CENTRAL BANK OF LESOTHO

QUARTERLY REVIEW

June 2017

MASERU

KINGDOM OF LESOTHO

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1. Executive Summary

The global economy displayed signs of recovery during the review quarter. In particular, growth was robust in advanced economies on account of stronger domestic demand, buoyant consumer spending as well as business investment. However, UK was an exception as it registered a drastic slowdown in output growth following a fall in production. Conversely, growth in emerging market economies picked-up during the second quarter of 2017. This was against a backdrop of firmer exports coupled with increased output by the extractive sector. The South African economy emerged from the technical recession and grew by 2.5 per cent supported by higher activity in agriculture, forestry and fishing. Monetary policy remained largely accommodative in most economies with the exception of the US which increased its federal market funds rate.

Compared to the significant contraction in the previous quarter, the domestic economic activity declined marginally during the quarter under review. The relatively small contraction was as a result of good performance by the primary sector given that the tertiary and the secondary sectors remained largely subdued. The labour market displayed mixed signals as employment by LNDC-assisted companies recorded positive growth while government employment as well as the Basotho migrant mineworkers declined during the review period. Owing to the high food inflation, domestic prices remained elevated during the review quarter.

Money supply registered a moderate increase during the review period relative to a much higher increase observed during the previous quarter. This development was attributed to a decline in both the net foreign assets and domestic claims. The fall in domestic claims was at the back of a fall in claims on other sectors while the fall in overall net foreign assets was ascribed to a decline in commercial banks deposits with non-residents.

The government budget operations recorded a narrower deficit during the quarter ending June 2017. The review quarter is also the first quarter of the fiscal calendar normally characterised by lower budget execution. The stock of public debt increased slightly compared to the previous quarter owing to the depreciation of Loti against major currencies in which foreign debt is denominated.

Lesotho's external sector position improved slighlty during the second quarter of 2017 compared to the previous quarter. This was due to the narrowing of the current account deficit coupled with the decline of the deficit in the financial account. The improvement in the current account emanated from improvements in both primary and secondary income accounts. Similarly, lower reduction in the official reserves and bank's foreign assets supported the recovery of the financial account balance. Consequently, the overall balance registered a deficit equivalent to 2.6 per cent of GDP during the review period compared to a deficit equivalent to 3.4 per cent recorded during the previous quarter.

2. International Economic Developments

During the second quarter of 2017, growth was robust in advanced economies except in the UK, where growth slowed markedly due to a fall in production. Growth in the Euro Area and Japan was boosted by stronger domestic demand, while growth in the US was kept buoyant by robust consumer spending and business investment. With regards to emerging market economies, growth picked up during the quarter, except in India, where growth unexpectedly slowed as a result of slower consumer spending and exports. The Chinese economy remained upbeat during the quarter, mainly supported by production and exports of steel. The South African economy emerged from a recession during the same quarter, growing by 2.5 per cent as a result of higher economic activity in Agriculture, Forestry and Fishing. Labour market conditions were favourable in most economies with unemployment rates either declining or remaining unchanged. In South Africa, the unemployment rate remained at 27.7 per cent, as the economy continued to grapple with lack of fixed investment spending and the sustained low business confidence.

Monetary policies remained accommodative in most economies with the exception of the US. The US continued hiking the policy rate in view of the strengthening economic activity and labour market conditions. Consumer prices eased in most economies, particularly in the US and the Euro Area, influenced by declines of prices in consumer goods across various sectors. In the UK, the level of inflation rose on account of higher costs of air fares, clothing and electricity while in China, inflation increased as a result of a rise in non-food items.

Commodity prices followed different trajectories during the quarter under review, with gold and wheat prices gaining momentum while the prices for platinum, oil and maize declined. Gold prices were supported by higher demand for the safe haven asset, as uncertainty in the global financial markets intensified, triggered by amongst others, the on-going political tension between North Korea and the US, whilst wheat prices were negatively impacted by the poor quality of wheat harvested. The platinum prices declined due to lower demand for diesel vehicles, which use platinum as an auto catalyst to reduce pollution emitted from the exhaust gas. Oil prices remained weak due to the supply glut in the US, which has continued to undermine OPEC's efforts to cut oil production. Maize prices fell on account of increased supply, which was supported by favourable weather conditions.

Table 1: Key World Economic Indicators

	Real GDP Growth		Inflation Rate		Key Interest Rate		Unemployment Rate	
	March 2017	June 2017	March 2016	June 2017	March 2016	June 2017	March 2017	June 2017
United States	1.2*	3.0	2.4	1.6	1.00	1.25	4.5	4.4
Euro Area	1.9*	2.1	1.5	1.3	0.00	0.00	9.2*	9.1
Japan	1.0	2.0	0.4*	0.4	-0.10	-0.10	2.8	2.8
United Kingdom	2.0*	1.7	2.3	2.6	0.25	0.25	4.6*	4.4
China	6.9	6.9	0.9	1.5	4.35	4.35	4.0	4.0
India	6.1	5.7	3.8	1.5	6.25	6.25	**n/a**	**n/a**
South Africa	-0.6*	2.5	6.1	5.1	7.00	7.00	27.7	27.7

Updated*
Source: Bloomberg, STATSSA and SARB, OECD National Accounts Statistics (database), US Bureau of Economic Analysis, National Bureau of Statistics China, Statistics Bureau of Japan, Government of India Department of Labour, United Kingdom Office for National Statistics

ADVANCED ECONOMIES

United States (US)

During the second quarter of 2017, US GDP grew by 3.0 per cent compared with a revised growth of 1.2 per cent in the quarter ending in March 2017. Growth in the US was supported by strong consumer spending and business investment during the quarter. The US unemployment rate dropped to 4.4 per cent from 4.5 per cent in the previous quarter due to improving employment opportunities in the services and mining sectors.

Inflation in the US eased to a rate of 1.6 per cent during the quarter under review, down from 2.4 per cent in the previous quarter as a result of lower fuel prices. During its meeting in June 2017, the FOMC decided to increase its policy rate by 25 basis points from a band of 0.75 – 1.00 per cent to a band of 1.00 – 1.25. The decision to raise the policy rate was in view of the strengthening labour market conditions and economic activity. In addition the committee expected the inflation rate increase and stabilise at 2 per cent, given the stable employment levels.

Euro Area

According to the advance release of the Euro Area real GDP, growth was estimated at 2.1 per cent in the second quarter of 2017, higher than 1.9 per cent registered in the previous quarter. Growth in the Euro Area was boosted mainly by high domestic demand during the quarter. This was the fastest growth since 2011, indicating a positive response to the European Central Bank's efforts to boost economic activity, which included extremely low interest rates. The unemployment rate in the Euro area fell slightly to 9.1 per cent in the quarter ending in June 2017 from 9.2 per cent in the previous quarter. Employment amongst the youth, which previously contributed the biggest share towards unemployment, rose during the quarter and therefore supported a reduction in the overall unemployment rate.

Consumer price inflation in the Euro Area dropped to 1.3 per cent in the quarter under review, from 1.5 per cent in the quarter ending in March 2017. The fall in the inflation rate resulted from declining prices of telecommunications, social protection and bread & cereal. The Governing Council of the European Central Bank decided to leave its policy rate at 0 per cent and to continue with the bond buying programme, capped at €60 billion per month, in the quarter under review. In light of the slow pace of growth in consumer prices, the ECB indicated that it would continue with the quantitative easing programme until inflation picks up to its target rate of 2 per cent.

Japan

Japan's real GDP grew by 2.0 per cent during the quarter ending in June 2017, following a 1.0 per cent growth in the previous quarter. Growth was mainly boosted by improved domestic demand, particularly, a recovery in business fixed investment and a resilience in private consumption. The unemployment rate remained unchanged at 2.8 per cent between the first and the second quarter of 2017. Higher employment figures were recorded in construction, information and technology, wholesale and retail, while the nursing and health care sectors reported declines, thus offsetting the observed increases.

The inflation rate in Japan remained steady at 0.4 per cent, from the previous quarter, reflecting a rise in core consumer prices, particularly energy prices. The Japanese's economy relies heavily on imported fuel, which was negatively affected by the weakening Japanese Yen during the review quarter. Prices for food remained unchanged from the previous quarter, while prices for transport and housing fell. During the same quarter, the Bank of Japan left its policy rate unchanged at -0.1 per cent from the previous quarter in a bid to support expansion in economic activity. The Bank of Japan also decided to continue with its asset purchasing programme. This highly accommodative monetary policy stance is expected to continue to support demand through higher spending by both the corporate and the household sector.

United Kingdom (UK)

The real GDP growth rate in the UK was estimated to fall from 2.0 per cent in the quarter ending in March 2017 to 1.7 per cent in the quarter ending in June 2017. Growth in the UK slowed due to a fall in production as concerns over Brexit heightened during the quarter under review. The observed growth was supported by the services sector, particularly retail trade. During the same quarter, the unemployment rate dropped to 4.4 per cent compared to a revised 4.6 per cent in the previous quarter, despite the slowdown in growth and falling real wages in the economy. The decline in the unemployment rate reflected higher employment figures for the youth population, which usually contributes the biggest share to the unemployment rate in the UK. Employment was highest in the services sector.

The inflation rate in the UK rose from 2.3 per cent in the quarter ending in March 2017 to 2.6 per cent in the quarter ending in June 2017. The increase in consumer prices was driven by increasing air fares, rising costs of clothing and electricity during the quarter. The Bank of England kept its key policy rate unchanged at 0.25 per cent during the review quarter. The decision was in light of worries about the slowdown in consumer spending as households struggled with rising prices and the slowing wage growth. The Bank of England noted that the slowdown in consumer spending had recently begun and it was therefore too early to judge how persistent it would be. The Bank also hinted that any policy rate hikes would be gradual.

EMERGING MARKET ECONOMIES

China

Growth in China remained stable at 6.9 per cent in the quarter under review, supported by firmer exports and production, in particular, of steel. During the same quarter, the unemployment rate remained stable at 4.0 per cent compared with the previous quarter. The stable unemployment rate was broadly in line with the economic performance during the quarter.

The inflation rate rose from 0.9 per cent in the first quarter of 2017 to 1.5 per cent in the second quarter of 2017. The increase was mainly driven by higher costs for non-food items. The Bank of China left the key policy rate unchanged at 4.35 per cent in the quarter under review. The decision to keep rates on hold was to maintain China's shift to a prudent and neutral monetary policy.

India

India's growth rate decelerated to 5.7 per cent during the second quarter of 2017, from 6.1 per cent in the quarter ending in March 2017. The subdued GDP growth resulted from a slowdown in consumer spending and exports during the same quarter. In line with weaker growth figures, the expectation is that employment for the second quarter of 2017 will fall.

During the second quarter of 2017, India's inflation rate was estimated to have declined to 1.5 per cent following a 3.8 per cent rate in the previous quarter. Inflationary pressures in India were dampened by falling food prices. The Reserve Bank of India left the policy rate unchanged during the quarter under review. The decision of the Reserve Bank of India was broadly consistent with a neutral stance of monetary policy in accordance with the objective of achieving the medium-term target for the inflation rate of 4 per cent while also supporting growth.

South Africa

The South African economy was lifted out of recession during the quarter under review, from a 0.7 per cent fall in the previous quarter. Higher output in Agriculture, Forestry and Fishing contributed to the upward growth movement. Despite better growth figures during the quarter under review, the unemployment rate in South Africa remained at its highest level reflecting lack of fixed investment spending by the private sector, as well as the sustained low business confidence.

During the second quarter of 2017, the inflation rate in South Africa fell to 5.1 per cent compared with 6.1 per cent in the quarter ending in March 2017. The fall in consumer prices was influenced by the slower pace of growth in the costs of transport, clothing and footwear, and restaurants and hotels. During the same quarter, the Reserve Bank of South Africa left the key policy rate unchanged at 7.00 per cent. The decision to keep an accommodative monetary policy stance was largely due to better-than-expected inflation which saw the rate returning to within the Bank's target range.

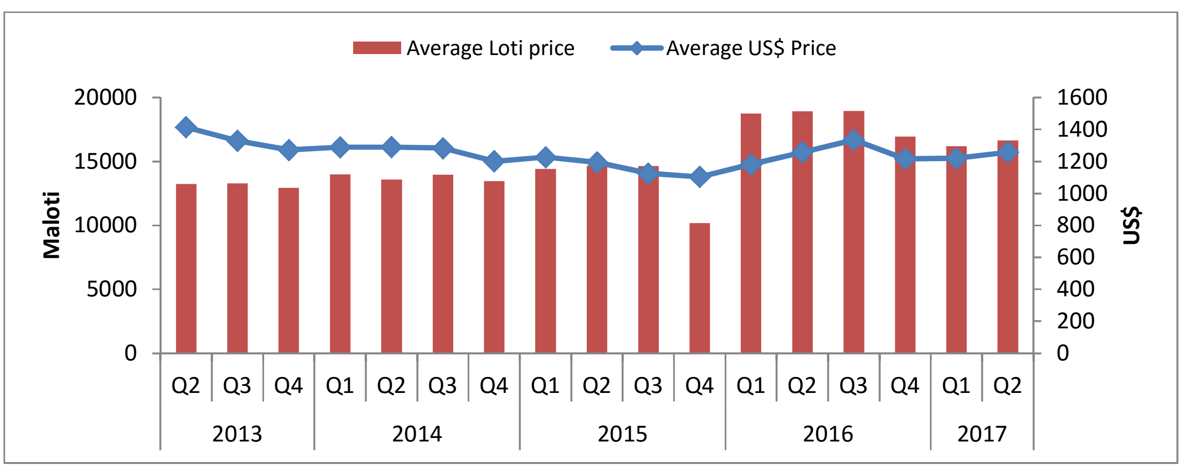
COMMODITIES

Minerals

Gold

The price of gold increased in both the Dollar and Maloti terms in the second quarter of 2017. In Dollar terms, gold prices went up by 3.2 per cent during the quarter under review, after slightly increasing by 0.3 per cent in the quarter ending in March 2017. In Maloti terms, the price of gold rose by 2.8 per cent, a recovery from a 4.4 per cent decline realised in the first quarter. The price was kept buoyant by increased demand for gold, as investors resorted to safe haven assets in the midst of heightened uncertainty in the global financial markets. In particular, the risks emanated from elections in the UK which resulted in hung parliament, uncertainty surrounding the US economic policies, and tensions arising from North Korea's nuclear programme.

Figure 1: **Average Price of Gold**

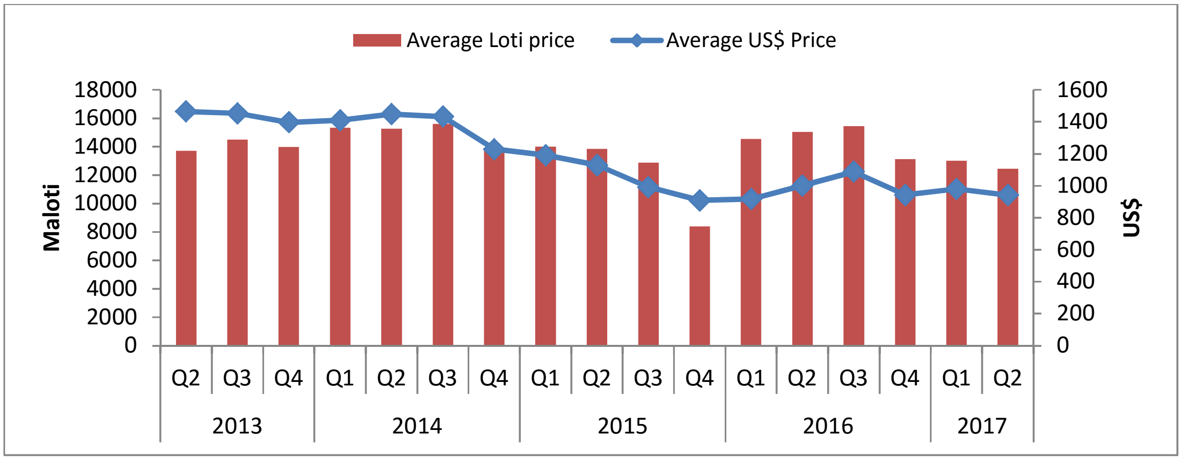


Source: Bloomberg

Platinum

During the second quarter of 2017, platinum prices declined in both the Dollar and Maloti terms. In Dollar terms, platinum prices fell by 4.0 per cent during the quarter under review against a 4.0 per cent increase in the first quarter of 2017. In Maloti terms, platinum prices declined by 4.9 per cent, after registering a 0.9 per cent decline in the previous quarter. The decline in platinum prices reflected a drop in sales for diesel automobiles, especially in Europe. Diesel vehicles use platinum for components of auto catalyst in order to lower pollution from the exhaust gas. There was also a slowdown in demand for platinum by the jewellery industry in China. With the jewellery industry being one of the biggest consumers of platinum, their low demand during the quarter led to a downturn in platinum prices.

Figure 2: **Average Price of Platinum**



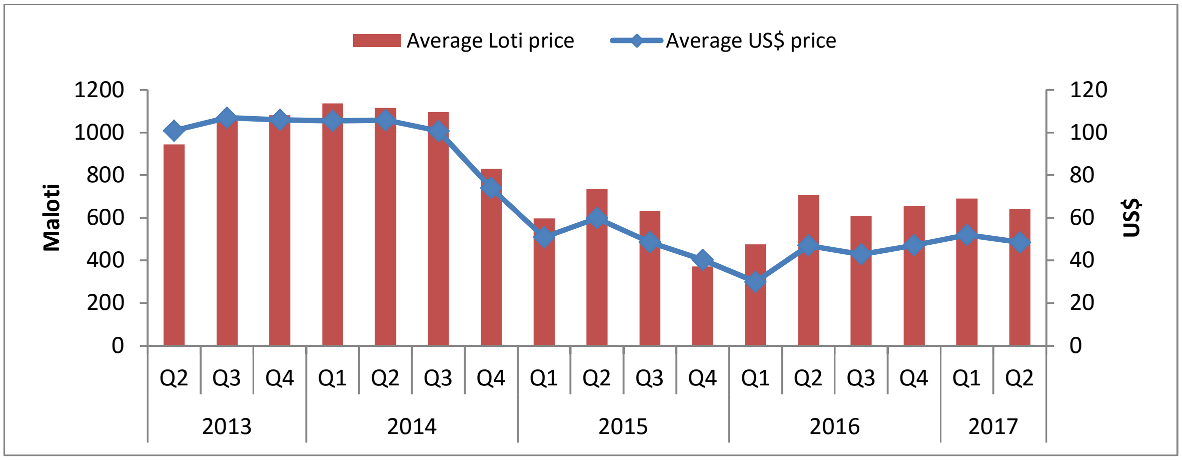
Source: Bloomberg

Energy

Oil

The price of oil, in Dollar terms, declined by 6.8 per cent in the second quarter of 2017 in contrast to 10.3 per cent increase in the first quarter of 2017. In Maloti terms, it declined by 7.2 per cent compared with an increase of 5.1 per cent in the previous quarter. The decline resulted from higher oil output by the US and Canada, undermining the OPEC's recent effort to cut excess supply. There was also increased output from some OPEC members which were exempted from the output cuts, notably Nigeria and Libya. This further threatened OPEC's plan to lift oil prices, which have endured an almost three year-long slump.

Figure 3: Average Price of Oil



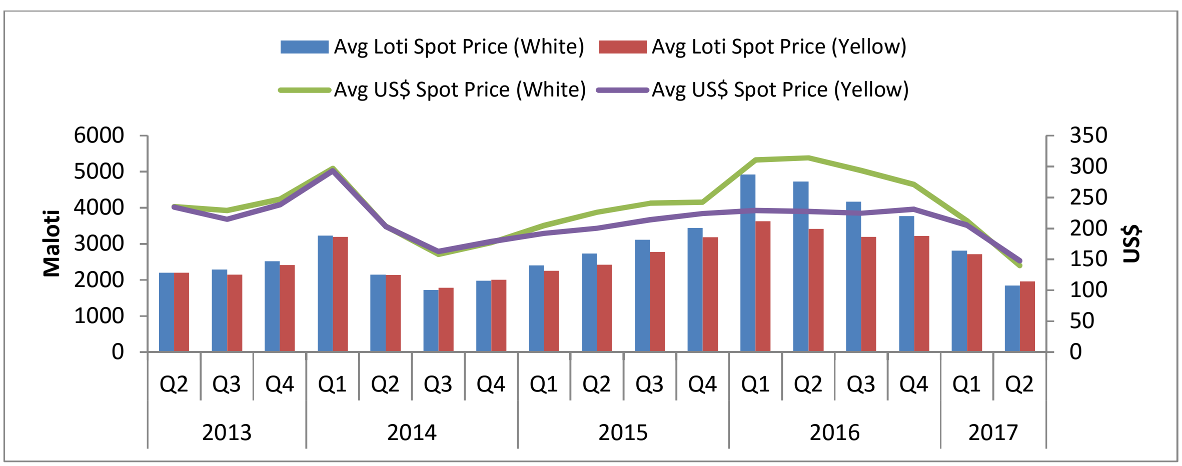
Source: Bloomberg

Agricultural Products

Maize

The price of white maize fell by 34.1 per cent in the second quarter of 2017, after a 21.7 per cent decline in the first quarter of 2017. Furthermore, there was a 27.9 per cent declined in the price of yellow maize. Expressed in Maloti terms, the price of white and yellow maize declined by 34.3 per cent and 28.1 per cent, respectively, during the quarter under review. The decline in the price of maize was mainly driven by increased production of maize in the global markets, with countries in the Southern hemisphere emerging from the El Nino weather pattern. Specifically a surge in production was driven by increased maize supplies from the US, Brazil and South Africa.

Figure 4: Average Price of Maize

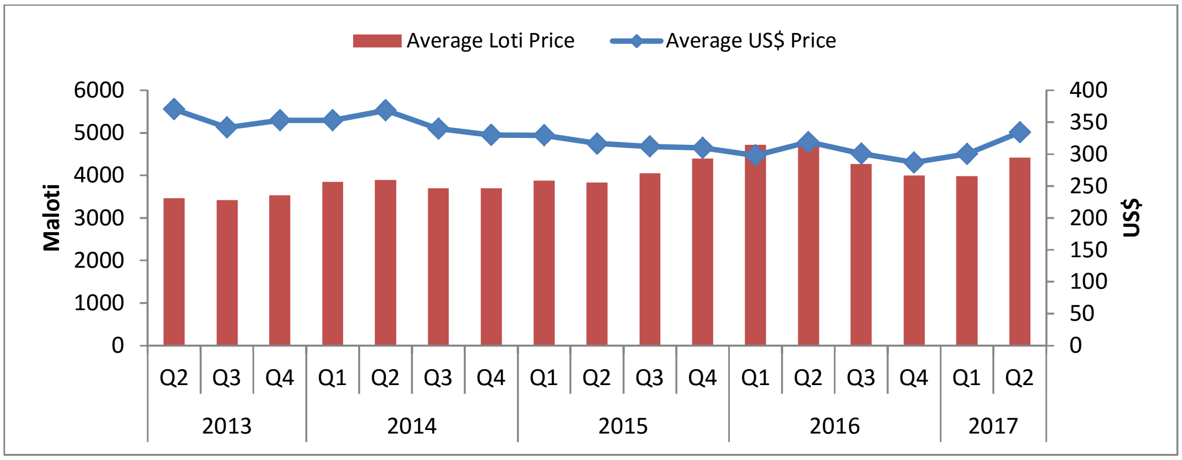


Source: Bloomberg

Wheat

In the second quarter of 2017, the Dollar price of wheat increased by 11.3 per cent following a 4.6 per cent rise in the previous quarter. In Maloti terms, the price of wheat recovered from a 0.3 per cent decline in the first quarter to a 10.9 per cent increase in the second quarter of 2017. The upward pressure on wheat price was due to poor quality wheat harvested, which resulted in limited availability of premium grade wheat. The situation was exacerbated by unfavourable weather conditions in the Northern hemisphere, particularly in Canada.

Figure 5: **Average Price of Wheat**

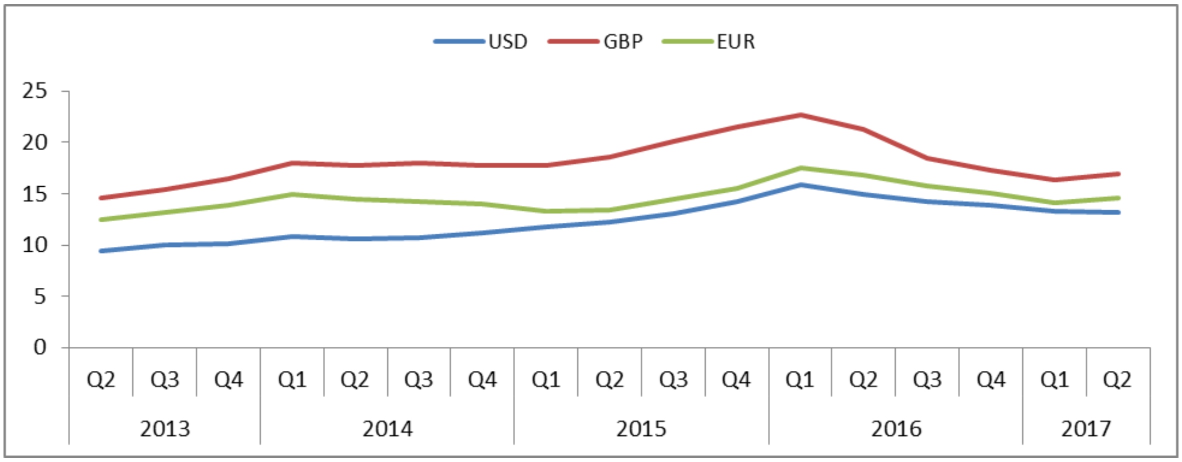


Source: Bloomberg

EXCHANGE RATES

During the second quarter of 2017, the Rand (Loti) lost momentum against the Pound and the Euro while it strengthened against the Dollar. Specifically, the Rand appreciated against the Dollar by 0.38 per cent during the quarter under review compared with an appreciation of 4.69 per cent in the previous quarter. The Rand remained resilient during the review quarter against the US dollar, despite the South Africa being downgraded to junk status by two credit rating agencies and a slippage into a technical recession in the face of heightened political uncertainty. Capital inflows to South Africa increased as a result of investors searching for higher yields in the emerging markets. Specifically, foreign holdings of South African bonds increased during the quarter. The US dollar was dragged down by uncertainty surrounding the policy rate normalization together with heightened risks in the global financial market. This resulted in the SA rand gaining momentum against the dollar. The Rand depreciated against the Pound by 3.60 per cent in the quarter under review compared to a 5.50 per cent appreciation in the previous quarter. The pound garnered strength from the expected rate hike in the second half of the year. The relatively strong service data, and the unity in the cabinet about a transition period for Brexit, which would ensure that UK and the EU do not automatically fall into the WTO trade rules as this would bring uncertainty in the markets. The Rand depreciated by approximately 3.0 per cent against the Euro during the quarter under review, compared to an appreciation of 5.90 per cent in the previous quarter. The euro gained strength from the fall of populist parties in the EU, as pro-EU parties won in countries such as France and the Netherlands. The Euro was also supported by the possible tapering of the QEE by the European Central Bank.

Figure 6: **Nominal Exchange Rate of Loti against Major Trading Currencies**



Source: Bloomberg

3. Real Sector Developments

OVERVIEW

Lesotho's economic activity contracted marginally in the second quarter of 2017 relative to the contraction recorded in the first quarter of 2017.The performance was somehow attributed to the positive growth in the primary sector given that the secondary and the tertiary sectors were subdued. In the labour market there were mixed performance as only the LNDC-assisted firms recorded positive growth while the government employment as well as the Basotho migrant mineworkers declined during the review period. Price developments in Lesotho remained heightened as food inflation remained high.

OUTPUT DEVELOPMENTS

During the second quarter of 2017, the overall economic activity (measured by EAI) declined by 0.5 per cent from a contraction of 4.3 per cent estimated for the first quarter of 2017, on a seasonally adjusted basis.

Table 2: Economic Performance by Industry *(Seasonally adjusted Quarter to Quarter Percentage Changes)*

		2016			2017	
	Weight	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**
EAI	**100**	**7.0**	**-2.0**	**-3.0**	**-4.3**	**-0.5**
Primary Sector						
Mining	**8.9**	-6.6	-3.3	18.2	4.9	15.1
Secondary Sector						
Manufacturing	**18.5**	-4.1	6.2	19.7	-8.4	-0.2
Electricity	**1.1**	-1.8	0.1	3.3	3.6	1.3
Water	**4.9**	2.7	6.8	1.6	-3.3	-8.2
Construction	**7.6**	146.9	-71.2	28.1	-14.3	-16.7
Tertiary Sector						
Trade	**11.0**	0.9	1.4	-8.1	-6.1	4.1
Telecom	**5.1**	1.1	-10.6	-2.4	34.7	1.1
Financial Sector	**6.5**	6.0	1.9	-4.0	1.3	0.2
Other services	**5.7**	9.9	0.6	-2.9	-14.1	5.4
Government	**30.6**	-7.1	26.7	-19.4	-9.5	-5.8

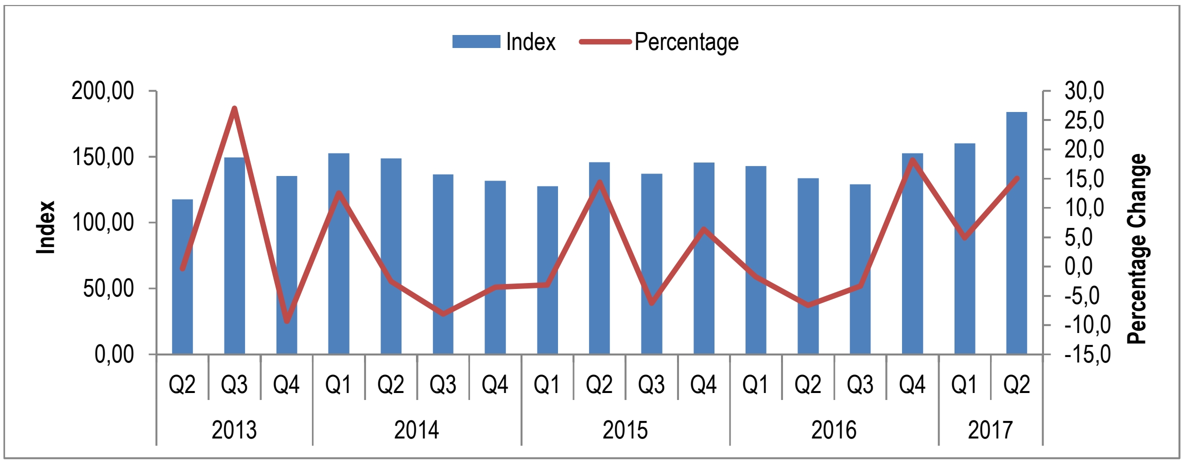
Source: Central Bank of Lesotho

Primary Sector

Mining and Quarrying

During the quarter under review, the mining and quarrying output grew at a relatively faster rate of 15.1 percent from 4.9 percent recorded in the previous quarter on a seasonally adjusted basis. The faster pace of growth in the industry mainly emanated from two thirds of the mines, thus tremendously increasing the mining production in the second quarter. Nonetheless, this was moderated by a slight decline in one of the mines, resulting in lower than expected output.

Figure 7: Mining and Quarrying Index



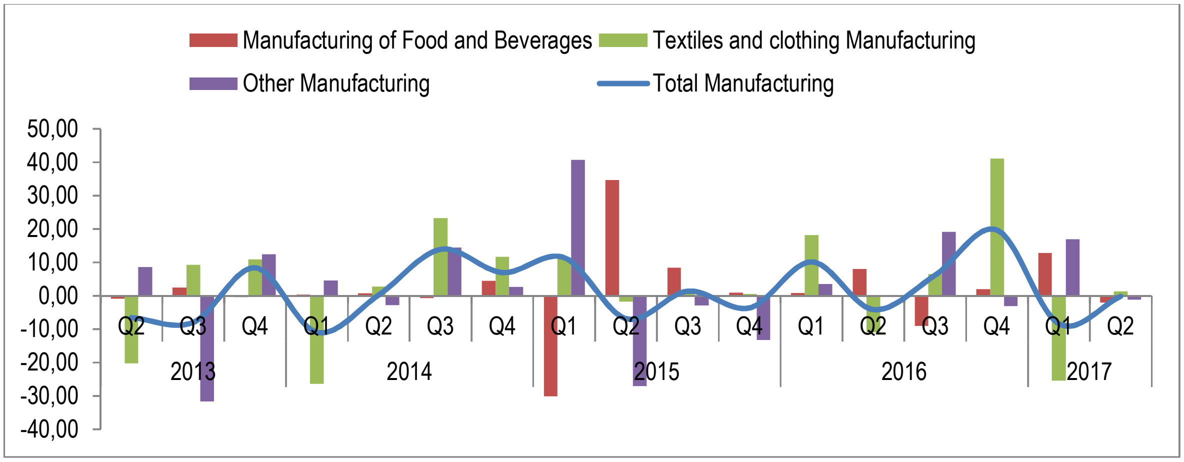
Source: Central Bank of Lesotho

Secondary Sector

Manufacturing

The manufacturing output marginally declined in the second quarter of 2017 relative to the first quarter. On a seasonally adjusted basis, manufacturing output index recorded an estimated decline of 0.2 percent during the review period from 8.4 percent in the first quarter of 2017. The decline in the manufacturing activity mainly emanated from the "food manufacturing" and "other manufacturing" categories while the "textile manufacturing" moderated the decline. The relatively slight decline in the manufacturing subsector's output is attributable to a large rebound in the demand for exports, especially the knit and woven garments during the review quarter from the subdued performance recorded in the previous quarter.

Figure 2: Manufacturing Subsector *(Quarter to Quarter Percentage Changes)*

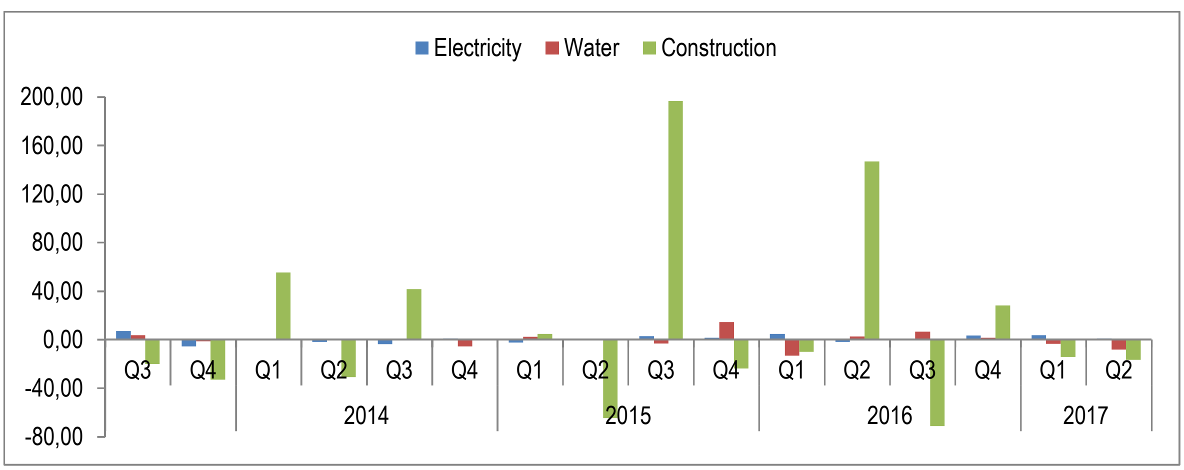


Source: Central Bank of Lesotho

Electricity

The electricity subsector output grew, albeit at a slower pace during the review period relative to the previous quarter on a seasonally adjusted basis. The economic activity index grew at 1.3 percent in the second quarter of 2017 form 3.6 percent recorded in the first quarter. The relatively slower pace of growth in electricity subsector in the second is mainly attributable to the "commercial and industrial" category, while the "general purpose" and "domestic" categories rebounded from a slump in the previous quarter and moderated the slowdown. The slower activity during the review period is in line with the slight pickup in the textile and clothing industry, especially the wet industries.

Figure 3: Secondary Sector *(Quarter to Quarter Percentage Changes)*



Source: Central Bank of Lesotho

Water

In the water subsector, the output contracted further by 8.2 percent during the review period from a contraction of 3.3 percent recorded in the previous quarter of 2017.The decline in the subsector's output was mainly due to the decline in water exports by LHDA while on the domestic front water output increased. Water produced for non-export consumption increased mainly emanating from the "industrial" and "other" categories while the "domestic" component moderated the increase. The domestic improvement in water subsector performance is attributable to the slight recovery of the manufacturing sector economic activity, especially the demand for the textiles and clothing exports.

Construction

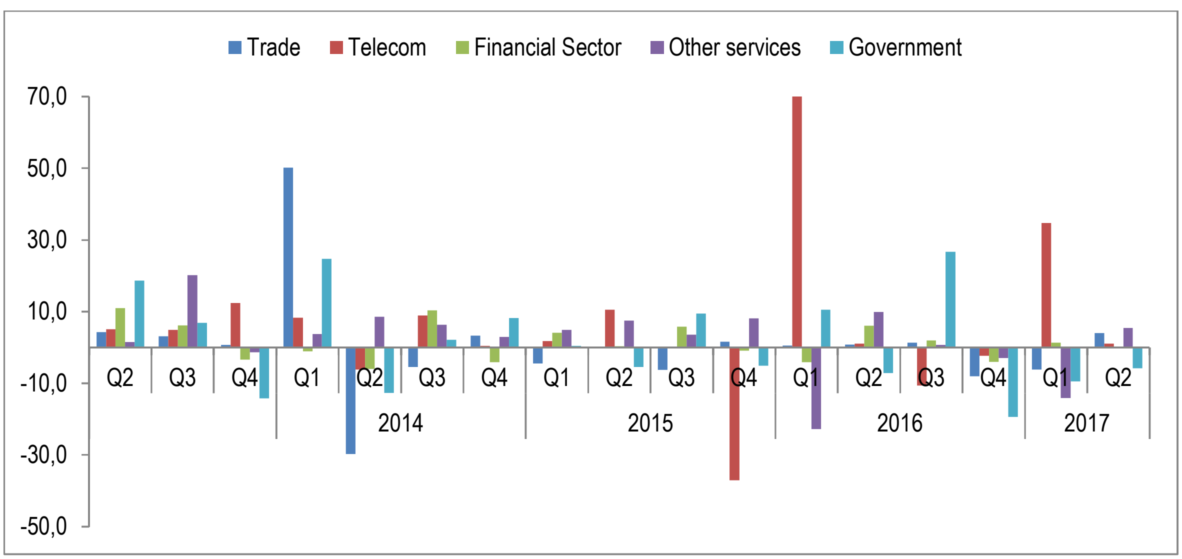
The construction subsector's output index further declined by a slightly higher percentage of 16.7 during the review period relatively to a contraction of 14.3 percent recorded in the first quarter of 2017, on seasonally adjusted basis. The decline is mainly attributed to decline in capital development projects of the Government of Lesotho during the review period

Tertiary Sector

Trade

The trade subsector experienced a turnaround in the second quarter of 2017 by growing at 4.1 percent relative to a contraction of 6.1 percent realized in the first quarter of 2017 on a seasonally adjusted basis. The increased activity was mainly due to "motor", "fuel" and "wholesale" trade components while the retail trade moderated the improvement. This is mainly attributed to increased consumer sentiment as the economy improved during the quarter under review, despite the accelerating inflation rate during the review quarter.

Figure 4: Tertiary Sector *(Quarter to Quarter Percentage Changes)*



Source: Central Bank of Lesotho

Telecommunications

The telecommunications subsector slowed down the second quarter of 2017 as it grew by 1.1 percent relative to a growth of 34.7 percent in the first quarter of 2017, on seasonally adjusted basis.

Finance

The seasonally adjusted data on financial sector intermediation shows that output slowed down by 0.2 percent in the second quarter of 2017 compared with 1.3 percent increase realized in the preceding quarter. The slowdown is mainly attributed to both banking sector credit and total deposits which grew at relatively slower pace during the review period compared with the preceding quarter.

Other Services

The seasonally adjusted "other services" output rebounded by a positive growth of 5.4 percent in the second quarter of 2017 from a contraction of 14.1percent in the first quarter. The reversal in the growth rate of this subsector's output is mainly attributed to the turnaround of activities in all of the subsector's categories except for the "other recreational activities", which continued to decline in the period under review relative to the previous period.

Government

The seasonally adjusted government output increased by 59.4 percent in the second quarter of 2017 compared with a contraction of 20.1 percent realized in the first quarter of 2014. The increase was mainly at the back of increased activity as the government massively increased the purchases of goods and services ahead of the recent national elections. The purchases of goods and services increased by more than twofold during the review period, but were moderated by the decline in compensation of employees. The decline in latter is mainly due to the Government's efforts to manage the wage bill and biometric registration of employees.

EMPLOYMENT DEVELOPMENTS

Employment by LNDC-assisted companies increased by 4.2 percent in the second quarter of 2017 form a decline of 1.8 percent realized in the preceding quarter. The rebound in the employment by firms assisted by LNDC mainly emanated from the woven and knit garments, retail, construction, as well as from food and beverages. However, the footwear, electronics and hotel & accommodation shed jobs during the review period. The increased number of employees during the quarter under review is attributed to a slight improvement in production and hence sales in the manufacturing sector especially the textile and clothing subsector from a slump in the preceding quarter. Moreover, increased employment in other sectors mainly reflects the buoyed performance of the economy during the quarter under review. However, some sectors shed jobs but at a relatively lesser pace.

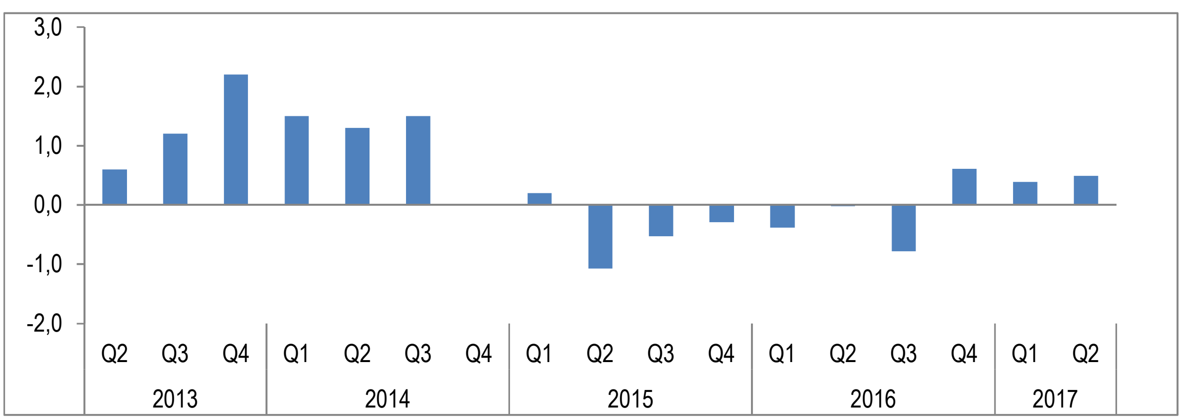
Table 2: Employment by LNDC Assisted Companies

Industry	2016			2017		% Change	
	Q2	Q3	Q4	Q1	Q2	Q/Q	Y/Y
Knit Garments………….	23829	24774	24818	24897	25252	1.4	6.0
Woven Garments…….	17274	17057	14921	13678	15561	13.8	-9.9
Footwear…………………	753	1265	1293	1403	1165	-17.0	54.7
Fabrics, Yarn etc……….	1777	1686	1801	1803	1817	0.8	2.3
Construction…………….	358	327	342	359	390	8.6	8.9
Food & Beverages……….	682	682	650	696	734	5.5	7.6
Electronics………………..	141	962	1007	1030	931	-9.6	560.3
Retail……………………….	139	139	109	109	146	33.9	5.0
Hotel Accomm………..	565	565	502	663	630	-5.0	11.5
Other……………………..	1908	1779	1226	1197	1217	1.7	-36.2
TOTAL……………………	**47246**	**49236**	**46669**	**45835**	**47843**	**4.4**	**0.9**

Source: Lesotho National Development Corporation

The total number of government employees declined by 0.6 percent during the review period from a decline of 0.5 percent recorded in the preceding quarter. The quarterly decline mainly emanated from the civil servants and teachers category even though total number of teachers declined by a smaller margin compared with the preceding quarter. Nonetheless, the total number of government employees, year-on-year basis, increased by 0.5 percent during the review period compared with 0.4 percent realized in the preceding quarter, year-on-year basis. The quarter-on-quarter decline is mainly attributed to the Government's efforts in containing the wage bill and revamping the system in order to get rid of "ghost" workers.

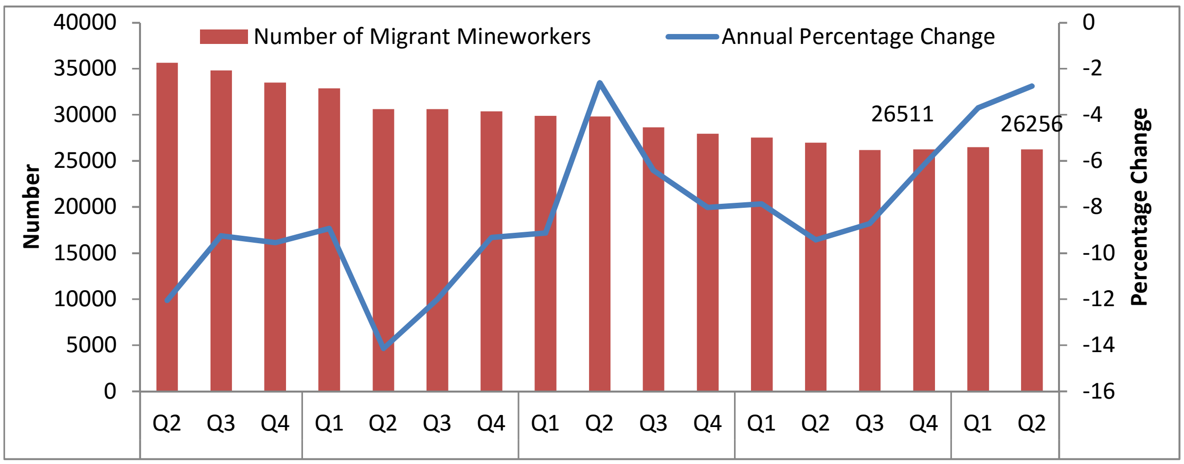
Figure 5: Government Employment *(Year-on-year Percentage Change)*



Source: Ministry of Finance

During the review period, the number of Basotho migrant mineworkers is estimated to have declined to 26256 in the second quarter of 2017 from 26511 recorded in the first quarter. The annual percentage change of the Basotho migrant mineworkers continued to decline during the quarter under review, albeit at a slower pace of 2.7 percent compared with 3.6 percent estimated for the first quarter of 2017. The decline in the number of migrant mineworkers is attributed to the fall in mining output, especially the gold and the iron ore output during the quarter under review.

Figure 6: Migrant Mineworkers *(Year-on-year Percentage Changes)*



Source: The Employment Bureau of Africa (TEBA)

PRICE DEVELOPMENTS

Inflation rate in Lesotho, as measured by the percentage change in the overall consumer price index (CPI) accelerated to 5.0 in the quarter ending in June 2017 from 4.4 percent estimated for the quarter ending in March 2017. The main contributors to the acceleration in headline inflation during the period under review are "Food and non-alcoholic beverages", "Furniture, households' equipment & routine maintenance", "Leisure, entertainment & Culture", "Education" and "Miscellaneous goods & services". However, the acceleration was moderated by components such as "Alcoholic beverages & Tobacco", "Housing, electricity gas & other fuels" and "Transport". The acceleration in overall inflation comes at a time when the food subsidy that was implemented in the previous year came to an end, despite falling food prices across the Southern African region.

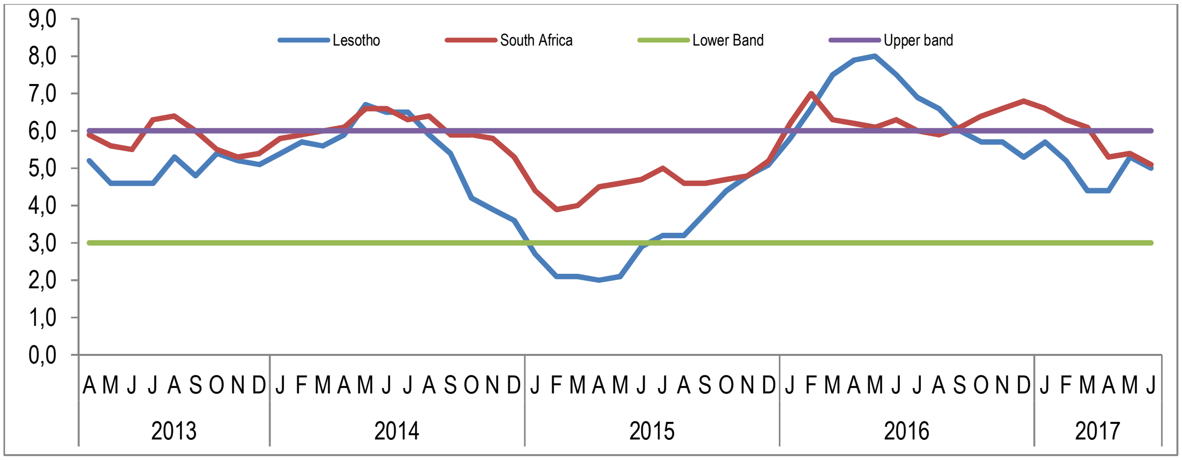
Table 3: Inflation Rate *(Annual Percentage Changes)*

		2017				
	Weight	Feb	Mar	Apr	May	Jun
All items	**100**	**5.2**	**4.4**	**4.4**	**5.3**	**5.0**
Food and non-alcoholic beverages	36.1	7.0	5.2	4.8	6.1	6.5
Alcoholic beverages & Tobacco	3.3	4.6	4.9	4.6	4.6	4.3
Clothing & footwear	13.1	2.7	2.6	2.8	3.2	2.6
Housing, electricity gas & other fuels	12.4	7.5	7.6	7.9	8.9	5.5
Furniture, households equipment & routine maintenance	8.5	3.0	3.5	4.7	6.5	6.5
Health	1.5	0.9	0.5	0.4	0.4	0.3
Transport	4.8	3.3	3.0	1.4	0.1	-0.3
Communication	2.1	0.0	0.0	0.0	0.0	0.0
Leisure, entertainment & Culture	5.7	0.3	0.8	2.4	4.1	5.1
Education	4.2	5.1	5.1	5.1	5.1	5.6
Restaurant & Hotels	1.0	1.2	1.0	0.9	1.0	1.4
Miscellaneous goods & services	7.3	3.2	3.1	3.9	5.1	5.1

Source: Bureau of Statistics

While Lesotho's headline inflation rate accelerated from 4.4 percent in the quarter ending in March 2017 to reach 5.0 percent in the quarter ending in June 2017, its South Africa counterpart declined from 6.0 percent. The SA headline inflation reached 5.1 percent in the quarter ending in June 2017, just 10 basis points above that of Lesotho. After decoupling for some time since September 2016, the headline inflation rates in the respective countries do move in tandem since May 2017. The decline from May to June in both inflation rates is at the back of declining food prices induced by expected good harvest. Nonetheless, the food and non-alcoholic beverages component in Lesotho remained resilient to the declining regional food prices.

Figure 7: Lesotho and South Africa's Inflation



Source: Bureau of Statistics, Statistics South Africa

4. Monetary and Financial Developments

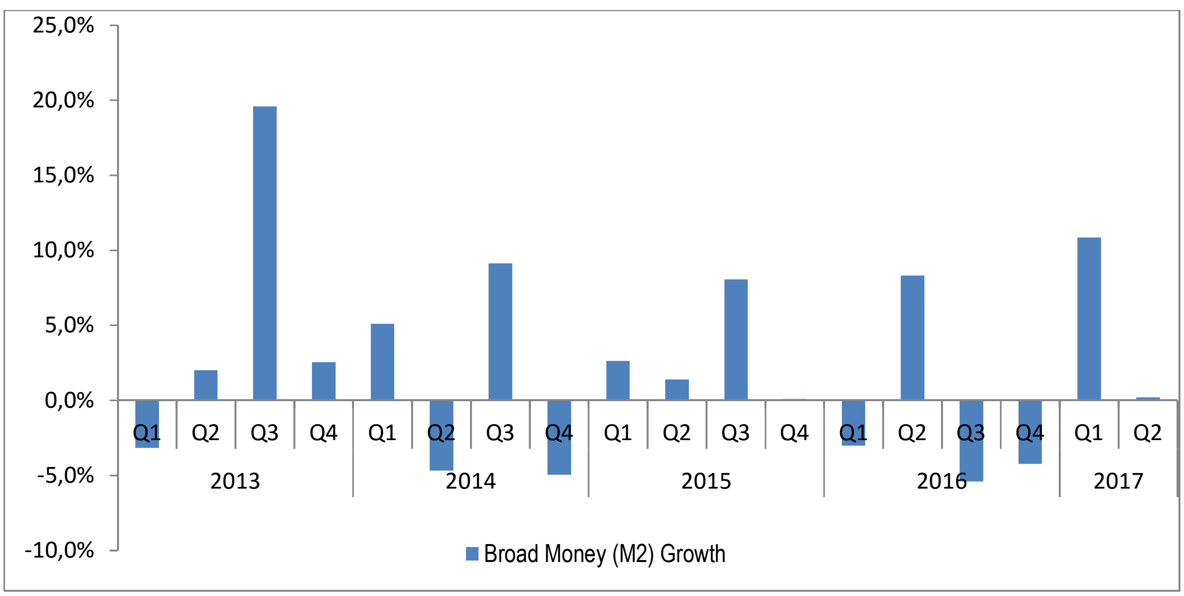
OVERVIEW

Money supply increased by 0.2 per cent in the quarter under review compared to an increase of 10.9 per cent in the previous quarter. This was on account of a 1.07 per cent increase in quasi money moderated by a 0.6 per cent decline in narrow money. Banking system Net Foreign Assets (NFA) declined by 0.56 per cent in quarter two of 2017 against a 0.79 per cent decline in the previous quarter. This was attributed to a decline in commercial banks' transferable deposits with non-residents as well as their holdings of foreign currency. Domestic claims registered a 2.63 per cent decline in the quarter ending June 2017 compared to an increase of 53.4 per cent in the quarter ending March 2017. The main reasons were drops in claims on other financial corporations (OFCs) and claims on Public Non-Financial Corporations. Credit extended to the business sector registered a decline of 0.07 per cent in the quarter under review from an increase of 6.90 per cent in the previous quarter. Credit extended to households increased at a rate of 2.13 per cent in the review period compared to an increase of 0.88 per cent in the previous period. This was on account of growth in both mortgage and personal loans.

BROAD MONEY (M2)

Money supply increased slightly in the quarter under review relative to the sharp increase observed in the previous quarter. Overall, money supply increased at a decreasing rate of 0.2 per cent during the second quarter of 2017 following a rise of 10.9 per cent in the quarter ending March 2017. This escalation was driven by a 2.63 per cent decline in domestic claims and a 0.56 per cent decline in Net Foreign Assets (NFA).

Figure 8: Broad Money (M2)



Source: Central Bank of Lesotho

Determinants of M2

Domestic Claims

Domestic claims, including net claims on government, declined at a rate of 2.63 per cent in the quarter ending June 2017 compared to an increase of 53.4 per cent registered in the quarter ending March 2017. This was chiefly on the back of a 6.36 per cent drop in commercial banks' net claims on central government coupled with an increase in central bank net claims on central government and a drop in claims on other sectors of 1.56 per cent and 1.75 per cent, respectively. Commercial banks' liabilities to central government increased by over 100 per cent in the quarter under review owing to new fixed deposit account holdings by Public Non-Financial Institutions. On the other hand, commercial banks' claims on Other Financial Corporations (OFCs) dropped by 48.58 per cent in the quarter ending June 2017 as investments in consolidated investment schemes were transferred to local and non-resident banks.

Table 2: Domestic Claims *(Million Maloti: End Period)*

	2016			2017		Changes(%)	
	June	Sept	Dec	Mar	June	Annual	Quarterly
Domestic Claims	**2158.58**	**2759.69**	**3160.32**	**4848.19**	**4770.61**	**121.0 %**	**-1.6%**
Net Claims on Government	**-3497.51**	**-2978.80**	**-2584.01**	**-1367.76**	**-1336.27**	**-61.8%**	**-2.3%**
Commercial Banks Net Claims	**810.94**	**829.84**	**824.41**	**829.95**	**827.19**	**2.0%**	**-0.3%**
Claims on Central Government	843.52	855.48	846.96	847.05	842.42	**-0.1%**	**-0.5%**
Liabilities to Central Government	32.58	25.64	22.55	17.09	15.23	**-53.3%**	**-10.9%**
Central Bank Net Claims	**-4308.45**	**-3808.64**	**-3408.41**	**-2197.71**	**-2163.46**	**-49.8%**	**-1.6%**
Claims on Central Government	1046.02	981.15	1106.94	1072.47	997.99	**-4.6%**	**-6.9%**
Liabilities to Central Government	5354.46	4789.80	4515.35	3270.18	3161.45	**-41.0%**	**-3.3%**
Claims on Other Sectors	**5656.09**	**5738.49**	**5744.32**	**6215.95**	**6106.89**	**8.0%**	**-1.8%**
Claims on OFCs	84.10	80.94	79.67	325.60	167.42	**99.1%**	**-48.6%**
Claims on Public Nonfinancial Corporations	0.00	0.00	0.00	48.70	4.67		**-90.4%**
Claims on St &Local Government	0.00	0.00	0.00	0.00	0.00		
Claims on Private Sector	**5571.99**	**5657.55**	**5664.65**	**5841.66**	**5934.79**	**6.5%**	**1.6%**
Claims on Business Enterprises	2196.70	2148.75	1966.75	2102.46	2100.98	**-4.4%**	**-0.1%**
Claims on Households	3375.29	3508.80	3697.90	3739.20	3833.81	**13.6%**	**2.5%**

Source: Central Bank of Lesotho

Net Foreign Assets

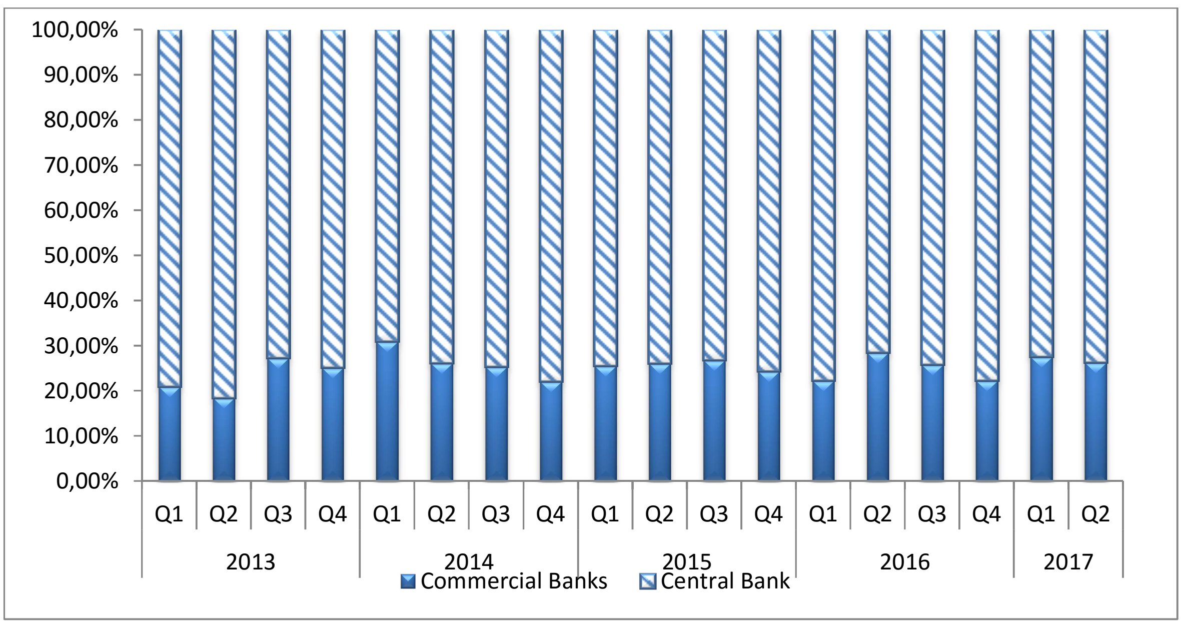
During the review period, total banking system Net Foreign Assets (NFA) experienced a decline of 0.56 per cent compared to a decline of 0.79 per cent in the previous quarter. This was attributed to a decline in commercial banks' NFA to the tune of 5.1 per cent in the second quarter of 2017 compared to an increase of 22.53 per cent in the previous quarter. Conversely, central bank NFA increased by 1.18 per cent in the quarter ending June 2017 following a decline of 7.52 per cent in the quarter ending March 2017. Commercial banks' claims on non-residents, specifically their transferable deposits with non-residents and holdings of foreign currency declined due to increased foreign transactions and a slowdown in the demand for foreign currency by bank clients. On the other hand, the central bank's liabilities to non-residents declined by 2.94 per cent.

Table 3: Net Foreign Assets *(Million Maloti: End Period)*

	2016			2017		Changes (%)	
	June	Sept	Dec	Mar	June	Annual	Quarterly
Commercial Banks	**4594.25**	**3680.96**	**2992.48**	**3666.75**	**3479.61**	**-24.3**	**-5.1**
Claims on Non-residents	4895.02	4041.09	3330.04	4057.79	3939.49	**-19.5**	**-2.9**
Liabilities to Non-residents	300.76	360.13	337.55	391.04	459.88	**52.9**	**17.6**
Central Bank	**11507.86**	**10534.13**	**10381.89**	**9601.58**	**9714.91**	**-15.6**	**1.2**
Claims on Non-residents	13233.44	12152.53	11920.42	11155.31	11222.91	**-15.2**	**0.6**
Liabilities to Non-residents	1725.58	1618.41	1538.53	1553.73	1508.01	**-12.6**	**-2.9**
Net Foreign Assets Total	**16102.11**	**14215.08**	**13374.37**	**13268.33**	**13194.52**	**-18.1**	**-0.6**

Source: Central Bank of Lesotho

Figure 9: Net Foreign Assets *(percentage shares)*



Source: Central Bank of Lesotho

Components of M2

The major components of broad money (M2) are narrow money (M1) and quasi money. During the review period, broad money increased by 0.2 per cent in the period under review compared to an increase of 10.9 per cent in the quarter ending March 2017. This was the result of a 1.0 per cent increase in quasi money following a 1.1 per cent increase in other deposit liabilities of commercial banks in the second quarter of 2017 relative to a 14.3 per cent increase in the previous quarter. The commercial banks other deposit liabilities benefited from new fixed deposit accounts opened by Public Non-Financial Corporations.

Table 4: Components of Money Supply *(Million Maloti: End Period)*

	2016			2017		Changes (%)	
	June	Sept	Dec	Mar	June	Annual	Quarterly
Broad Money (M2)	**10646.59**	**10069.99**	**9644.19**	**10692.01**	**10713.06**	**0.6**	**0.2**
Narrow Money (M1)	**5206.05**	**4870.73**	**4875.62**	**5253.55**	**5222.87**	**0.3**	**-0.6**
Currency Outside DCs	907.06	940.02	943.02	934.51	919.40	**1.4**	**-1.6**
Transferable Deposits	4298.99	3930.72	3932.60	4319.04	4303.47	**0.1**	**-0.4**
Quasi Money	**5440.54**	**5199.26**	**4768.57**	**5438.45**	**5490.19**	**0.9**	**1.0**
Other Deposits Commercial Banks	5385.45	5144.79	4718.59	5391.06	5449.00	**1.2**	**1.1**
Other Deposits Central Bank	55.09	54.47	49.98	47.40	41.19	**-25.2**	**-13.1**

Source: Central Bank of Lesotho

CREDIT EXTENSION

Trends of Credit Extended to Business Enterprises

Total credit extended to business enterprises declined by 0.07 per cent in the quarter ending June 2017 compared to an increase of 6.90 per cent in the quarter ending March 2017. The sectors that experienced a decline in credit were Agriculture, construction, manufacturing, real estate and business services as well as community, social and personal services. The decline was moderated by increased credit extension to mining and quarrying, electricity, gas and water as well as wholesale, retail, hotel and restaurant. The main drivers of the reduced credit extension were monthly runoffs net of new loans as well as un-utilised overdraft facilities.

Table 5: Credit Extension by Economic Activity (Million Maloti)

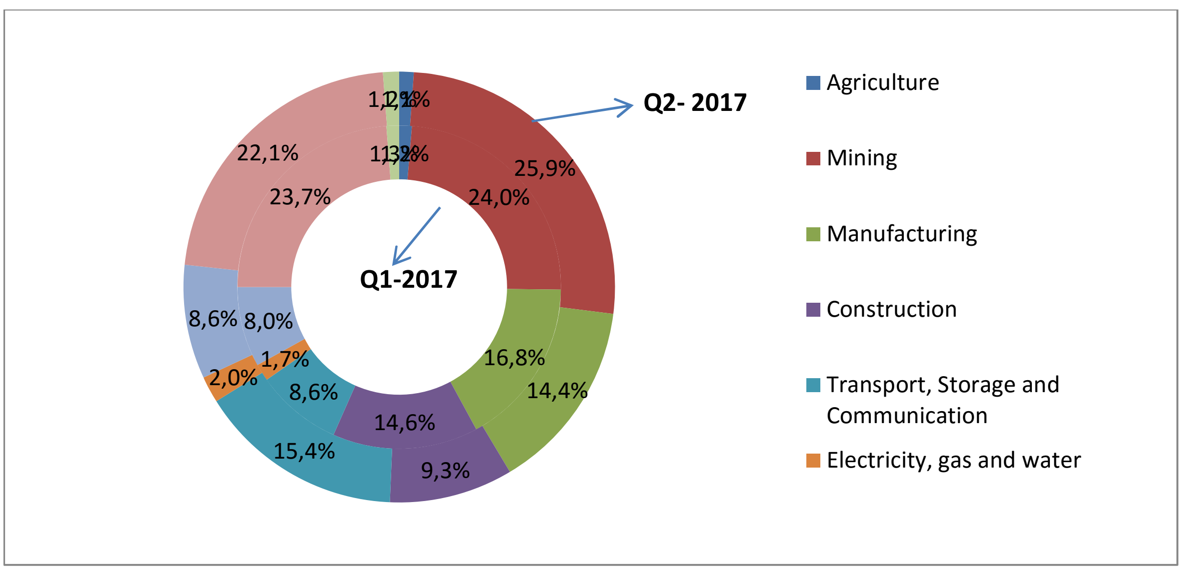
	2016			2017		Changes (%)	
SECTOR	**June**	**Sept**	**Dec**	**Mar**	**June**	**Annual**	**Quarterly**
Agriculture	20.34	24.58	25.31	26.20	22.73	**11.7**	**-13.2**
Mining	414.73	432.56	363.84	504.98	544.27	**31.2**	**7.8**
Manufacturing	428.66	413.44	319.40	354.10	303.00	**-29.3**	**-14.4**
Electricity, gas and water	31.97	39.69	38.53	36.55	41.91	**31.1**	**14.7**
Construction	289.91	284.43	313.50	305.92	195.17	**-32.7**	**-36.2**
Wholesale, Retail, Hotel & Restaurant	146.92	165.74	185.65	168.13	179.74	**22.3**	**6.9**
Transport, Storage and Communication	274.97	171.98	184.69	180.84	323.73	**17.7**	**79.0**
NBFIs, Real Estate and Business Services	567.82	594.09	509.46	499.07	465.19	**-18.1**	**-6.8**
Community, Social & Personal Service	21.36	22.22	26.38	26.68	25.26	**18.3**	**-5.3**
All Sectors	**2196.70**	**2148.75**	**1966.75**	**2102.46**	**2100.98**	**-4.4**	**-0.1**

Source: Central Bank of Lesotho

Distribution of credit Extended to Business Enterprises

When the distribution of credit to business enterprises is considered, mining, real estate and business services, and transport, storage and communication received the biggest share of credit at 25.9 per cent, 22.1 per cent and 15.4 per cent, respectively. The agriculture sector continues to receive the lowest share of credit. These developments are broadly in line with those registered in the quarter ending March 2017.

Figure 10: Distribution of Credit *(Percentage Shares)*

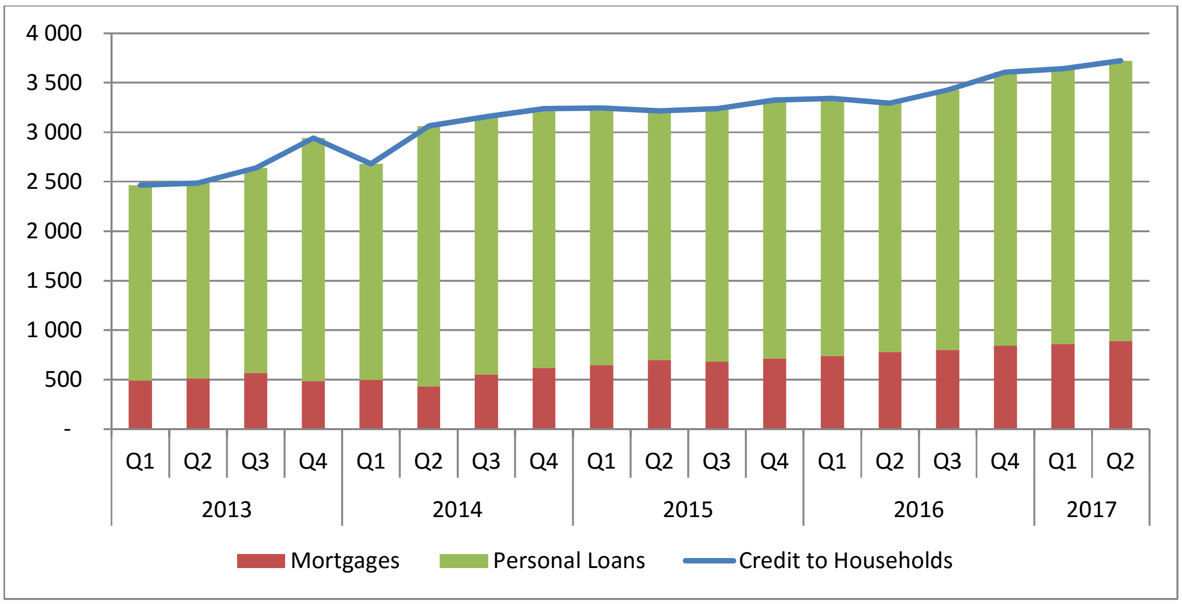


Source: Central Bank of Lesotho

Credit Extended to Households

Credit extended to households increased by 2.13 per cent in the quarter ending June 2017 compared to a moderate increase of 0.88 per cent in the quarter ending March 2017. Specifically, mortgage loans increased by 3.98 per cent in the second quarter of 2017 relative to an increase of 1.90 per cent in the first quarter of 2017. Moreover, personal loans increased by 1.57 per cent in the review period compared to an increase of 0.71 per cent in the previous period. Although personal loans still account for the biggest proportion of loans to household, it is encouraging to note the persistent growth in mortgage loans quarter on quarter.

Figure 11: Credit Extension to Household *(Million Maloti)*



Source: Central Bank of Lesotho

LIQUIDITY OF COMMERCIAL BANKS

Components of Liquidity

The credit to deposit ratio increased moderately from 59.2 per cent to 59.8 per cent in between the first and second quarters of 2017. This was on account of a 1.33 per cent increase in private sector credit that outstripped the 0.44 per cent increase in total deposits. The liquidity ratio registered a 0.22 per cent increase in the quarter under review. This was due to an increase in commercial banks' balances due from banks in South Africa following increased government spending through the domestic banking system.

Table 6: Components of Liquidity *(Million Maloti)*

	2016			2017	
	June	Sept	Dec	Mar	June
Credit to Deposit Ratio	**56.7%**	**61.5%**	**64.6%**	**59.2%**	**59.8%**
Private Sector Credit	5495.21	5579.90	5584.59	5752.01	5828.32
Total Deposits	9684.43	9075.50	8651.19	9710.10	9752.47
Liquidity Ratio	**86.0%**	**77.0%**	**72.4%**	**74.3%**	**74.5%**
Notes and Coins	349.94	361.15	582.42	411.35	431.95
Balance due from banks in Lesotho	2577.87	2043.77	2127.76	1922.62	1875.00
Balance due from banks in SA	4501.12	3725.30	2533.81	3577.09	3600.58
Surplus funds	55.32	5.08	170.39	461.26	517.13
Government Securities	843.52	855.48	846.96	847.05	842.42
Total	**8327.78**	**6990.78**	**6261.34**	**7219.36**	**7267.07**

Source: Central Bank of Lesotho

Commercial Banks Sources of Funds

The main sources of funds for commercial banks are deposits which comprise of transferable and other deposits. Transferable deposits included in broad money declined at a rate of 0.36 per cent in the second quarter of 2017 against an increase of 9.83 per cent in the first quarter of 2017. This was due to increased third party payments on behalf of the private sector. On the other hand, other deposits included in broad money increased by 1.07 in the quarter under review compared to an increase of 14.25 per cent in the previous quarter. The developments in other deposits benefited from call and fixed time deposit injections by Public Non-Financial Corporations and the private sector.

Table 7: Sources of funds for ODCs *(Million Maloti)*

	2016			2017		Changes (%)	
	June	Sept	Dec	Mar	June	Annual	Quarterly
Transferable Deposits Incl. in BM	**4298.99**	**3930.72**	**3932.60**	**4319.04**	**4303.47**	**0.1**	**-0.4**
Other Financial Corporations	65.19	30.68	38.29	61.53	34.86	**-46.5**	**-43.3**
Public Nonfinancial Corporations	33.92	29.76	17.25	81.56	72.81	**114.7**	**-10.7**
Private Sector	4181.92	3852.31	3859.10	4157.99	4177.84	**-0.1**	**0.5**
Other NFCs	2734.49	2528.86	2299.58	2215.67	2403.05	**-12.1**	**8.5**
Other Sectors (Households)	1447.44	1323.45	1559.52	1942.31	1774.79	**22.6**	**-8.6**
Other Deposits Incl. in BM	**5385.45**	**5144.79**	**4718.59**	**5391.06**	**5449.00**	**1.2**	**1.1**
Other Financial Corporations	120.78	97.70	75.14	90.94	95.38	**-21.0**	**4.9**
Public Nonfinancial Corporations	231.33	173.38	94.45	419.75	376.32	**62.7**	**-10.3**
Private Sector	5033.33	4873.70	4549.00	4880.37	4977.30	**-1.1**	**2.0**
Other NFCs	3571.34	3423.29	3022.96	3161.99	3276.23	**-8.3**	**3.6**
Other Sectors (Households)	1462.00	1450.41	1526.04	1718.38	1701.06	**16.4**	**-1.0**
Total Deposits	**9684.43**	**9075.50**	**8651.19**	**9710.10**	**9752.47**	**0.7**	**0.4**

Source: Central Bank of Lesotho

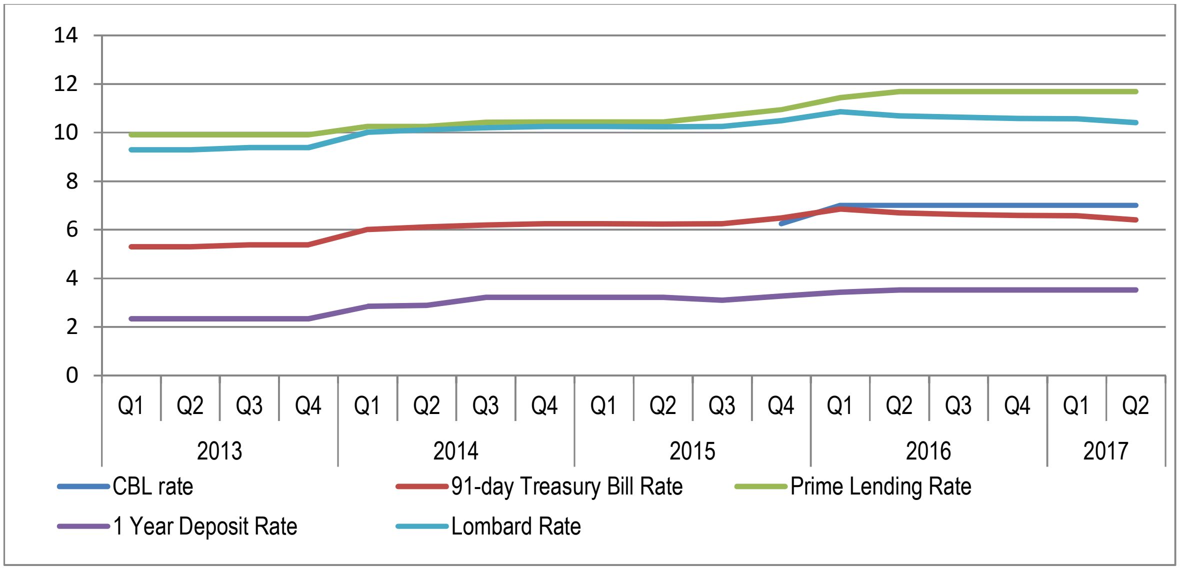
MONEY AND CAPITAL MARKET DEVELOPMENTS

Money Market

Interest Rates

The CBL rate remained constant at 7 per cent between the first and second quarters of 2017. Commercial bank prime lending rate also remained stable at an average of 11.69 per cent from March 2017 to June 2017. There were no changes to the 1 year deposit rate that stood at 3.52 per cent during the same period. The 91-day Tbill slightly declined from 6.57 per cent in March 2017 to 6.42 per cent in June 2017.

Figure 12: Short Term Interest Rates *(Per Cent per Annum)*



Source: Central Bank of Lesotho

Table 8: **Interest Rates**

	2016			2017	
	Jun	**Sept**	**Dec**	**Mar**	**June**
Central Bank					
CBL rate	7.00	7.00	7.00	7.00	7.00
T-Bill Rate - 91 days	6.69	6.64	6.58	6.57	6.42
Lombard Rate	10.69	10.64	10.58	10.57	10.42
Commercial Banks					
Call	1.82	1.19	1.19	1.19	1.19
Time:					
31 days	0.44	0.44	0.44	0.44	0.44
88 days	1.12	1.11	1.12	1.12	1.12
6 months	2.53	2.52	2.53	2.53	2.53
1 year	3.52	3.52	3.52	3.52	3.52
Savings	0.56	0.56	0.56	0.56	0.56
Prime	11.69	11.69	11.69	11.69	11.69
South Africa					
Repo	7.00	7.00	7.00	7.00	7.00
T-Bill Rate - 91 days	7.19	7.36	7.61	7.29	7.33
Marginal Lending Rate					
Prime	10.5	10.50	10.50	10.50	10.50

Source: Central Bank of Lesotho

Holding of Treasury Bills and T-Bill rates

The overall holding of treasury bills experienced a moderate declined of 0.06 per cent in the quarter under review, compared to a decline of 0.4 per cent observed in the first quarter of 2017. The major source of the decline was a reduced holding of treasury bills by the banking system of 0.09 per cent compared to a decrease of 5.71 per cent realized in the quarter ending March 2017. The 91 days yield rate declined by 2.4 per cent in the quarter under review after a decline of 0.15 per cent in the quarter ending March 2017.

Table 9: Holding of Bills and Yields *(Million Maloti)*

	2016				2017
	Jun	Sept	Dec	Mar	Jun
Treasury Bills	**598.39**	**601.59**	**606.36**	**603.87**	**603.52**
Banking System	393.49	387.23	395.20	372.64	372.32
Non-Bank Sector	204.9	214.36	211.16	231.24	231.19
Memorandum Item					
Yield Bills (91-days)	6.8	6.75	6.69	6.68	6.52

Source: Central Bank of Lesotho

Holding of Treasury Bonds and T-Bonds Rates

The holding of treasury bonds declined by 0.13 per cent in the quarter ending June 2017, relative to an increase of 2.45 per cent observed in the quarter ending March 2017. This decline was driven by a 0.65 per cent decline in the holding of treasury bonds by the non-bank sector despite a 0.18 per cent increase in the holdings of treasury bonds by the banking system.

Table 10: Holding of Bonds *(Million Maloti)*

	2016				2017
	Jun	Sept	Dec	Mar	Jun
Holding of Treasury Bonds	**681.85**	**714.50**	**734.50**	**752.50**	**751.50**
Banking System	472.19	469.48	466.00	471.29	472.12
Non-Bank Sector	209.65	245.03	268.50	281.21	279.39

Source: Central Bank of Lesotho

The holding of treasury bonds during the review period comprised the 7 year treasury bonds and the 10 year treasury bonds, with the maturity date ranging from 2017 to 2025.

Table 11: Treasury bonds Maturity Dates and Coupon

ISIN[1]	Maturity Date	Coupon rate	Tenure
LSOOOA1GZ7WO	2019/02/13	8.50	7 years
LS000A1Z8458	2022/10/11	8.00	7 years
LS000A1Z8466	2025/10/07	9.00	10 years
LS000A1GR838	2021/06/22	10.00	10 years

Source: Central Bank of Lesotho

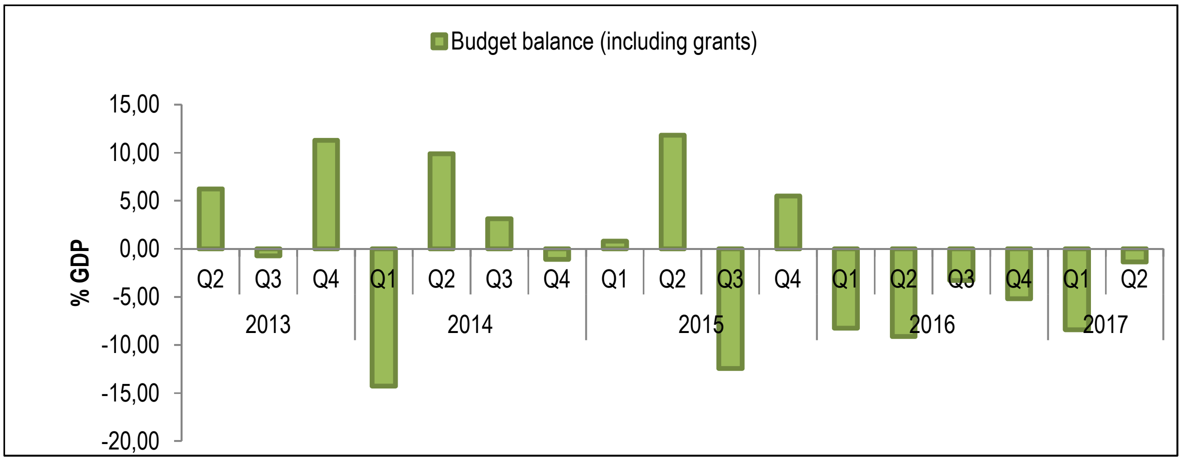
[1] International Securities Identification Number

5. Government Finance

OVERVIEW

The Government budget operations[2] registered the smallest deficit in four years equivalent to 1.4 per cent of GDP during the quarter ending in June, 2017 compared to the revised deficit of 8.4 per cent in the quarter ending in March, 2017. Apart from high expenditures, the main drivers of this deficit during the quarter under review included a significant decline in tax revenues following a one-off annual receipt of Rand Monetary compensation that was made in the previous quarter. The total revenue registered 38.6 per cent of GDP while the total outlays recorded 41.3 per cent. Furthermore, the public debt stock recorded 35.2 per cent of GDP during the quarter under review compared to the revised 34.9 per cent in the first quarter of 2017. The exchange rate effect, among other factors, contributed to the rise in the debt-to-GDP ratio.

Figure 13: Fiscal Balance *(Per cent of GDP)*

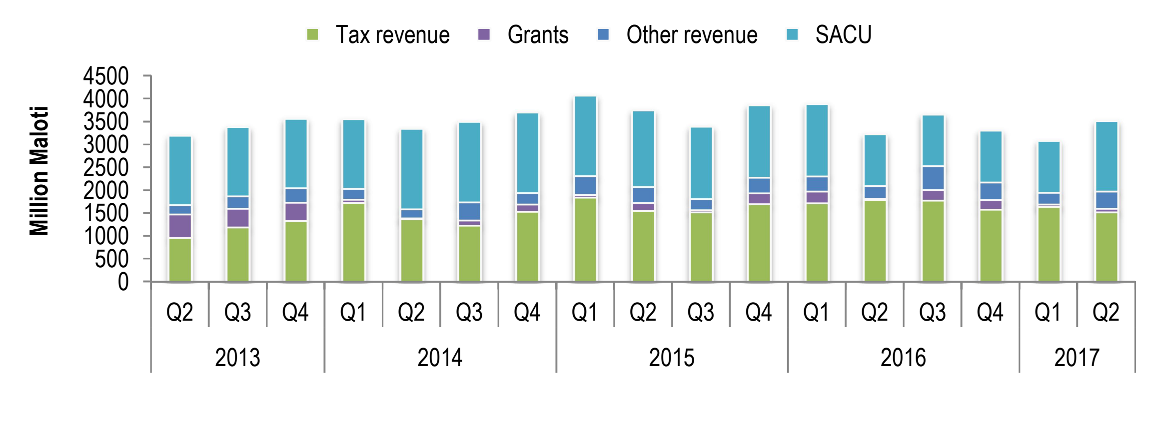


Source: Central Bank of Lesotho (CBL) and Ministry of Finance (MOF)

REVENUE

The The revenue increased by 14.0 per cent during the review quarter relative to 6.8 per cent decline in the first quarter of 2017. The main contributing factors included SACU receipts, value-added tax, LHWP water royalties, and a marginal increase on income taxes. The positive projections for 2017 economic growth in some SACU member states, contributed to higher estimates on SACU revenue collection. As such, Lesotho quarterly share has increased by 17.4 per cent of GDP during the current review quarter - the first fiscal quarter of 2017/2018. The improvements in domestic economy also contributed to the observed boost in certain tax revenues collection albeit business environment weakened. Furthermore, the rise in the LHDA water royalties was due to the delayed receipts in the previous quarter.

Figure 14: Total Revenue *(Million Maloti)*



Source: CBL and MOF

TOTAL EXPENDITURE

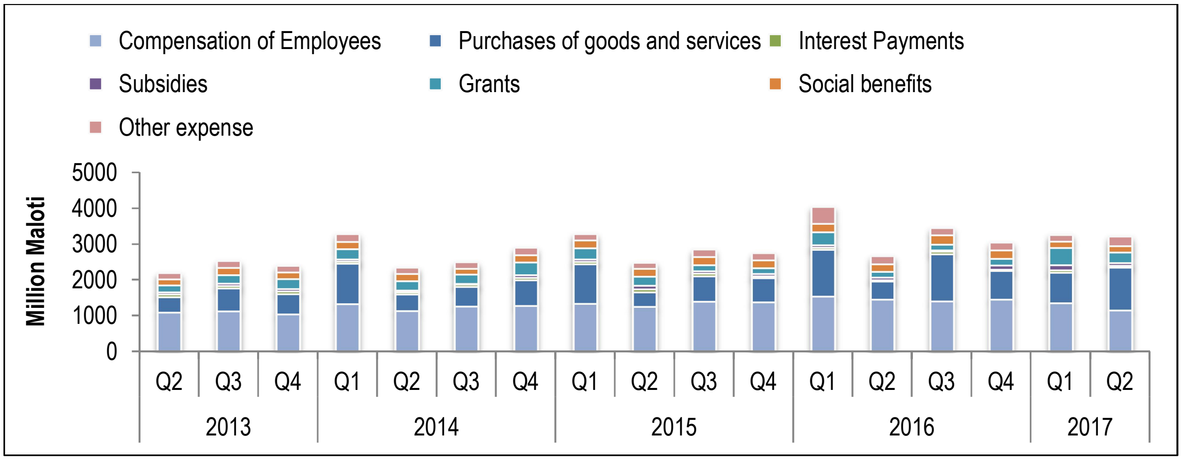
The Government spending (expenses and nonfinancial assets) decreased by 5.0 per cent during the quarter ending June, 2017 compared to the revised rise of 2.9 per cent in the previous quarter. Apart from the late presentation of 2017/2018[3] Budget Speech in July, 2017 and hence the release of 2017/2018 Appropriation Act, the reason for the decline in expense or recurrent spending was also attributable to the decline in compensation of employees, particularly the wages and salaries. This development was at the back of the implementation of the Government's wage bill management strategies coupled with biometric registration of public servants.

Moreover, a fall was also experienced under interest payments, subsidies, grants, and social benefits. In respect of interest payments, lower payment for Metolong Dam financing compared to the previous quarter resulted in the lower interest payment. The foreign interest payments on Metolong dam usually account for more than half of the total foreign interest payments. Although, other components of expense increased significantly such as 'purchases of goods and services' and 'other expense', this did not over shadow the fall in other components of government spending.

In terms of non-financial assets (or capital expenditure), the spending decreased by 25.0 per cent during the review quarter compared with the revised fall of 12.5 per cent in the previous quarter. Thus, the review quarter ended without the release of the 2017/2018 Appropriation Act, hence the delay for implementation of some projects which were Government-financed. The capital budget spending during this current quarter included payments made on 'purchases of vehicles' and 'other transport machinery' by different Ministries, and, roads and dam construction projects under Metolong Dam Authority and Roads Directorate.

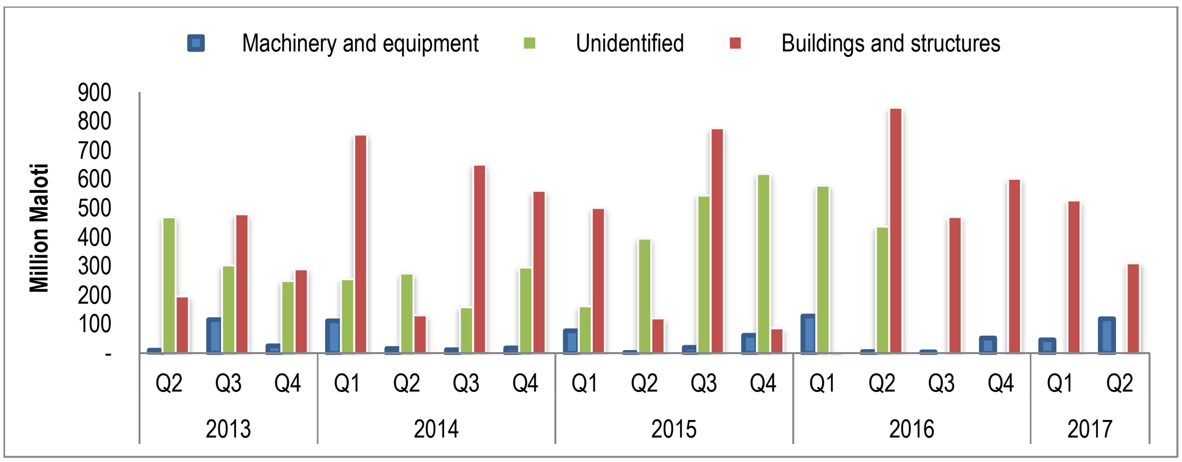
[3] The fiscal year starts from April to March

Figure 15: Total Expense *(Million Maloti)*



Source: CBL and MOF

Figure 16: Total Non-financial assets or Capital expenditure *(Million Maloti)*



Source: CBL and MOF

Table 12: Statement of Sources and Uses of Cash *(Million Maloti)*

	2016			2017		Q-to-Q	GDP
	Q2	Q3	Q4	Q1	Q2	(%)	(%)
Total Revenue	**3,227.87**	**3,657.79**	**3,306.33**	**3,081.64**	**3,514.18**	**14.0**	**39.7**
Tax revenue	1,794.41	1,782.59	1,582.53	1,642.74	1,527.86	-7.0	17.2
Grants	27.16	228.20	209.55	56.66	74.72	31.9	0.8
Other revenue	276.56	517.27	384.51	252.50	373.05	47.7	4.2
SACU receipts	1,129.74	1,129.74	1,129.74	1,129.74	1,538.55	36.2	17.4
Total Expense	**2,660.38**	**3,441.53**	**3,061.56**	**3,252.53**	**3,204.55**	**-1.5**	**36.2**
Compensation of Employees	1,442.08	1,399.57	1,449.11	1,346.24	1,138.74	-15.4	12.9
Purchases of goods and services	510.41	1,312.40	796.58	849.71	1,203.29	41.6	13.6
Interest Payments	29.57	72.13	35.41	67.17	48.64	-27.6	0.5
Subsidies	83.53	39.96	117.24	140.50	77.66	-44.7	0.9
Grants	156.48	158.84	187.39	481.52	296.70	-38.4	3.3
Social benefits	208.49	255.33	238.57	182.08	171.94	-5.6	1.9
Other expense	229.81	203.29	216.03	185.31	267.57	44.4	3.0
Net Cash Inflow From Operating Activities	**567.49**	**216.26**	**244.78**	**-170.89**	**309.63**	**-**	**3.5**
Total Nonfinancial Assets	**1,290.59**	**475.53**	**654.90**	**573.10**	**429.97**	**-25.0**	**4.9**
Fixed Assets	1,290.59	475.53	654.90	573.10	429.97	-25.0	4.9
Non-Produced Assets	0.00	0.00	0.00	0.00	0.00	0.0	0.0
Cash deficit(-)/surplus(+)	**-723.10**	**-259.26**	**-410.12**	**-743.99**	**-120.34**	**-**	**-1.4**
Net Cash Inflow From Financing Activities	**625.43**	**534.59**	**254.63**	**1,246.12**	**33.85**	**-**	**0.4**
Net Acquisition of Financial assets	469.98	556.61	337.38	1,249.65	60.60	-	0.7
Net Incurrence of Liabilities	155.45	-22.02	-82.75	-3.53	-26.74	-	-0.3
Statistical Discrepancy	-97.67	275.32	-155.49	502.13	-86.48	-	-1.0
Memo Item							
Total Expenditure	3,950.97	3,917.06	3,716.46	3,825.63	3,634.52	-5.0	-0.4

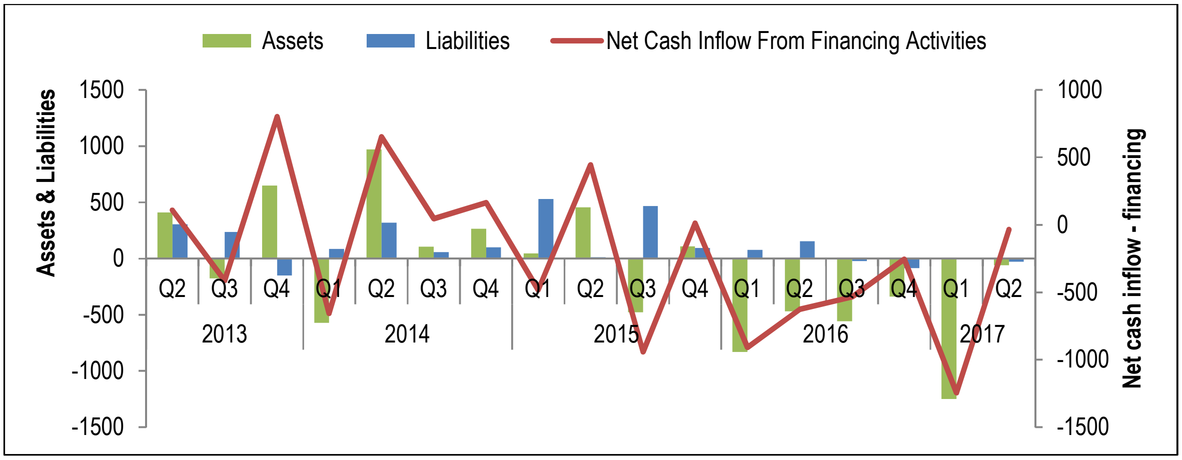
Source: CBL and MOF

FINANCIAL ASSETS AND LIABILITIES

The Government holding of financial assets and liabilities (on net basis) declined by M33.85 million in the quarter ending in June, 2017 compared to a significant decline of M1.25 billion in the first quarter of 2017. This was attributable to, among others, a fall in the deposits (net acquisition of assets) of the Government within the Central Bank to the tune of M108.73 million, coupled with M45.19 million fall in the foreign loans (net incurrence of liabilities).

Out of the list of debt instruments, the foreign loans in particular, recorded disbursements amounting to M30.01 million while their amortisation registered M75.20 million. The disbursing projects included: social assistance project, Metolong dam for potable water, second private sector competitiveness and economic diversification, and smallholder agricultural development.

Figure 17: Net Cash Inflow from Financing Activities *(Million Maloti)*

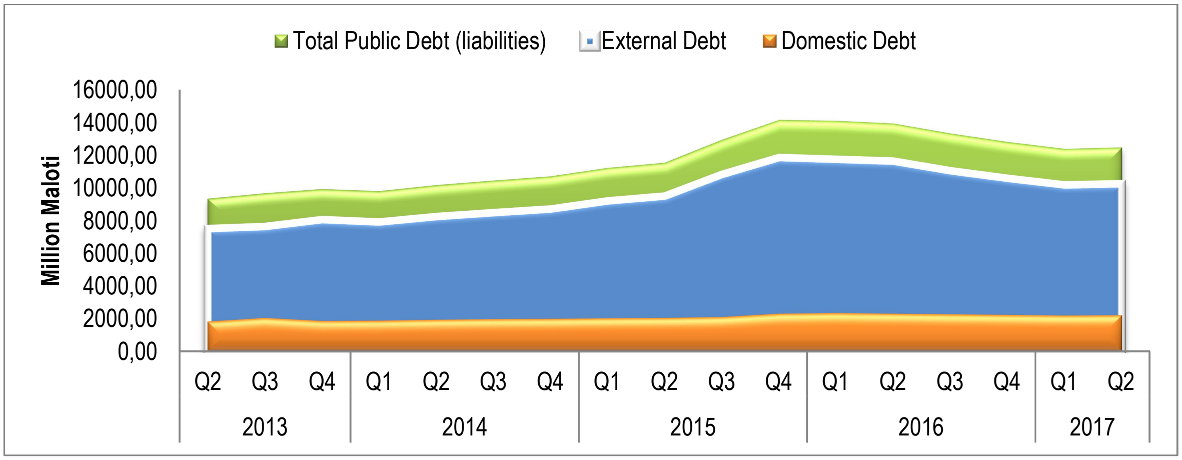


Source: CBL and MOF

TOTAL PUBLIC DEBT

The stock of public debt increased marginally to the tune of M12.48 billion during the quarter ending in June, 2017 from M12.38 billion in the quarter ending in March, 2017. In percentage terms, it increased by 0.8 per cent during the quarter under review compared with revised fall of 3.4 per cent in the previous quarter. The external and domestic debt instruments contributed to the rise in the public debt stock. In particular, the external loans funded by multilateral creditors (International Development Association arm of the World Bank, and EIB) contributed to the rise in public debt stock. The reason for the increase was attributable to marginal disbursements coupled with the exchange rate depreciation in which external loans are denominated.

Figure 18: Outstanding Public Debt *(Million Maloti)*



Source: CBL and MOF

Table 13: Public Debt Stock *(Million Maloti)*

			2016		2017	Debt / GDP (%)	
	Q2	Q3	Q4	Q1	Q2	Q1	Q2
TOTAL PUBLIC DEBT	**13,937.68**	**13,334.34**	**12,817.40**	**12,378.33**	**12,477.71**	**34.93**	**35.21**
EXTERNAL DEBT	**11,645.31**	**11,067.75**	**10,595.31**	**10,183.95**	**10,264.88**	**28.74**	**28.97**
Bilateral Loans	1,087.30	1,010.67	972.95	905.47	926.89	2.56	2.62
Concessional	1,087.30	1,010.67	972.95	905.47	926.89	2.56	2.62
Non-concessional	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Multilateral Loans	9,682.59	9,257.71	8,858.92	8,556.44	8,602.36	24.15	24.27
Concessional	7,999.57	7,588.43	7,205.93	6,912.31	6,953.57	19.51	19.62
Non-concessional	1,683.01	1,669.28	1,652.99	1,644.13	1,648.80	4.64	4.65
Financial Institutions	0.64	0.60	0.60	0.60	0.54	0.00	0.00
Concessional	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Non-concessional	0.64	0.60	0.60	0.60	0.54	0.00	0.00
Suppliers' Credit	874.78	798.76	762.83	721.44	735.09	2.04	2.07
DOMESTIC DEBT	**2,292.38**	**2,266.59**	**2,222.09**	**2,194.38**	**2,212.82**	**6.19**	**6.24**
Banks	1,877.82	1,807.20	1,742.43	1,681.93	1,702.24	4.75	4.80
Long-term	1,484.33	1,419.87	1,347.23	1,309.24	1,329.78	3.69	3.75
Treasury bonds	472.53	469.87	466.39	471.68	472.51	1.33	1.33
Central Bank (IMF-ECF)	1,011.80	950.00	880.84	837.56	857.28	2.36	2.42
Short-term (t-bills)	393.49	387.34	395.20	372.69	372.46	1.05	1.05
Non-bank	414.55	459.38	479.66	512.45	510.58	1.45	1.44
Short-term (t-bills)	204.90	214.36	211.16	231.24	231.20	0.65	0.65
Long-term (t-bonds)	209.65	245.02	268.50	281.21	279.39	0.79	0.79

Source: CBL and MOF

6. Foreign Trade and Payments

OVERVIEW

Lesotho continued to be a net borrower from the rest of the world, although at the lower rate compared with the previous quarter. The observed performance was attributed to the narrowing of current account deficit together with a decline of the deficit in the financial account. The contraction in the current account deficit largely emanated from the improvements in the primary and secondary income accounts during the review quarter. The slightly improved performance of the financial account was driven by lower reduction in the official reserves as well as a drawdown in commercial banks' foreign assets during the period. As a result, the overall balance registered a deficit equivalent to 2.6 per cent of GDP in the quarter ending in June 2017, lower than 3.4 per cent of GDP in the quarter ending in March 2017.

CURRENT ACCOUNT

The deficit in the current account balance narrowed for the second consecutive quarter during the review period. The deficit contracted by 4.8 per cent during the review quarter, compared with a fall of 7.5 per cent in the previous quarter. The decline in the deficit was largely driven by an increase in the primary and secondary income account balances. However, the expansion in trade account deficit moderated the improvement in the current account during the period. An increase in the trade account deficit resulted largely from the escalation in merchandise imports which take the largest share in trade account, despite an improvement in the merchandise exports during the quarter. The observed deficit in the trade account was also driven by a rise in the services account deficit during the review quarter. Relative to GDP, the current account balance registered a deficit of 8.2 per cent in the review quarter, lower than a deficit of 8.6 per cent in the previous quarter.

Table 14: **Current Account Balance** *(Million Maloti)*

	2016			2017		% Changes	
	Q2	Q3	Q4	Q1*	Q2+	Q/Q	Y/Y
Current Account	**-592.93**	**-651.34**	**-827.68**	**-765.28**	**-725.18**	**-4.8**	**15.8**
(a) Goods	-2361.07	-2665.16	-2552.37	-2733.50	-2883.52	**5.9**	**16.4**
Merchandise exports, f.o.b.	3342.49	3264.99	3104.90	2953.31	3335.20	**12.3**	**-0.2**
Of which diamonds	974.21	647.19	576.25	870.27	1176.54	**53.1**	**20.6**
Of which textiles & clothing	1675.13	1853.02	1797.59	1462.67	1469.87	**0.4**	**-13.8**
Of which re-exports	21.17	56.93	25.07	14.15	13.41	**-3.0**	**-14.7**
Other exports	671.98	707.85	705.99	606.22	675.38	**9.8**	**0.5**
Merchandise imports, f.o.b.	5703.56	5930.15	5657.27	5686.81	6218.72	**9.4**	**8.0**
(b) Services	**-970.78**	**-673.22**	**-988.33**	**-958.54**	**-1121.59**	**16.5**	**15.4**
(c) Primary Income	**1128.09**	**1111.06**	**1106.23**	**1076.05**	**1226.75**	**13.6**	**9.3**
(d) Secondary Income	**1610.84**	**1575.98**	**1606.80**	**1850.71**	**2053.19**	**12.6**	**19.6**

+ Preliminary Estimates
** Revised Estimates*
Source: Central Bank of Lesotho

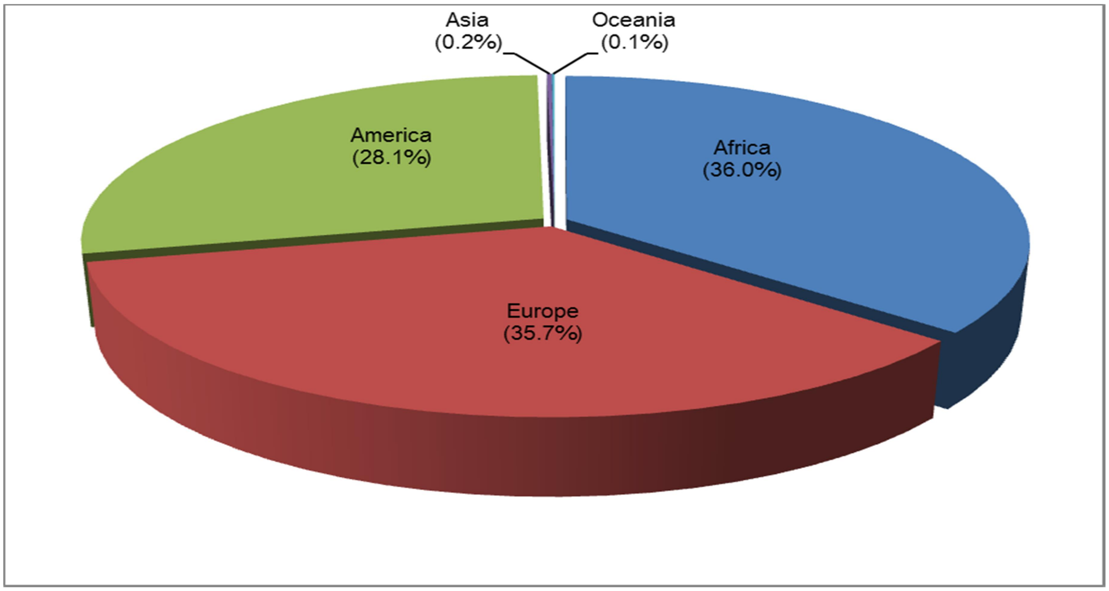
Merchandise Exports

During the second quarter of 2017, the value of merchandise exports increased by 12.3 per cent, higher than a rise of 0.7 per cent realised in the first quarter of 2017. The growth in merchandise exports emanated mainly from increased diamond exports during the review quarter. Diamond exports rose by 53.1 per cent during the quarter, following an escalation of 51.0 per cent in the preceding quarter. The improvement in diamond exports was supported by increased diamond production together with favourable prices in the global diamond market. The observed performance of merchandise export also benefitted from increased water exports to SA during the quarter. In addition, the largest component in merchandise exports which is textiles and clothing rose marginally by 0.4 per cent in the review quarter, recovering from 18.6 per cent decline in the previous quarter. On the year by year basis, merchandise exports contracted by 0.2 per cent in the second quarter of 2017, compared with 3.0 per cent decline in the first quarter of 2017. Relative to GDP, merchandise exports registered 37.6 per cent in the quarter under review, higher than 33.3 per cent of GDP in the previous quarter.

Direction of Trade - Exports

The African market, particularly the SACU region was the largest destination of Lesotho's exports in the review quarter. It absorbed 36.0 per cent of the total exports during the quarter compared with 26.4 per cent in the previous quarter. The second largest recipient of Lesotho's goods was the European market where a large portion of Lesotho's rough diamond is destined. It recorded a share of 35.7 per cent of the total exports in the review period, following a share of 35.6 per cent in the previous quarter. The North American market, particularly US became the third destination of Lesotho's exports with a share of 28.1 per cent of the total exports compared with a share of 37.7 per cent in the preceding quarter. This is where a large portion of textiles and clothing, about 63 per cent of the total textiles and clothing, is destined. Asia and Oceania markets continued to account for the smallest share of Lesotho's exports, with the shares of 0.2 and 0.1per cent respectively.

Figure 19: Direction of Merchandise Exports *(Percentage Share)*



Source: Central Bank of Lesotho

Merchandise Imports

The value of merchandise imports surged by 9.4 per cent during the quarter ending in June 2017, compared to an increase of 1.4 per cent in the preceding quarter. The growth was largely driven by a substantial rise in imports of iron and steel products from SA. The rise in merchandise imports mirrored an improvement in domestic economic activity during the period. On an annual basis, merchandise imports rose by 9.0 per cent during the review quarter, in contrast with a decline of 11.2 per cent in the previous quarter. As a percentage of GDP, the value of merchandised imports constituted 70.2 per cent in the second quarter of 2017, increasing from 64.2 per cent in the first quarter.

Services

Lesotho continued to be a net importer of services during the quarter under review. The payments for services acquired abroad increased by 16.5 per cent, equivalent to 12.7 per cent of GDP during the quarter under review, compared with a 3.0 per cent decline or 10.8 per cent of GDP in the previous quarter. The increase in services was driven largely by the growth in payments for air transport services and freight and insurance services on imported goods. On an annual basis, the net services grew by 15.4 per cent during the quarter under review, against a 2.0 per cent fall in the previous quarter.

Primary Income

The primary income account registered a 13.6 per cent rise in surplus during the review quarter, in contrast with a fall of 2.7 per cent in the previous quarter. The escalation in income was largely influenced by an increase in inflows from returns on portfolio investments abroad by both the Central Bank and commercial banks. Moreover, the growth in income account was supported by increased receipts from SA government for maintenance of the dams constructed under the Lesotho Highlands Water Project. On an annual basis, the primary income account increased by 13.6 per cent during the review quarter, following a decline of 2.7 per cent in the preceding quarter. Relative to GDP, the primary income constituted 13.8 per cent in the second quarter of 2017, after registering a 12.1 per cent in the previous quarter.

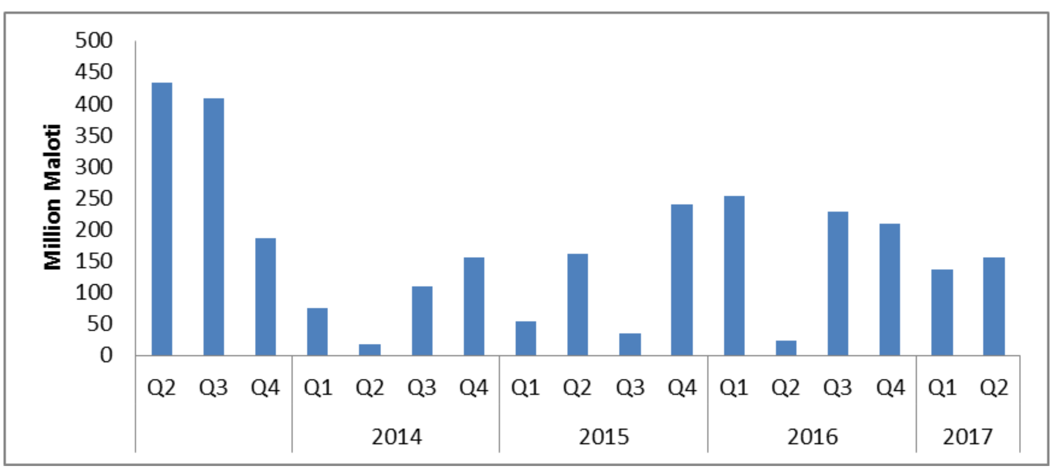
Secondary Income

The secondary income account improved in the second quarter of 2017. It grew by 12.6 per cent in the quarter ending in June 2017, following an increase of 15.2 per cent in the quarter ending in March 2017. This was at the back of a 36.2 per cent rise in SACU receipts during the review period. The increase in income account also emanated from receipts of donor grants to support the government budget in the second quarter of 2017. The secondary income registered 23.2 per cent of GDP in the first quarter of 2017 compared with 20.9 per cent of GDP recorded in the second quarter of 2017. On an annual basis, the secondary income account rose by 27.4 per cent in the review quarter, compared with a fall of 18.0 per cent in the previous quarter.

CAPITAL ACCOUNT

During the second quarter of 2017, inflows in the capital account rose by 13.2 per cent, equivalent to 1.8 per cent of GDP in contrast with a decline of 34.5 per cent or 1.5 per cent of GDP in the first quarter of 2017. The increase in capital account was largely driven by a 31.9 per cent rise in receipts of foreign grants for financing of capital projects during the quarter, compared to a decline of 72.9 per cent in the previous quarter. The capital inflows for financing of Polihali dam remained relatively unchanged during the review quarter.

Figure 20: Capital Account *(Million Maloti)*

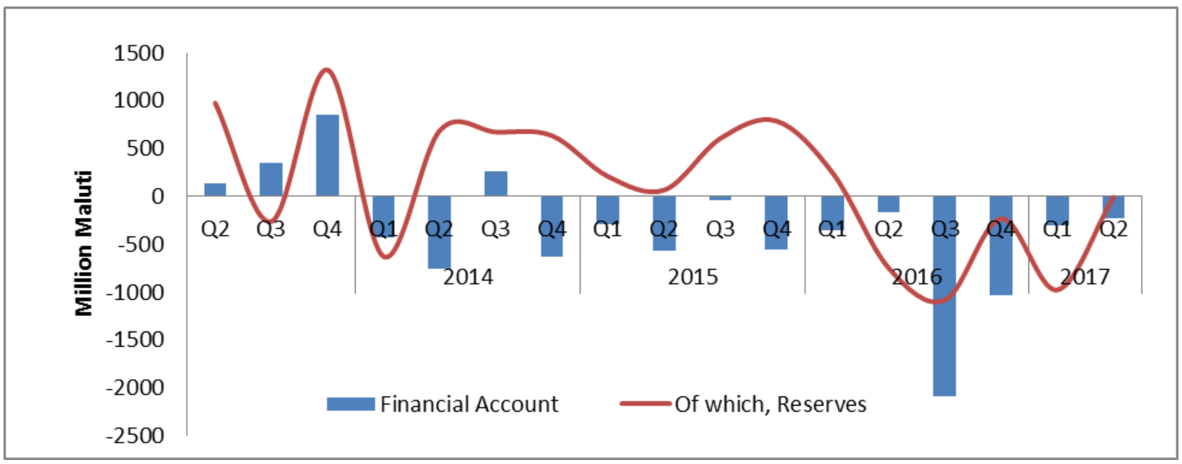


Source: Central Bank of Lesotho

FINANCIAL ACCOUNT

The net borrowing in the financial account narrowed to a deficit of 2.6 per cent of GDP in the second quarter of 2017, following a 3.4 per cent of GDP in the previous period. The observed performance was largely driven by slower reduction in reserve assets, while direct investments remained constant during the review quarter. The reduction in reserve assets recorded 0.1 per cent of GDP in the quarter under review compared with 11.0 per cent of GDP in the previous quarter. The deficit in the financial account was also driven by a reduction in commercial banks' foreign assets to finance imports of goods and services during the quarter. Commercial banks' foreign assets inflows registered 1.3 per cent of GDP in the quarter ending in June 2017, in contrast with an outflow equivalent to 8.2 per cent of GDP in the quarter ending in March 2017.

Figure 21: Financial Account *(Million Maloti)*

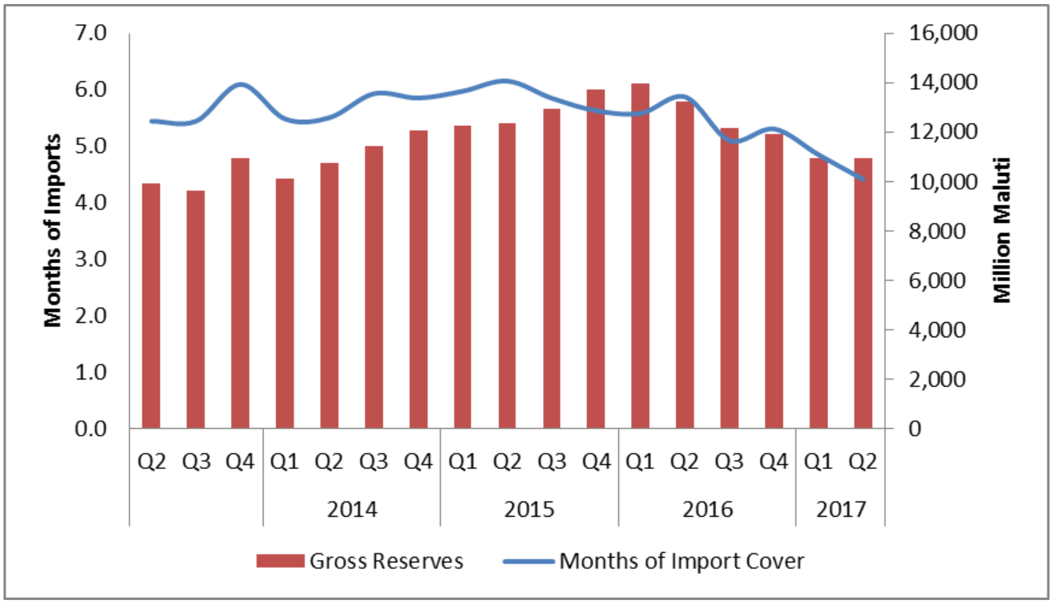


Source: Central Bank of Lesotho

RESERVE ASSETS

During the second quarter of 2017, the stock of international reserves decreased by 0.1 per cent to M10.9 billion compared with a decline of 8.2 per cent in the previous quarter. The deterioration in the reserve assets was underpinned by a reduction in government deposits albeit at a lower rate during the review period. In addition, an increase in payments for imports of goods and services contributed to the drop in reserves assets. Consequently, gross reserves measured in months of import cover declined to 4.4 months in the quarter ending in June 2017, from 4.9 months in the quarter ending in March 2017.

Figure 22: Reserves Assets



Source: Central Bank of Lesotho