	470.3	479.8	513.5	644.6
Liabilities to Central Government	3382.2	4025.2	4465.8	4751.0	5186.8
Total Net Claims Government	**-2067.0**	**-2679.8**	**-3148.9**	**-3422.9**	**-3751.8**

IMF loans on-lent to the GOL.

Net Foreign Assets

The net foreign assets of the entire banking system increased by 7.7 per cent in the second quarter of 2013 following a decrease of 0.4 per cent recorded in March, 2013. The increase in total net foreign assets was on account of an 11.0 per cent increase in net foreign assets of the Central Bank. This was due to an increase in investments as a result of a revaluation gain. The accumulation of foreign assets was also caused by the fiscal surplus and is in line with the overall balance surplus in the balance of payments.

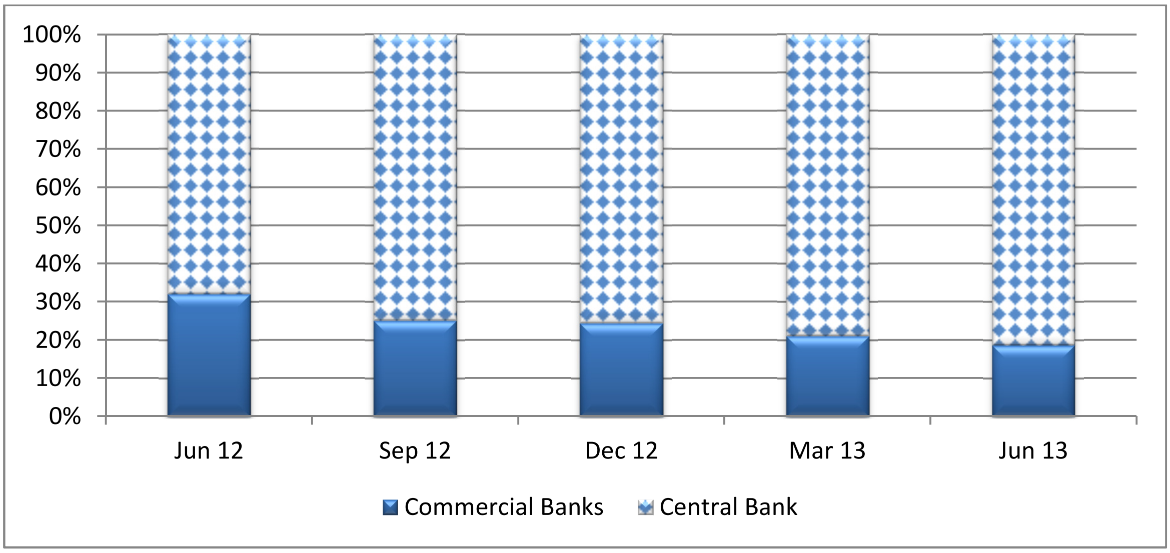
Table 14: Banking System's Claims and Liabilities on Non-residents

(Million Maloti: End of Period)

	2012			2013	
	Jun	**Sep**	**Dec**	**Mar**	**Jun**
A. Commercial Banks	**2803.1**	**2357.9**	**2486.7**	**2137.9**	**2030.9**
Claims on Non-residents	2984.2	2540.8	2569.5	2669.1	2411.0
Liabilities to Non-residents	-181.2	-182.9	-82.8	-531.2	-380.1
B. Central Bank	**5924.2**	**7016.1**	**7654.2**	**7959.1**	**8846.9**
Claims on Non-residents	6808.0	7907.5	8563.6	8926.2	9903.9
Liabilities to Non-residents	-883.8	-891.4	-909.3	-967.1	-1057.0
Net Foreign Assets Total	**8727.2**	**9374.0**	**10140.9**	**10097.0**	**10877.8**

Figure 16: Net Foreign Assets

(Percentage shares)



Money Market Developments

Total holding of Treasury bills and bonds decreased by 0.4 per cent during the quarter under review as compared to an 1.6 per cent increase in the previous quarter. The decline was mainly as a result of 0.9 per cent fall in holding of treasury bills as compared to a 2.2 per cent increase in the last quarter. This is because there was a return to the normal trend of issuance of treasury bills after the conclusion of the Extended Credit Facility (ECF) program.

Table 15: Holding of Treasury Bills and Bonds

(Face Value; Million Maloti)

	2012			2013	
	Jun	**Sep**	**Dec**	**Mar**	**Jun**
Total Holding of Bills and Bonds	**1159.2**	**1167.2**	**1171.5**	**1136.3**	**1160.3**
Treasury Bills	**592.9**	**571.4**	**559.5**	**571.7**	**541.5**
Banking System	472.7	467.8	455.4	445.7	424.4
Non-Bank Sector	120.2	103.6	104.1	126.0	117.1
Treasury Bonds	**566.4**	**595.8**	**611.9**	**564.6**	**618.8**
Banking System	375.0	376.1	401.2	405.0	405.2
Non-Bank Sector	191.3	219.7	210.7	159.6	213.6
Memorandum Item					
Average Yield Bills (per cent)	5.59	5.56	5.45	5.54	5.54
Average Yield Bonds (per cent)*	8.90	8.90	8.60	9.60	9.60

* Average of a five year bond

Money Market and Short-term Interest Rates

During the second quarter of 2013, all the Central Bank's interest rates declined while all commercial banks' interest rates remained unchanged. The 91-day Treasury bill and Lombard rates declined to 5.27 and 9.27 per cent respectively. The 3 basis point decline in the 91 day Treasury bill rate was as a result of the decline in issuance of Treasury bill thus causing bidders to bid at the highest prices so as to be successful. On the South African side however, all the rates remained constant except the 91 day T-bill rate which increased. The reason is that during that period there was under subscription and under-allotment due to rates that were perceived not to be in line with market rates by the National Treasury.

Table 16: Major Money Market Interest Rates

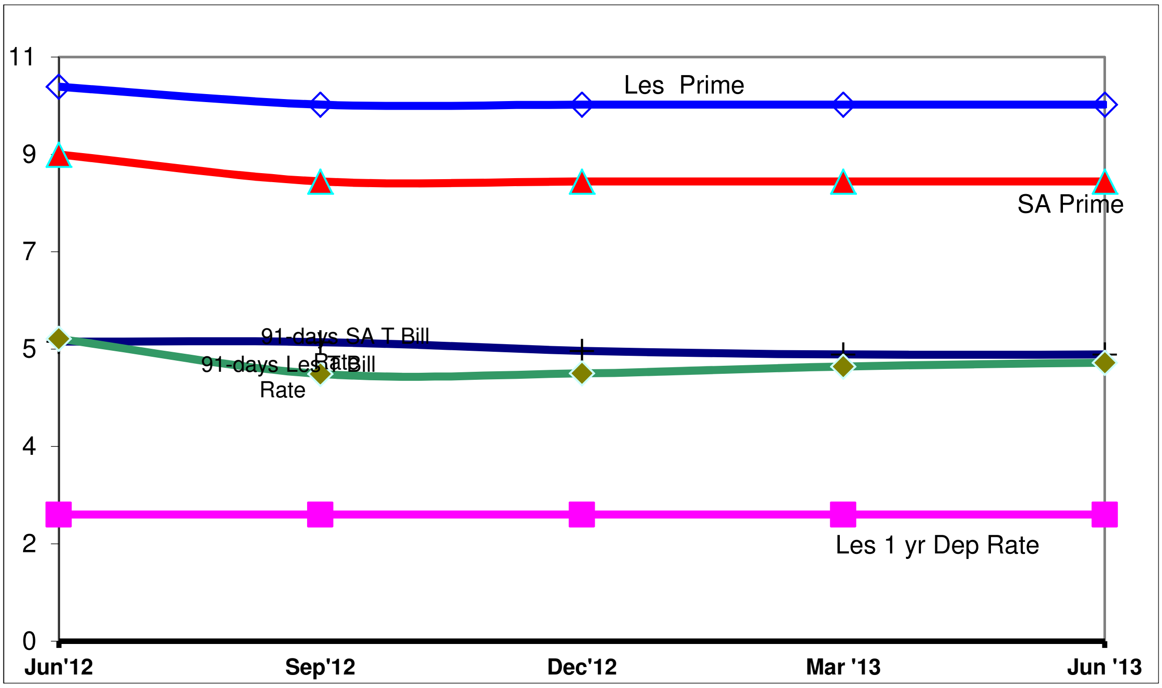
	2012			2013	
	Jun	Sep	Dec	Mar	Jun
Central Bank					
T Bill Rate – 91 Days	5.59	5.43	5.37	5.30	5.27
Lombard Rate	9.54	9.43	9.37	9.30	9.27
Commercial Banks[5]					
Call	0.77	0.77	0.77	0.77	0.77
Time:					
31 days	0.91	0.91	0.91	0.91	0.91
88 days	1.41	1.41	1.41	1.41	1.41
6 months	1.69	1.69	1.69	1.69	1.69
1 year	2.34	2.34	2.34	2.34	2.34
Savings	0.84	0.84	0.84	0.84	0.84
Prime	10.25	9.92	9.92	9.92	9.92
South Africa*					
Repo	5.50	5.00	5.00	5.00	5.00
T Bill Rate – 91 Days	5.59	4.90	4.95	5.08	5.15
Marginal Lending					
Rate	10.50	10.50	10.5	10.50	10.50
Prime	9.00	8.50	8.5	8.5	8.5

* Figures for South Africa were obtained from the SARB

[5] Average rates by commercial banks

Figure 17: **Short-Term Interest Rates**

(Per cent Per Annum)



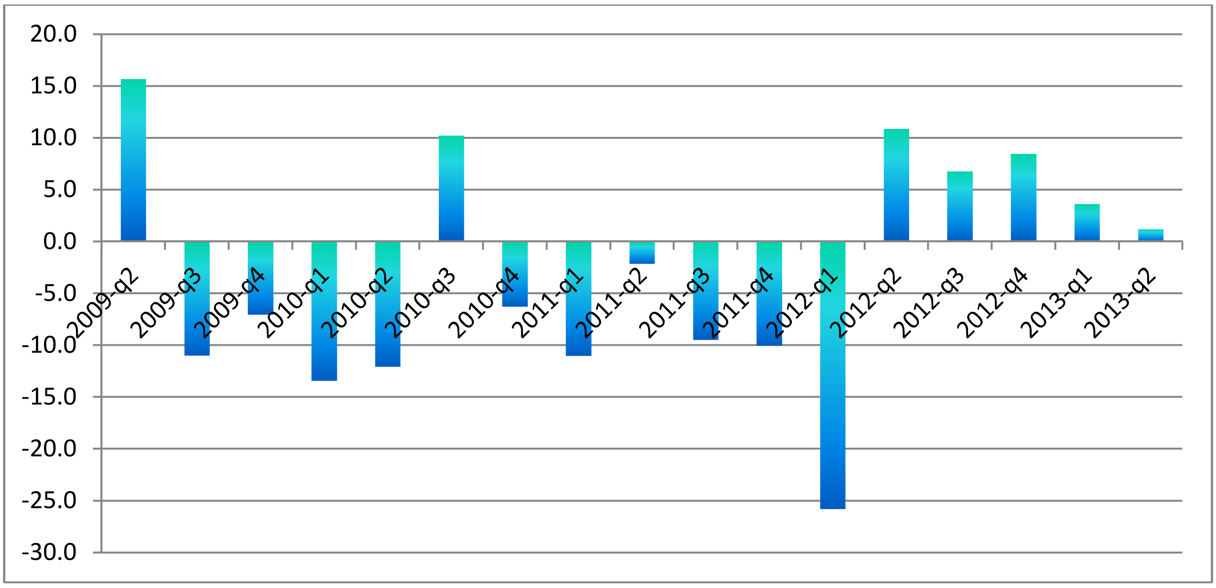
V. Government Finance

Overview

For the quarter ending in June, 2013 government budgetary operations estimates indicated a surplus equivalent to 1.2 per cent of GDP. This surplus, though lower than the surplus of 3.6 per cent of GDP recorded in the previous quarter, comes as a result of revenue being higher than expenditure, despite an increase in both. On a quarterly basis, total revenue increased by 8.7 per cent following a fall of 2.1 per cent in the previous quarter, and total expenditure further rose by 26.8 per cent in contrast to an increase of 0.1 in the previous quarter.

Figure 18: Overall Balance

(In per cent of GDP)



Source: Ministry of Finance (MoF)

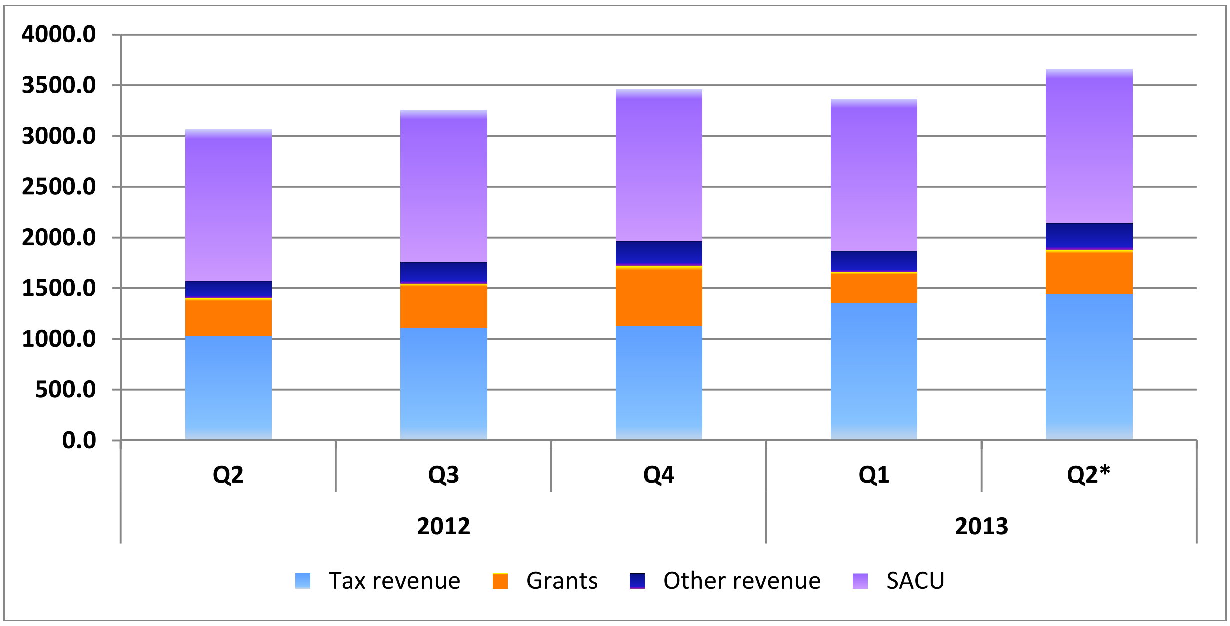
Revenue

The observed growth in total revenue[4] resulted from an increase in all its major components. Tax revenue increased by 6.7 per cent, a rate lower than the 20.2 per cent recorded in the previous quarter. The deceleration is attributed to the decline in income tax and VAT, which have been affected mostly by the slowdown in the retail and wholesale sector. Preliminary estimates indicate that grants recovered from a fall of 49.2 per cent in the previous quarter to 42.6 per cent growth during the quarter under review. Other revenue[5] grew by 24.7 per cent in comparison to the previous quarter, where it fell by 11.5 per cent. The growth in other revenue reflects amongst others the rise of 16.4 per cent in water royalties' receipts during the quarter ending in June, 2013. SACU revenue on the other hand increased marginally by 1.5 per cent during the review period.

[4] Total revenue comprises of tax revenue, grants, other revenue and SACU receipts
[5] Other revenue includes property income(interest, dividends &rent) and income from sales of goods and services

Figure 19: Government Revenue

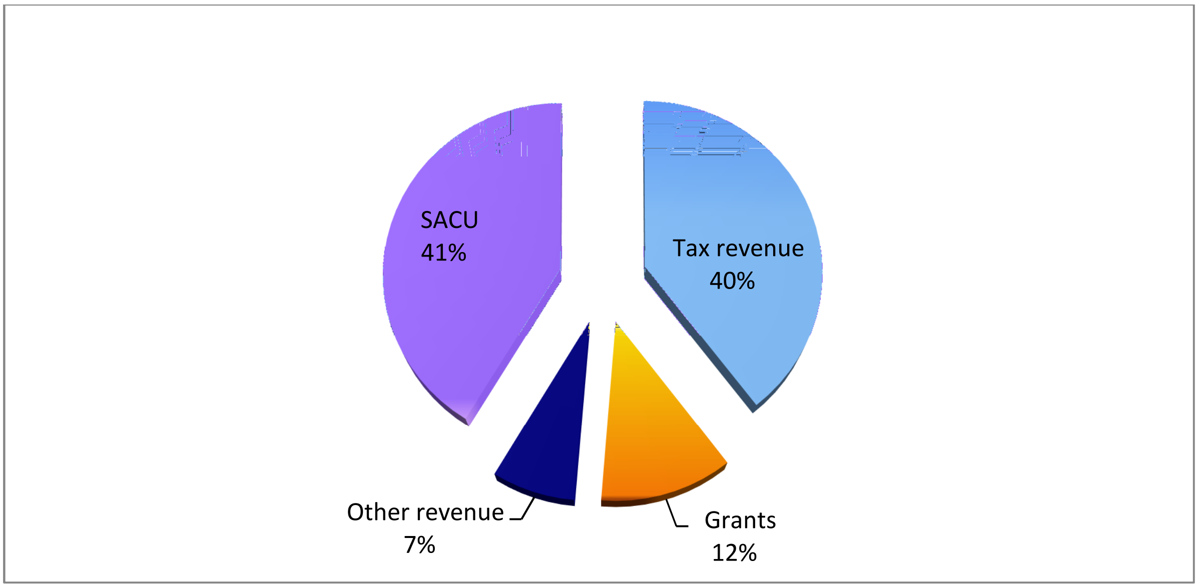
(Million Maloti)



Source: Ministry of Finance (MoF)
*Preliminary estimates

For the quarter under review, SACU revenue and tax revenue continue to be the major sources of government revenue, with contribution shares of 41 per cent and 40 per cent, respectively.

Figure 20: Sources of Government Revenue

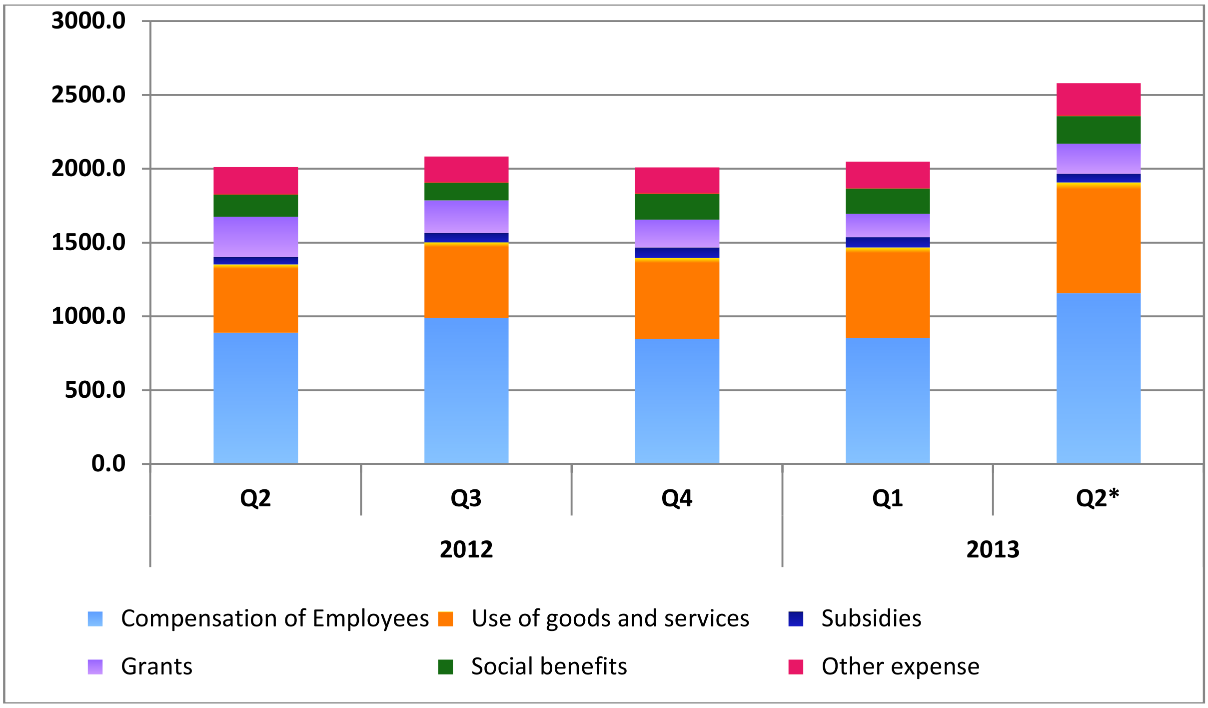


Expenses

Following a flat trajectory in past four quarters, expenses grew during the quarter under review. Amongst the components of government expenses, compensation of employees grew the most, in part reflecting the upward adjustment in civil servants wages and salaries which became effective from the beginning of the fiscal year. The number of government employees also grew, in particular that of teacher as a result of new six schools opened in January 2013. Compensation of employees increased by 35.7 per cent, in contrast to an increase of 0.5 per cent recorded in the previous quarter. Use of goods and services grew by 22.1 per cent in the quarter ending in June compared with an increase of 12.4 per cent recorded in the previous quarter.

Figure 21: **Government Expenses**

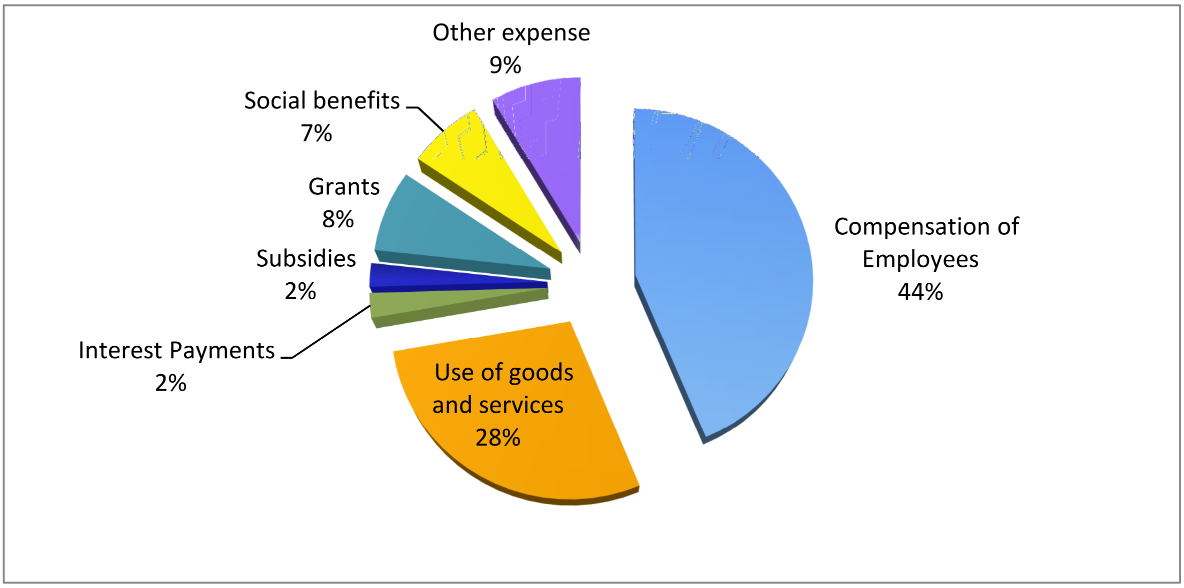
(Million Maloti)



Source: MoF

*Preliminary estimates

Figure 22: Expenses by Type



Compensation of employees and use of goods and services continued to account for the largest share of expenses at 44.0 per cent and 28.0 per cent, respectively. In the third position are subsidies and transfers, with a share of around 17.0 per cent.

Non-financial Assets

Non-financial assets are acquired using financial resources allocated through the capital estimates. Spending on acquisition of non-financial assets declined by 16.9 per cent during the quarter under review in comparison to an increase of 9.5 per cent in the previous quarter. The decrease partly reflected the winding down of some of the large on-going projects implemented in collaboration with donors such as MCA, including activities related to the Metolong dam project. Nonetheless, there are still a number of on-going capital projects which take up a large proportion of the capital budget such as Roma, Ramabanta, Semonkong, Sekake Road, in which government is the major financier.

Table 17: Summary of Government Budgetary Operations

	2012			2013	
	Q2	Q3	Q4	Q1	Q2*
Revenue	**3063.4**	**3252.9**	**3458.9**	**3365.9**	**3659.8**
Tax revenue	1026.6	1112.8	1129.9	1357.8	1448.2
o/w Income tax	*539.3*	*569.0*	*671.7*	*620.2*	*490.0*
o/w VAT	*383.9*	*387.9*	*424.2*	*444.5*	*405.7*
Grants	377.1	433.9	593.9	300.9	429.2
Recurrent	*0.0*	*0.0*	*196.4*	*0.0*	80.8
Capital	*377.2*	*433.9*	*397.5*	*300.9*	*348.4*
Other revenue	168.1	214.6	243.5	215.6	268.8
o/w water royalties	*138.8*	*159.6*	*222.7*	*114.7*	*133.5*
SACU	1491.6	1491.6	1491.6	1491.6	1513.6
Expense	**2057.1**	**2109.9**	**2072.5**	**2074.3**	**2629.3**
Compensation of Employees	889.4	990.1	848.2	852.4	1156.3
o/w wages and salaries	*749.6*	*791.3*	*760.6*	*925.0*	*1003.3*
Use of goods and services	461.1	511.5	546.9	614.8	750.8
Interest Payments	46.3	27.4	63.2	27.4	49.8
External	16.5	18.7	26.7	17.8	19.5
Domestic	29.8	8.7	36.5	9.6	30.2
Subsidies	49.9	62.1	71.5	69.5	58.5
Grants	274.8	221.7	189.7	156.7	204.4
Social benefits	148.9	119.3	172.6	171.7	185.9
Other expense	186.6	177.8	180.4	181.8	223.8
Gross operating Balance	***1006.3***	***1142.9***	***1386.4***	***1291.6***	***1030.5***
Nonfinancial assets	***465.5***	***804.7***	***1015.1***	***1111.1***	***923.6***
Deficit/surplus [Net lending(+)/borrowing(-)]	***540.8***	***338.3***	***371.3***	***180.5***	***106.9***
Financial assets and liabilities	**45.3**	**486.8**	**331.3**	**315.9**	**59.8**
Financial assets	601.4	621.6	440.6	284.5	435.6
Deposits	601.4	621.6	440.6	284.5	435.6
Liabilities	556.1	134.8	109.3	-31.4	375.8
Domestic	305.1	-10.2	27.7	52.6	114.6
Foreign	250.9	145.0	81.6	-84.0	261.2

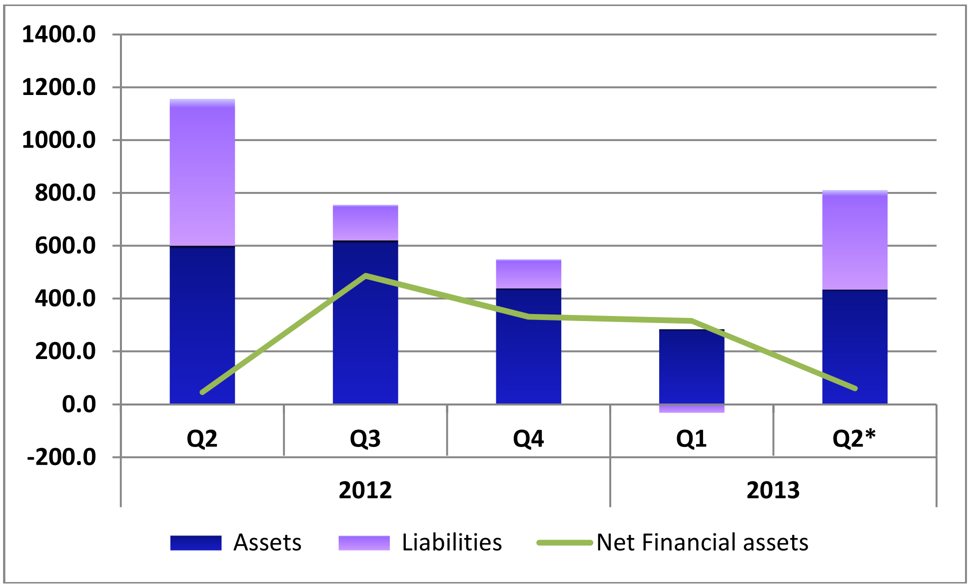
Source: CBL & MoF
*Preliminary estimates

Financial Assets and Liabilities

Government's net position in financial assets and liabilities transactions remains positive, reflecting that government was able to finance its operations without having to source extra resources from the financial sector. This position still reinforces government's efforts to build up international reserves in the medium term. Government deposits within the banking sector grew by 9.2 per cent following a rise of 6.4 per cent in the previous quarter. On the other hand, domestic liabilities declined by 2.5 per cent in contrast to an increase of 1.6 percent in the previous quarter, while preliminary estimates indicate that foreign liabilities have surged due to higher disbursements during the quarter under review than in the previous quarter. Overall government liabilities increased by 28.5 per cent during the quarter ending in June 2013 in contrast to a decline of 11.7 per cent observed in the previous quarter.

Figure 23: Government Financing

(Flows in million Maloti)



Source: CBL
*Preliminary estimates

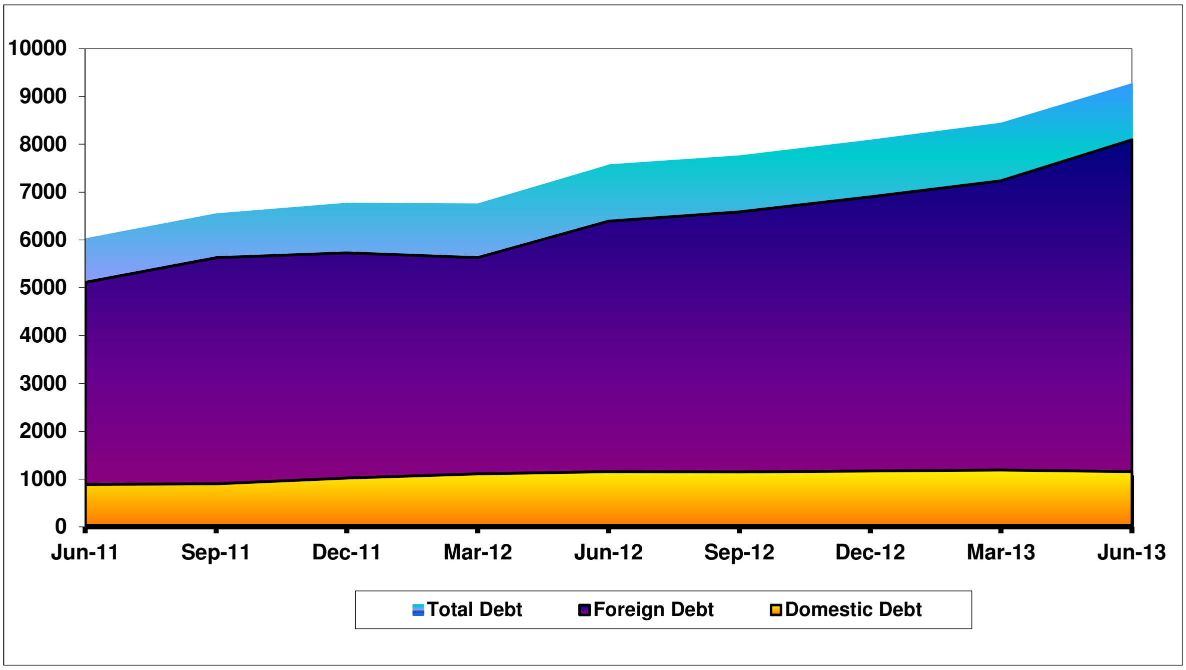
Public Debt

Outstanding government debt[6] increased by 9.8 per cent in the quarter under review compared with 4.4 per cent increase recorded in the previous quarter. The increase in total public debt was due to an increase in external debt. External debt rose by 11.8 per cent while domestic debt declined by 2.5 per cent. As a percentage of GDP, public debt stood at 46.5 per cent compared with 42.4 per cent recorded in the previous quarter. External debt continued to be the largest component of the overall debt stock at 87.6 per cent while domestic debt constituted 12.4 per cent of total public debt stock.

[6] Government debt stock is made up of both external and domestic borrowing.

Figure 24: **Outstanding Public Debt**

(Million Maloti: End of Period)



Source: MoF

External debt

External debt increased by 11.8 per cent on a quarterly basis, compared with an increase of 4.9 per cent recorded in the quarter ending in March, 2013. The increase was caused mainly by the depreciation of the Loti against the US dollar. Loans from multilateral sources continued to constitute a larger share of external borrowing at 88.5 per cent while bilateral loans constituted 5.0 per cent. As a percentage of GDP, external debt was 40.7 per cent during the review period, which was higher than 36.4 per cent recorded in the previous quarter.

Table 18: External Debt

(Million Maloti)

	2012			2013	
	Q2	Q3	Q4	Q1	Q2*
External Debt	**6397.7**	**6591.7**	**6901.4**	**7240.9**	**9257.3**
Bilateral Loans	260.6	312.5	340.6	367.4	403.6
Concessional	260.6	312.5	281.7	303.9	335.0
Non-concessional	0.0	0.0	58.9	63.5	68.6
Multilateral Loans	5739.2	5863.3	6119.5	6387.9	7167.3
Concessional	5442.5	5412	5643.5	5891	6079.5
Non-concessional	296.7	451.3	476	496.9	215.8
Financial Institutions	63.5	62.0	62.0	59.8	60.7
Concessional	0.0	0.0	0.0	0.0	0.0
Non-concessional	63.5	62.0	62.0	59.8	60.7
Suppliers' Credit	334.4	353.9	379.3	425.8	465.4

Source: MoF
* Preliminary estimates

Domestic Debt

Domestic debt stock comprises Treasury bills and bonds. It decreased by 2.5 per cent during quarter ending in June, in comparison with an increase of 1.6 per cent recorded in the previous quarter. The decline resulted mainly from the reduction in the volume of Treasury bills and bonds auctioned during the review period as compared to the previous quarter, where more stock was auctioned as a precaution to avoid falling below the NIR target floor. Commercial banks hold the largest share of Treasury bills and bonds at 71.5 per cent, while the non-bank sector holds 28.5 per cent. As a percentage of GDP, domestic debt was 5.8 per cent on a quarter-to-quarter basis compared with a 6.0 per cent observed in the previous quarter.

Table 19: Domestic Debt

(Million Maloti)

	2012			2013	
	Q2	Q3	Q4	Q1	Q2*
Total Domestic Debt	**1159.2**	**1153.3**	**1171.5**	**1190.3**	**1160.3**
Banks	847.7	843.9	960.7	850.7	829.6
Long-term	375	376.1	401.2	405.0	405.2
Short-term	472.7	467.8	559.5	445.7	424.4
o/w treasury bills	472.7	467.8	559.5	445.7	424.4
Non –bank	311.5	309.3	314.8	339.6	330.7
Short-term (TBs)	120.2	103.6	104.1	126.0	117.1
Long-term	191.3	205.7	210.7	213.6	213.6

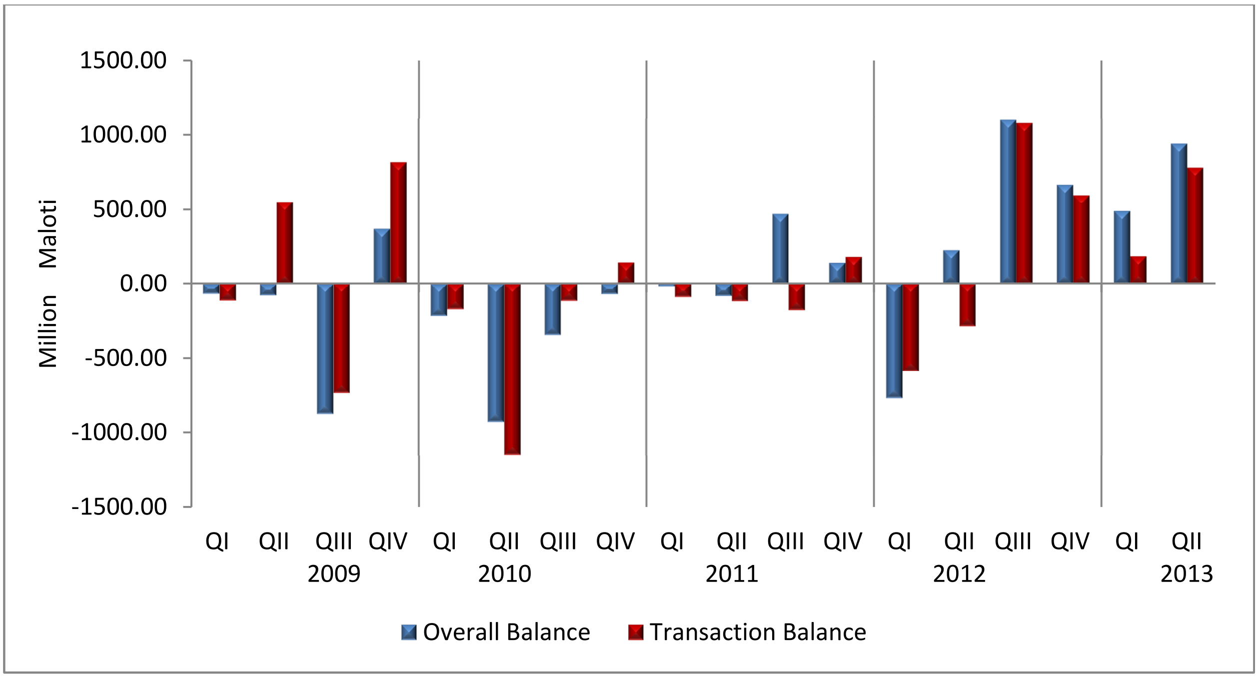
Source: MoF
* Preliminary estimates

V. Foreign Trade and Payments

Overview

The external sector position continued to register a surplus in the second quarter of 2013, as a result of the narrowing of the current account deficit, increased capital and financial account inflows together with revaluation gains from major trading currencies in which foreign reserves assets were held. The overall balance, in seasonally adjusted terms improved to a surplus equivalent to 18.8 per cent of GDP, in the review quarter, compared to a 9.7 per cent of GDP surplus realised in the previous quarter. Transaction balance, registered a higher surplus of 15.9 per cent of GDP in the quarter ending in June 2013, relative to that of 3.5 per cent of GDP in the quarter ending in March 2013.

Figure 25: Balance of Payments



Current Account

A lower current account deficit of M645.8million was recorded during the second quarter of 2013, compared with that of M981.5 million in the previous quarter. The narrowing of the deficit resulted largely from narrowing of trade account deficit on the back of a decline in both merchandise exports and imports as well as a drop in payments for services acquired abroad. The decline in merchandise exports resulted mainly from a drop in diamond exports together with decreased textiles and clothing exports during the quarter. Moreover merchandise imports fell due to the reduction in imports from the non-common customs area. The trade deficit narrowed down to M3.0 billion in the review quarter, from M3.4 billion in the previous quarter. In addition, a marginal increase in the income account balance contributed to the observed narrowing of the current account deficit during the review period. However, the fall in current transfers' receivables dampened the improvement in the current account balance during the period. As a share of GDP, current account balance registered a deficit of 13.0 per cent in the second quarter, compared with a deficit of 19.7 per cent in the previous quarter.

Table 20: Current Account Balance

(Million Maloti)

	2012			2013	
	QII	QIII	QIV	QI*	QII+
I. Current Account	-1474.23	-451.16	-668.99	-981.50	-645.77
(a) Goods	-2992.63	-2061.52	-2280.21	-2668.94	-2268.22
Merchandise exports f.o.b.	2114.96	2232.72	2075.89	1970.39	1551.57
Of which diamonds	747.35	658.85	532.66	565.84	393.30
Of which textiles and clothing	868.04	958.18	953.75	820.63	801.10
Other exports	334.08	441.49	405.21	583.92	357.17
Merchandise imports f.o.b.	-5107.59	-4294.24	-4356.10	-4639.33	-3819.79
(b) Services	-806.35	-769.92	-803.59	-787.98	-776.11
(c) Income	411.23	432.58	411.89	435.62	435.85
(d) Current Transfers	1913.35	1947.52	2002.74	2039.80	1962.71

* Revised estimates
\+ Preliminary estimates

Merchandise Exports

Merchandise exports' earnings deteriorated for the second consecutive quarter in 2013, despite the weakness of the local currency against the major trading currencies during the period. It declined by 21.2 per cent during the quarter ending in June 2013, relative to a fall of 5.1 per cent recorded in the first quarter of 2013. The drop in exports was underpinned by a 30.5 per cent decrease in diamond exports in the second quarter of 2013, compared with a rise of 6.2 per cent in the first quarter 2013. The decrease in diamond exports reflected a decline in diamond production in the previous quarter, as Letšeng diamond mine stopped its operations for preparation of the installation of a new crusher machine during that period. The fall in diamond exports was also reflected the slowdown in the global demand, due to the weakness of global economic activity, particularly in the European and Asian economies during the review quarter. In addition, there was a 2.4 per cent decline in textiles and clothing exports during the period, albeit lower than a decrease of 14.0 per cent in the previous quarter. On an annual basis, merchandise exports fell by 26.6 per cent in the second quarter of 2013. As a percentage of

GDP, merchandise exports registered 31.2 per cent compared with 39.6 per cent recorded in the quarter ending in March 2013.

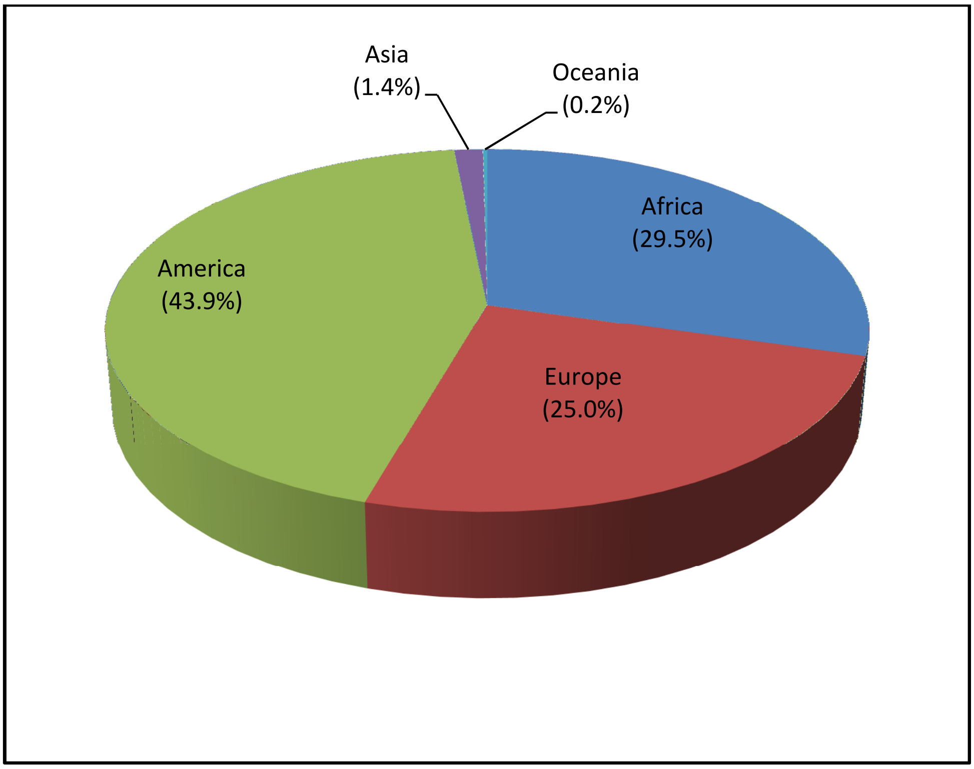
Merchandise Imports

Merchandise imports dropped by 17.6 per cent in the review quarter, compared with a revised growth of 6.5 per cent in the previous quarter. This reflected the slowdown in domestic economic activity which led to a decrease in demand for foreign goods. As a share of GDP, merchandise imports recorded 76.7 per cent in the second quarter, compared with 93.2 per cent in the previous quarter.

Direction of Trade

In the second quarter of 2013, the American market surpassed the SACU region to become the largest recipient of Lesotho's exports with a share of 43.9 per cent of total exports, compared with a share of 32.9 per cent registered in the previous quarter. The second largest recipient of Lesotho's exports was the African continent, particularly SACU region with a share of 29.5 per cent during the quarter, lower than 37.3 percentage share observed in the previous quarter. The European market, where a large proportion of diamond export is destined, was the third largest destination market for Lesotho's exports with a share of 25.0 per cent in the review period, compared with 28.9 per cent recorded in the previous quarter. The remaining Lesotho exports were destined to Asian and Oceania markets with shares of 1.4 per cent and 0.2 per cent, respectively during the review quarter.

Figure 26: Direction of Merchandise Exports (percentage share)



Services Account

During the quarter under review, the net services account recorded a deficit, as the country continued to be a net importer of services. The services deficit of M776.1 million was realised in the second quarter of 2013, following that of M788.0 million in the previous quarter. The narrowing of the deficit resulted largely from the drop in payments for freight services on imported goods during the period. However, an increase in payments for Lesotho embassies abroad moderated the decline in the deficit of services account. As a share of GDP, net services showed a deficit of 15.6 per cent in the quarter ending in June 2013, relative to a deficit of 15.8 per cent in the previous quarter.

Income Account

The net income account increased marginally by 0.1 per cent in the quarter ending in June 2013, lower than 5.7 per cent registered in the first quarter of 2013. The growth emanated largely from the drop in interest paid by government on foreign loans coupled with lower receipts by LHDA for operational cost. The net income registered an inflow equivalent to 8.8 per cent of GDP during the review quarter, compared with 8.7 per cent of GDP in the previous quarter.

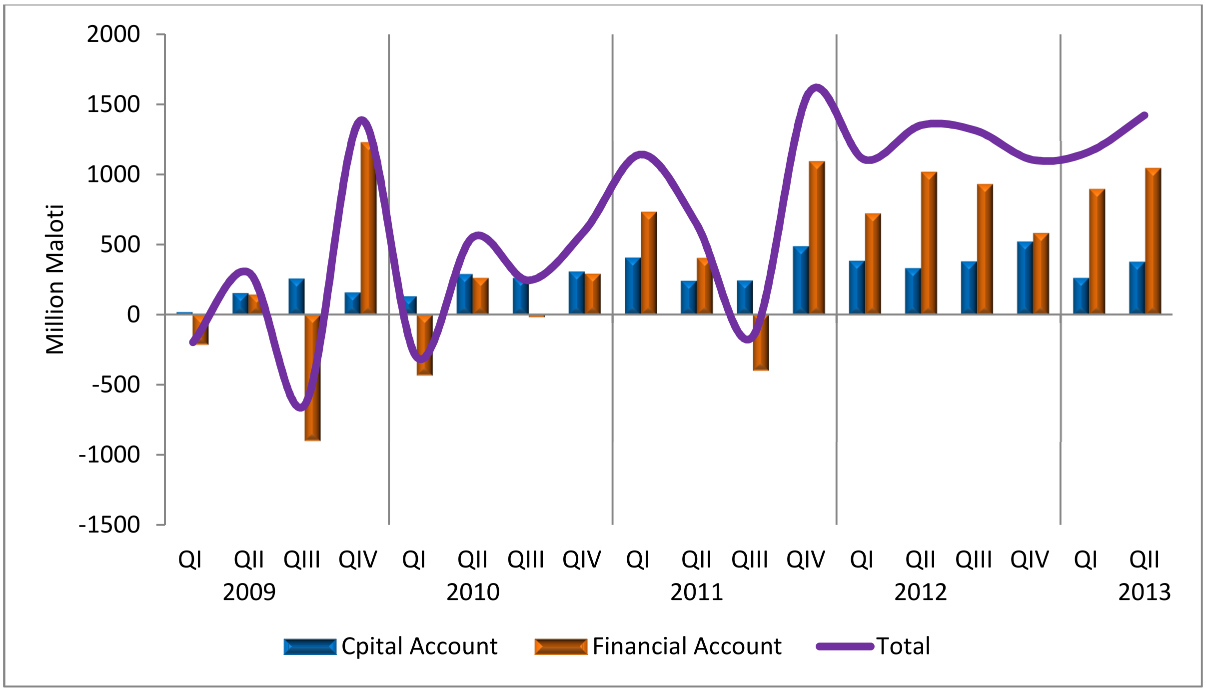
Current Transfers

In the second quarter of 2013, the current transfers' receivables declined by 3.8 per cent, in contrast with an increase of 1.8 per cent in the previous quarter. The observed movement was basically normalization after receipt of the rand compensation payment in the previous quarter, which is normally received at the beginning of the year. However, an increase of 1.5 per cent in SACU receipts which takes the largest share of the net current transfers moderated the fall in current transfers. As a percentage of GDP, the net current transfers recorded 39.4 per cent during the review quarter, lower than the 41.0 per cent in the previous quarter.

Capital and Financial Account

The net surplus in the capital and financial account balance widened to M1.4 billion in the quarter ending in June 2013, from a net surplus of M1.2 billion recorded in the quarter ending in March 2013, as both capital and financial inflows increased during the quarter. The growth of 42.6 per cent of capital inflows was realised during the quarter, in contrast with a fall of 49.3 per cent in the previous quarter, due to an increase in foreign grants received by Government. The financial account registered a net inflow of M1.0 billion during the second quarter of 2013, compared with a net inflow of M895.9 million in the previous quarter. This resulted largely from drawdown of commercial banks' foreign assets which recorded an inflow of M258.1 million during the quarter, compared with an outflow of M99.5 million to increase their foreign assets in the previous quarter. In addition, the widening of financial account inflows was due to an increase of M114.1 million in CBL foreign liabilities, from M57.7 million in the previous quarter. A rise in government foreign loan disbursements as well as decreased repayments also contributed to an increase in financial account inflows. Relative to GDP, capital and financial account surplus was 28.5 per cent during the review period, higher than the 23.3 per cent realised in the previous quarter.

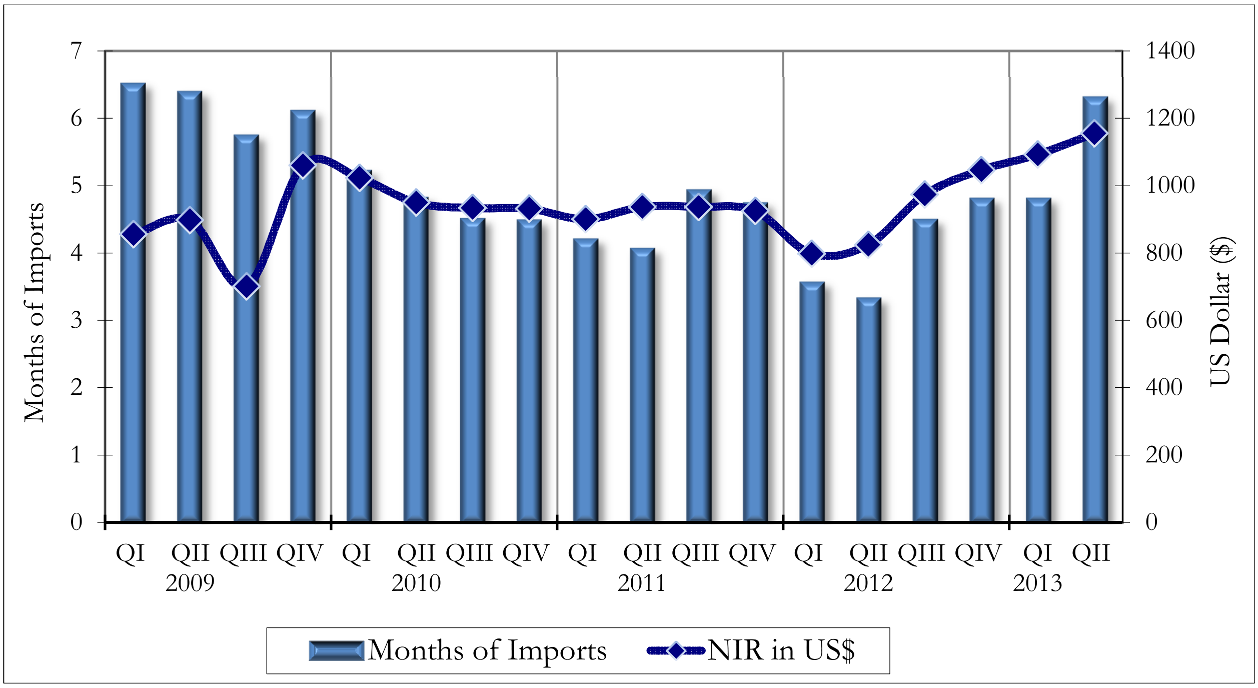
Figure 27: Capital and Financial Account



Reserve Assets

The stock of gross international reserves grew by 10.9 per cent to M9.9 billion in the quarter ending in June 2013, from M8.9 billion observed in the quarter ending in March 2013. The accumulation of foreign reserves attributed to an increase in government deposits together with gains from depreciation of local currency against the major currencies in which foreign reserves were held. Measured in months of import cover, gross official reserves rose to 6.3 months during the quarter under review, following 4.8 months recorded in the previous quarter. This reflected a rise in stock of foreign reserves coupled with a drop in payments for imported goods and services during the quarter.

Figure 28: **Reserve Assets**



Exchange Rates

The domestic currency unit, the Loti, which is fixed at par to the Rand, continued to depreciate against the major trading currencies during the quarter ending in June 2013. The weakness of the Rand/Loti was influenced by unfavourable economic factors in South Africa, as continuing labour unrest in the mining and other sectors reduced investors' confidence and negatively affected foreign capital inflows into the country. The depreciation was also underpinned by the lower international commodity prices of key SA commodity exports as well as concerns about sustainability of the financing of widening of SA current account deficit. On quarterly average the Loti/Rand depreciated by 3.2 per cent to M9.36, 4.9 per cent to M12.42 and 5.1per cent to M14.61, against the US Dollar, the Euro and Pound Sterling, respectively during the quarter.

Figure 29: Nominal Exchange Rate of the Loti against Major Currencies