



Economic Review

March 2012

Lesotho's Consumer Inflation: A Closer Look at the Numbers

Lesotho's inflation has evolved quite interestingly in recent months.....

Introduction

Inflation is an important indicator of the health of an economy. It is a measure of the general price level in an economy, which increases (decreases) when aggregate demand is greater (lower) than productive capacity/aggregate supply. Empirical evidence suggests that inflation has an adverse and possibly non-linear effect on long-run growth. Most of the empirical findings indicate that, on the one hand, when inflation is low, it has no significant effect on growth. On the other hand, when inflation is high ($\pi > 8.0\%$ per annum), it has a negative and statistically significant effect on growth. In addition, high inflation has been observed to have devastating social costs. That is why countries implement monetary policy to maintain price stability and keep inflation at low levels.

In Lesotho, price stability is maintained through the fixed exchange rate regime through which Lesotho's currency, the loti is pegged at par to the South African currency, the rand. The exchange rate peg results in lower inflation by constraining the scope for excessive monetary expansion. This can happen in various ways. It provides a highly

visible commitment, hence raises the political costs of imprudent monetary and fiscal policies. Credibility of the peg also enhances confidence in the domestic currency, thus increasing demand for the same, which reduces the inflationary consequences of a given expansion in money supply. In addition, the Central Bank of Lesotho (CBL) uses open-market operations to influence overall monetary and credit conditions by changing the supply and demand for liquidity. The CBL holds regular auctions of treasury bills (TBs) to influence the level of liquid reserves held by domestic commercial banks. Through the sale (purchase) of TBs, the CBL reduces (increases) liquidity in the financial system, hence money supply.

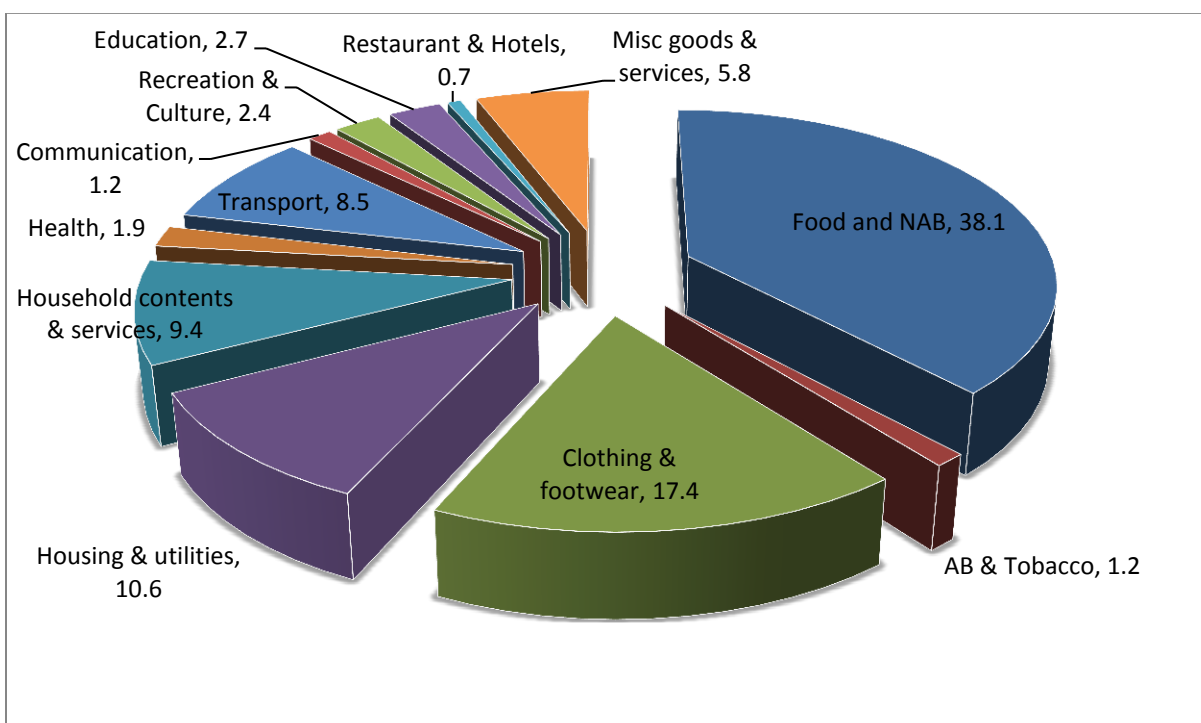
Lesotho's inflation has evolved quite interestingly in recent months. Thus it is important to understand the numbers and the factors behind their recent movements. This article is intended to take a closer look at Lesotho's consumer price index (CPI) numbers with a view to answer some of the questions that have arisen in relation to recent behavior of the CPI.

The Nature of Lesotho's Inflation and Recent Trends

The CPI is used to measure inflation in Lesotho. The Bureau of Statistics (BOS) in Lesotho collects prices of items forming a fixed basket of goods and services every month from twelve urban areas and forty five selected rural areas of Lesotho to calculate the CPI for a particular month. The different items in the basket are allocated weights, which were determined on the basis of Lesotho's 2002/03 Household Budget Survey (HBS). These weights reflect the average percentage of a typical

household's total spending that goes to a specific category of goods or services. As depicted by figure 1 below, on average, a typical Lesotho household devotes the highest percentage (38.1 per cent) of their total spending to food and non-alcoholic beverages (NAB) followed by clothing and food wear at 17.4 per cent and then housing and utilities at 10.6 per cent. All the other categories have weights of less than 10.0 per cent.

Figure 1: Lesotho's CPI Weights

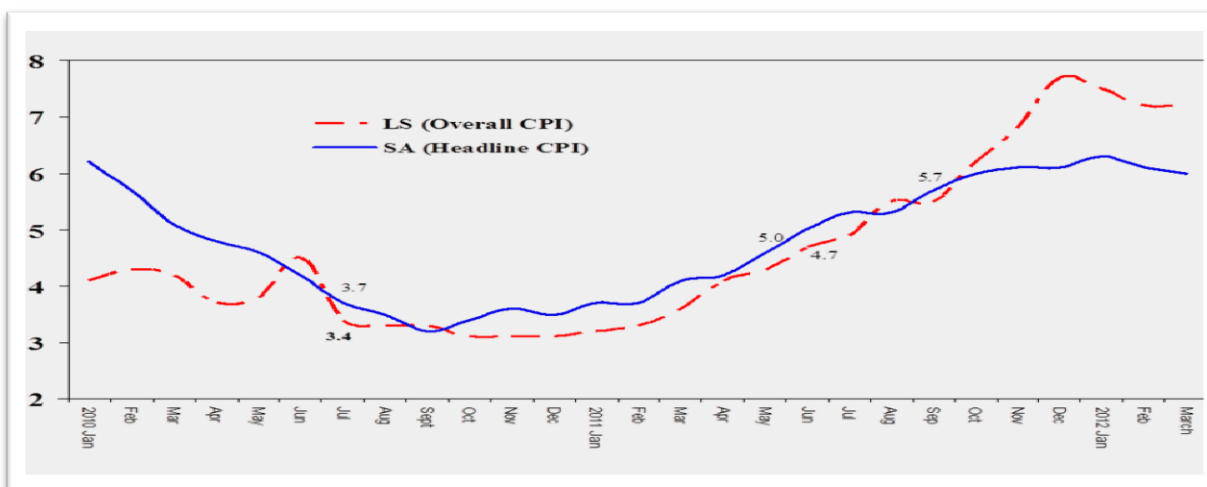


Source: Bureau of Statistics, Lesotho

Lesotho's inflation has increased significantly in recent months and reached its peak in the fourth quarter of 2011 after which it appeared to be retracting. After decelerating from the beginning of 2009 to the end of the third quarter of 2010, Lesotho's inflation rate reached a trough at 3.1 per cent in the fourth quarter of 2010.

Thereafter it went on an upward trajectory to a peak of 7.7 per cent in December 2011. Inflation started the new year with a deceleration, registering the rate of 7.5 per cent in January 2012, falling to 7.2 per cent in February 2012 and remaining at the same rate in the following month.

Figure 2: Lesotho and South Africa's Inflation Rates



Source: Lesotho CPI – Bureau of Statistics, SA CPI – Statistics South Africa

The rise in inflation since the fourth quarter of 2010 was reflected mainly in the food and NAB, clothing and footwear, housing and utilities (which includes gas and other household fuels), and the transport categories. The contribution of the food and NAB category increased from 1.2 percentage points in October 2010 to 2.9 percentage points in December 2011 and decreased to 2.7 percentage points in March 2012. This mainly reflected the upsurge in global food prices as explained

below. The contribution to inflation by the 'housing, utilities, gas and fuels' category increased from 30 basis points in October 2010 to 80 basis points in March 2012, primarily due to increases in the prices of gas and paraffin, which are fuels used by households to cook and heat homes. During the same period, the 'transport' category's contribution also rose from 30 basis points to 60 basis points as a result of petrol and diesel price increases.

Table 1: Contributions to CPI Inflation

	2011				2012		
	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Total	5.5	6.2	6.8	7.7	7.5	7.2	7.2
Of which:							
Food and NAB	2.1	2.4	2.6	2.9	2.9	2.7	2.7
AB & Tobacco	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Clothing & footwear	1.0	1.1	1.2	1.3	1.3	1.3	1.3
Housing, utilities, gas & fuels	0.6	0.7	0.7	0.8	0.8	0.8	0.8
Household contents & services	0.5	0.6	0.6	0.7	0.7	0.7	0.7
Health	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Transport	0.5	0.5	0.6	0.7	0.6	0.6	0.6
Communication	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Recreation & Culture	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Education	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Restaurant & Hotels	0.0	0.0	0.0	0.1	0.1	0.1	0.1
Misc goods & services	0.3	0.4	0.4	0.4	0.4	0.4	0.4

Source: Central Bank of Lesotho's Calculations

Factors that may have contributed to Recent Inflation Trends

Theory and empirical findings have identified a number of factors that determine inflation. Amongst them, the following are

believed to have contributed to movements in Lesotho's inflation during the period being reviewed by this article.

South Africa's Inflation

The strong dependency of Lesotho on imports from SA means that Lesotho also imports the bulk of its inflation from SA. In addition, the fixed exchange rate regime that Lesotho is operating under means that Lesotho borrows monetary policy hence inflation from SA. That is why as depicted in figure 2 above, Lesotho's inflation rate closely tracks that of SA, with strong deviations occurring only where

commodities that carry high weights in either of the two countries' CPI baskets exhibit very high or low inflation. Since the beginning of the fourth quarter of 2011, Lesotho's inflation rate had been rising faster than that of SA, mainly fuelled by rapid increases in food prices, which, as demonstrated in figure 1, carry the highest weight of 38.1 per cent in Lesotho's CPI basket.

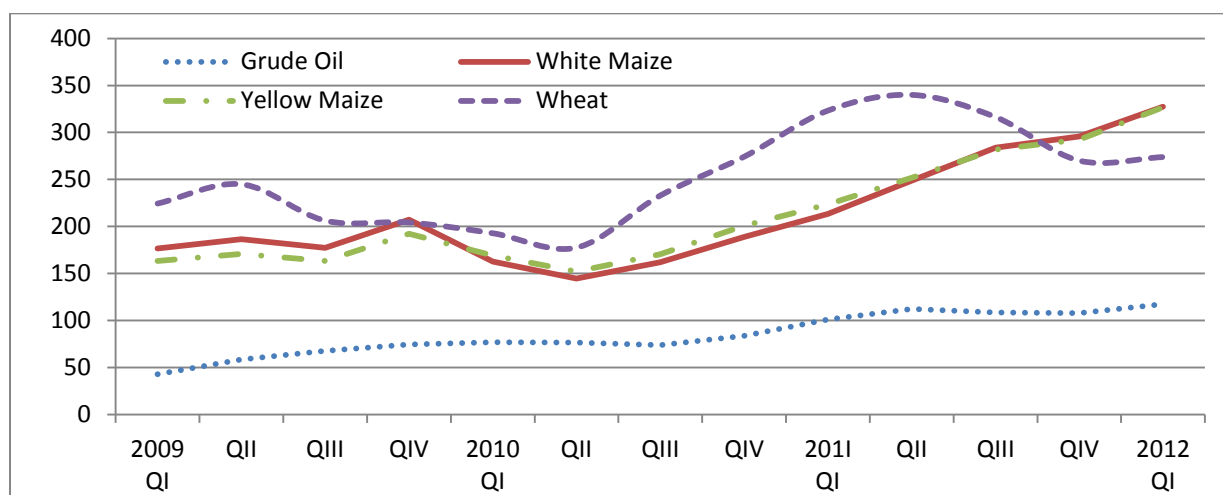
Commodity Prices (Food and Fuel)

Since their surge in late 2010, international food prices remained high in the first quarter of 2012. As depicted in figure 3 below, the prices of white and yellow maize continued on an upward trajectory while that of wheat declined during the first three months of 2012. At the global level the upsurge in maize prices was attributable to stronger import demand in Asia. Regionally, South Africa, the biggest maize producer on the African continent, was struggling with constricted maize stocks ahead of the next harvesting season in May 2012. Even though SA's harvest had increased in 2010/11 compared with the previous harvest period, SA had committed a lot of its maize produce to exports resulting in a deficit that had to be met with imports. Looking at the domestic situation, Lesotho's food produce was far lower than the requirement, thus increasing vulnerability to high international food prices as reliance on

imports increased. The international price of crude oil also rose in recent months on account of increased demand and concerns about supply disruptions.

The rise in the prices of these food commodities and of crude oil has the direct impact of pushing up the prices of their by-products. In addition, it may have the second round effects on other components of the CPI, especially goods and services in whose production these commodities or their by-products are used as inputs. Furthermore, when the increase in food and fuel prices is persistent, it creates expectations of rising inflation that could spill over into higher wage demands, hence higher underlying inflation. The inflationary impact of these commodities is most significant in economies where their share in the consumption basket is high, like food in the case of Lesotho.

Figure 3: Commodity Prices (Quarterly Averages in US\$ Terms)



Source: Bloomberg

Exchange Rate Developments

The loti strengthened against the major trading currencies during the first quarter of 2012, following depreciation in the previous two quarters. It appreciated by quarterly averages of 4.1%, 6.8% and 4.3% against the US Dollar, the Euro and Pound Sterling,

respectively. The appreciation of the loti is expected to have reduced the prices of imported goods and services, thus contributing to the deceleration in inflation during the first quarter of 2012.

Domestic Fiscal Policy

Fiscal policy can impact on inflation if money creation is used to finance government expenditure. Empirical observations indicate that when governments are faced with large fiscal deficits and investors are pessimistic about government's ability to honor its debts and hence are not willing to lend to government through buying bonds, governments may resort to seignorage. The Lesotho government's ability to print money and inflate the economy is limited by the fixed exchange rate regime that Lesotho is operating under. Fiscal indiscipline could result in a collapse of the exchange rate peg with devastating inflationary effects. The

Government of Lesotho had been pursuing fiscal prudence resulting in fiscal surpluses from 2003/04 to 2009/10. Fiscal deficits of 8.5 per cent of GDP and 4.5 per cent of GDP were recorded in 2010/11 and 2011/12, respectively, as a result of the decline in government revenue related to the recent global economic recession. However, fiscal consolidation measures were undertaken to contain expenditure and prevent the fiscal deficits from ballooning. Government budgetary operations recorded non-cumulative fiscal deficits of 4.9 per cent of GDP and 7.9 per cent of GDP in the fourth quarter of 2011 and first quarter of 2012, respectively.

World Development Report (WDR) 2012: Gender Equality and Development: Implications for Lesotho's Economy

The World Bank recognizes the role of gender equality and women empowerment for poverty reduction and development effectiveness.....

Introduction

Promoting gender equality and empowering women is one of the Millennium Development Goals (MDGs) set out by the United Nations and forms part of the development and public policy agenda in many countries around the globe. As part of the global initiative towards development, the World Bank publishes the 'World Development Report' every year. This year's theme is "Gender Equality and Development". The report emphasises the feedback link between gender equality and economic development by noting that economic growth is good for equal rights and opportunities and that gender equity, in turn, is an important stimulant of high productivity and market growth, necessary for economic development.

According to the 2012 WDR, the process towards reducing gender disparities in all areas of life: education, health, and other economic processes is an issue of many decades. Some progress has been made in promoting gender equality. Nonetheless, a number of challenges were experienced and not all gaps between men and women have been reduced.

The article reviews recent global trends in gender equality. It highlights dimensions in which Lesotho has succeeded or failed to make progress and assesses the implications of Lesotho's progress.

Review of Recent Global Trends in Gender Inequality

The WDR 2012 outlines patterns and trends of gender equality and identifies gaps that exist despite the progress achieved over the past three decades. Commendable progress has been achieved in educational attainment, health and survival and economic participation. Nonetheless, it has not been uniform across all countries and in other spheres of life gaps still emerge that need rigorous attention and action.

In terms of educational attainment, the average years of schooling for women relative to men in the developing countries increased from 0.56 in 1980 to 0.86 in 2010. Other indicators of

educational attainment also show relatively greater progress in this area. For example, there are considerable gains even in regions with largest gender gaps- South Asia and Sub-Saharan Africa-(SSA), in particular West Africa. In the period between 1999 and 2008, the number of girls in primary schools in SSA increased from 85 girls for every 100 boys to 91 girls for every 100 boys. In roughly 45 developing countries, including Lesotho, the number of girls was greater than the number of boys in secondary education. In terms of tertiary education, enrolment growth has also been commendable for women relative to men across the globe.

Gender equality has also improved in the health and survival dimension in the last five decades. In most regions in the world, women live longer than men and while the gap is still rising in some regions, it is stabilising in others. For example in low-income countries, the ratio of life expectancy of women relative to men rose from 1.04 in 1960 to 1.06 in 2008, on average. However, in SSA countries, HIV/AIDS has shrunk gains in life expectancy for women relative to men, especially in countries like Botswana.

In terms of economic participation, the number of women relative to men in the labour market has increased markedly

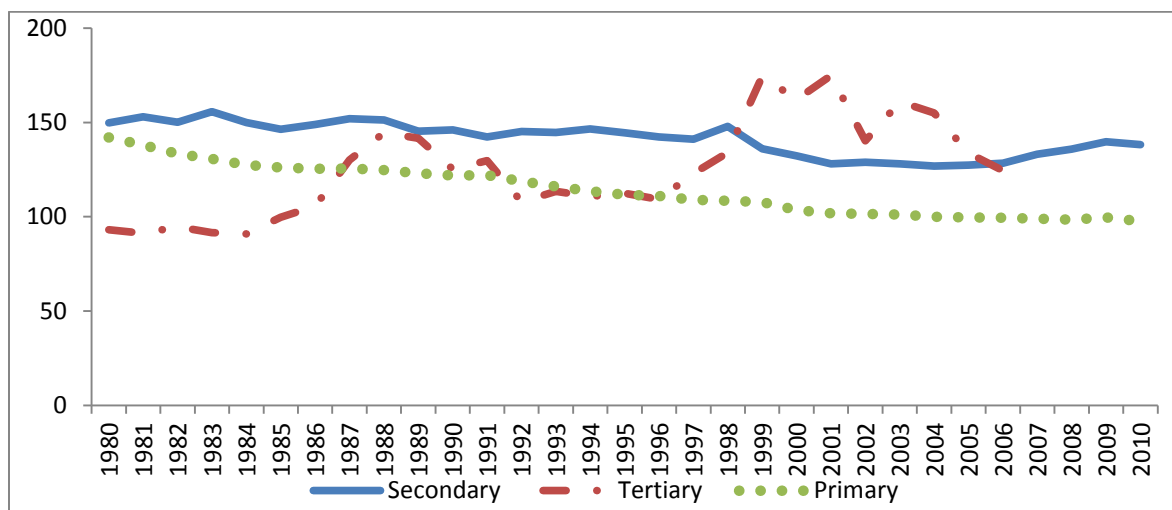
over the past three decades. The gender gap in the labour market narrowed from around 32.0 percentage points in 1980 to 26.0 percentage points in 2008. Women labour force participation rates exceed 50.0 per cent in SSA, East Asia and the Pacific, Europe, Central Asia, and Latin America and the Caribbean. Driving these trends has been the combined effects of economic development, declining fertility rates and rising education standards among women. Moreover, greater openness to trade and economic integration have stimulated the growth of the export-oriented sectors such as manufacturing (garments). This has attracted a lot of women into the workforce across the globe.

Gender Equality in Lesotho

Lesotho's performance in gender equity is high compared to other countries in Southern Africa such as South Africa. In terms of educational attainment at primary and secondary school levels enrolment for women relative to men remained high though it has been declining over the years. However, the ratio of female enrolment relative to male enrolment in tertiary education has been

increasing during the same period. Regarding primary school enrolment, the percentage of women relative to men was 142.1 per cent in 1980 and fell to 97.6 per cent in 2010 (figure 4 below). Moreover, the secondary enrolment ratio of female-to-male declined from 149.7 per cent in 1980 to 138.2 per cent in 2010.

Figure 4: The Ratio of Female School Enrolment in Education (Primary, Secondary and Tertiary)



Source: World Bank, World Development Indicators 2012

Nonetheless, the tertiary enrolment ratio of women relative to men increased by 31.4 percentage points from 1980 to 2006 (figure 4 above). The percentage of women relative to men enrolled at universities and colleges across the country increased from below 100.0 per cent in 1980 and to around 142.0 per cent in 1988. It declined to just above 110.0 per cent in 1992 and increased again to around 170.0 per cent in the early 2000s. Even though it retreated to around 130.0 per cent in 2006, it still remained high compared to the early 1980s and 1990s.

In terms of the health and survival dimension, there was an improvement in life expectancy for both men and women between 1980 and 1992. The number of years a female person could live during this period increased from 55 to 61 years while for males it increased from 55 years in 1980 to 58 years in 1992. However, from 1993 to 2002 life expectancy of women declined by 9 years relative to a decline of 6 years for men. The decline in women's life

expectancy was due to high maternal deaths.

The growth of economic opportunities has drawn more women and men into the labour market across the country but women appear to have benefited more. Between 1990 and 1999, the ratio of female to male labour force participation increased from 80.9 per cent to 85.0 per cent, but it declined thereafter to around 80.5 per cent in 2010.

Differences in participation rates still exist in terms of the distribution of men and women across industries and occupation. For example, there are more women than men in the manufacturing sector and the number of women relative to men is increasing in the services sector. Moreover, the number of seats occupied by women in parliament and national government seats has been increasing. For example, the percentage of women in national parliament was 4.6 per cent in 1997 and it increased to 24.2 per cent in 2010.

Conclusion

Improvements in women's education and health have been linked to better outcomes for their children in a number of countries. The high participation of women in education in Lesotho increases their chances of participating in formal salaried employment thus giving them greater control over household resources. This augurs well for children's education and health, which are foundations for children to have good futures, good careers that would enhance their contribution to economic growth and development. The low life expectancy of

women offsets this and should be addressed.

The increased number of women in Lesotho's parliament implies an increase in women's representation in policy making. This is expected to result in an improvement in the formulation and implementation of policies that improve the lives of women and their households and increase in the provision of public goods that matter more to women, such as water and sanitation.