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Probable date of presentation to the Committee on Operations and Development Effectiveness (CODE)

25 February 2020

FOR CONSIDERATION

MEMORANDUM

TO : THE BOARDS OF DIRECTORS

FROM : Vincent O. NMEHIELLE
Secretary General

SUBJECT : LESOTHO: COUNTRY STRATEGY PAPER 2020-2024 *

Please find attached the above-mentioned document.

Attach:

Cc: The President

*** Questions on this document should be referred to:**

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AFRICAN DEVELOPMENT BANK

AFRICAN DEVELOPMENT FUND

KINGDOM OF LESOTHO

COUNTRY STRATEGY PAPER 2020-2024

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REGIONAL DIRECTORATE GENERAL – SOUTH
January 2020

AFRICAN DEVELOPMENT BANK GROUP

LESOTHO

COUNTRY STRATEGY PAPER 2020-2024

RDGS

January 2020

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CURRENCY EQUIVALENTS

Currency		=	Lesotho Maloti (LSL)	
UA	1.00	=	1.36834	USD
UA	1.00	=	1.23989	EUR
UA	1.00	=	20.85380	LSL
USD	1.00	=	15.24022	LSL

As of December 2019

WEIGHTS AND MEASURES

Metric System

GOVERNMENT FISCAL YEAR

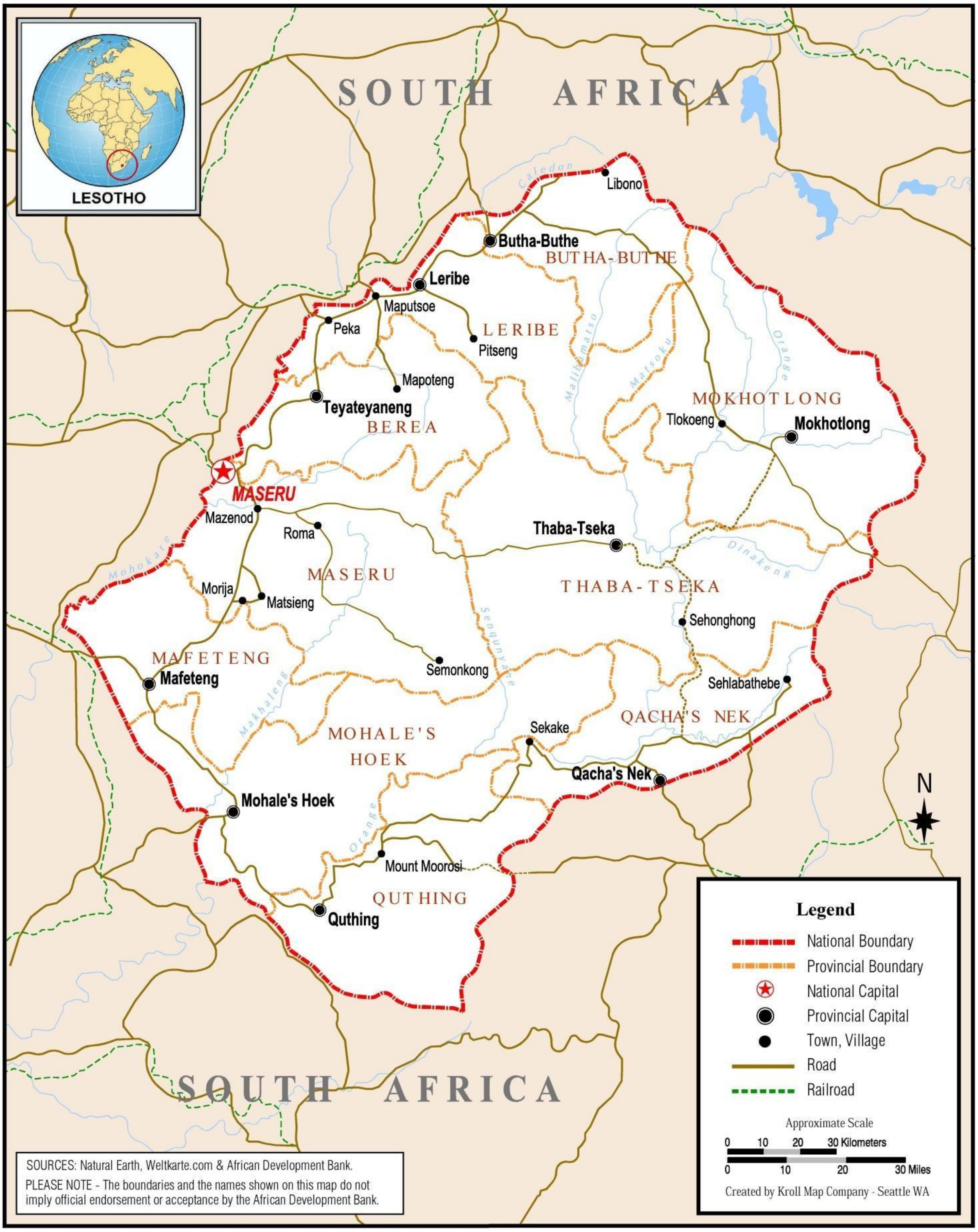
April 1- March 31

ACRONYMS AND ABBREVIATIONS

ABC	All Basotho Convention
ADB	African Development Bank (window)
ADF	African Development Fund (window)
ACFTA	African Continental Free Trade Area
AfDB	African Development Bank Group
AGOA	Africa Growth and Opportunity Act
ASYCUDA	Automated Systems for Customs Data
AU	African Union
CBoL	Central Bank of Lesotho
CMU	Cash Management Unit
CEDAW	Convention on the Elimination of All forms of Discrimination Against Women
CFTA	Continental Free Trade Area
CMA	Common Monetary Area
CODE	Committee on Operations and Development Effectiveness
CPI	Corruption Perception Index
CPIP	Country Portfolio Improvement Plan
CPPR	Country Portfolio Performance Review
CSP	Country Strategy Paper
CSOs	Civil Society Organizations
CR	Completion Report
DCEC	Directorate of Corruption and Economic Crimes
DP	Development Partners
DPG	Development Partners' Group
EAs	Executing Agencies
EDB	Ease of Doing Business
FY	Fiscal Year
GBV	Gender Based Violence
GCF	Global Climate Fund
GCR	Global Competitiveness Report
GDP	Gross Domestic Product
GHG	Green House Gas
HDI	Human Development Index
HIV/AIDS	Human Immunodeficiency Virus Infection & Acquired Immune Deficiency Syndrome
IFMIS	Integrated Financial Management Information System
ILP	Indicative Lending Program
ISPFM	Institutional Support for Public Financial Management
JfYA	Jobs for Youth in Africa
KoL	Kingdom of Lesotho
LEC	Lesotho Electricity Company
LEL	Lesotho Economic Laboratories
LHWP	Lesotho Highlands Water Project
LNBS	Lesotho National Broadcasting Services
LNDC	Lesotho National Development Corporation

MCC	Millennium Challenge Corporation
MDGs	Millennium Development Goals
MNCs	Multinational Corporations
MSEDMC	Ministry of Small Enterprise Development, Marketing, and Cooperatives
MSMEs	Micro, Small and Medium Scale Enterprises
NAPACC	National Adaptation Program of Action on Climate Change
NDC	Nationally Determined Contributions
NEC	National Executive Committee
NSDP	National Strategic Development Plan
NUL	National University of Lesotho
OAG	Office of the Auditor General
ODA	Official Development Assistance
PAC	Public Accounts Committee
PCR	Project Completion Report
PDAM	Public Debt and Aid Management
PEPFAR	President's Emergency Plan for AIDS Relief
PFM	Public Financial Management
PIR	Policy Interest Rate
PIUs	Program Implementation Units
PPAD	Procurement Policy and Advice Division
PPP	Public Private Partnership
RDGS	Regional Directorate General South
RBF	Results Based Framework
SACU	Southern African Customs Union
SADC	Southern Africa Development Community
SDGs	Sustainable Development Goals
SMMEs	Small, Micro & Medium Scale Enterprises
UA	Unit of Account
UNDAF	United Nations Development Assistance Framework
UNDP	United Nations Development Program
UNFPA	United Nations Population Fund
WB	World Bank

GENERAL MAP OF LESOTHO



EXECUTIVE SUMMARY

1. **The Country Strategy Paper (CSP) 2020-2024 provides a framework for Bank assistance to the Kingdom of Lesotho (KoL)**. It is anchored on the country's second National Strategic Development Plan (NSDP II) 2018/19-2022/23. The NSDP II pillars include i) Promoting Inclusive and Sustainable Economic Growth and Private Sector–led Job Creation; ii) Strengthening Human Capital (through developing human capabilities in Health, Education, Nutrition and Social Protection); iii) Building Enabling Infrastructure; and iv) Strengthening National Governance and Accountability Systems. The theme of NSDP II **is Employment and Inclusive Growth*:* In Pursuit of Economic and Institutional Transformation for Private Sector-led Jobs and Inclusive Growth.** The CSP is consistent with the objectives of the Bank's Ten-Year Strategy (TYS) 2013-2022 and the Bank's High 5s (Light Up and Power Africa, Feed Africa, Industrialize Africa, Integrate Africa and Improve the Quality of Life of the People of Africa). The CSP will support the KoL in its quest for private sector-driven broad based and inclusive growth as articulated in NSDP II.

2. **On the political front, the country's political stability and economic development generally are being challenged by a weak coalition and internal rivalry in the ruling party resulting in political uncertainty and undermining investor confidence.** As a result, Lesotho had to hold elections in June 2017 for the third time in a period of five years since 2012. This led to the formation of a four-party coalition government, led by Prime Minister Thomas Thabane. According to a review of the NSDP I, chronic political uncertainty and politicization of civil service management were some of the key factors that contributed to the sub-optimal implementation of NSDP I.

3. **Overall, the domestic growth outlook remains subdued due to heightened policy uncertainty at the global, regional and domestic levels.** This is reflected in the country's liquidity and fiscal challenges characterized by a huge wage bill (24% of GDP) and staggering payment arrears (USD76 million) thus undermining fiscal sustainability. Lesotho's GDP growth rate remains sluggish averaging 1.72% during the period 2014-2018. However, it is estimated to grow by 2.6% in 2019 owing to strong performance in the mining sector, and recovery of textiles and clothing in tandem with an increase in global demand. The projections are 1.8% and 1.7% in 2020 and 2021, respectively, depending on the performance of the South African economy and the trade war between the United States of America (USA) on one hand and China and European Union (EU) on the other hand.

4. **On account of the country's overarching development challenge which is the lack of structural transformation stemming from weak linkages between agriculture and industry**, lack of value addition, low agricultural productivity, huge infrastructural deficit and weak institutional capacity, the country finds itself at a crossroads needing new drivers of growth, a more streamlined role for the state, and a dynamic private sector to help it seize opportunities in regional and global markets. The country, therefore, needs continued Bank assistance to enhance macroeconomic stability while at the same time positioning itself to take advantage of potential regional opportunities from Southern African Development Community (SADC) and Continental Free Trade Area (CFTA). The Bank's support as a catalyst, convener, connector, and financier will absolutely be crucial in the implementation of NSDP II and hence the main rationale for the Bank's engagement in Lesotho.

5. **The CSP's main theme/objective is Job Creation Through Private Sector-led Inclusive Growth as outlined in NSDP II.** To achieve this objective, the CSP is articulated around the following two priority areas: **i) Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation; and ii) Leveraging Technology for Improved Governance and Institutional Capacity**. The first priority area will focus on creating high value-added jobs and livelihood opportunities in agriculture and agro-industry, tourism and other sectors targeting the youth and women. The second priority area will seek to improve economic and financial governance, transformative technological innovations in governance, enhance institutional capacity and strengthen accountability and oversight institutions. The two priority areas are complementary and mutually reinforcing, as the overall focus of

both is employment creation and poverty reduction. Both priority areas are anchored on NSDP II and are consistent with the TYS 2013-2022 and the High Five Priority Agenda.

6. The Bank's total net commitment to Lesotho as of 31 December 2019 was UA 53.64 million supporting 9 ongoing operations. Sixty-nine percent (69%) of these operations are funded by African Development Fund (ADF) loans and 31% by grants from ADF, Strategic Climate Fund (SCF), Fund for African Private Sector Assistance (FAPA), Global Environment Fund (GEF) and Rural Water Supply and Sanitation Initiative (RWSSI). In terms of sectorial distribution, the Information, Communication and Technology (ICT) sector is the largest beneficiary of total commitment (33%), followed by multisector and governance sector (29%), water and sanitation sector (23%) and energy sector (15%). In terms of distribution of resources as per the High 5 priorities of the Bank, the portfolio is dominated by Improve the Quality of Life for the People of Africa (37% of total commitment), followed by Integrate Africa (33%), Light Up and Power Africa (15%), and Industrialize Africa (15%).

7. **Portfolio performance was assessed to be satisfactory as of 31 December 2019.** More specifically, the overall portfolio rating improved to 3.0 (on a scale of 1-4, with 1 being highly unsatisfactory and 4 highly satisfactory) in 2019 up from 2.7 in 2017, and 2.1 in 2015. There are neither problematic projects (PP), nor potentially problematic projects (PPP) in the current portfolio. Consequently, both Project-at-Risk and Commitments-at-Risk (CAR) were rated 0% as of 31 December 2019. In addition, the disbursement rate for ongoing operations increased from 26.2% in December 2017 to 34.8% in December 2018 and to 46.4% in December 2019. The improved portfolio ratings reflects RDGS proactivity of RDGS in portfolio management. More specifically, RDGS has used its proximity to Lesotho to undertake frequent follow-up and monitoring missions to the country.

8. The Bank has identified various projects and has developed a pipeline that is aligned to the priority areas of the CSP, NSDP-II, TYS and High 5 priorities. These projects include an agriculture value chain development project, an enable youth program, a private sector intervention, a technology innovation project, and an institutional support project. The total cost of the indicative program is UA 25 million. There is a possibility that the agriculture value chain project will be co-financed and implemented with strong collaboration with other development partners in Lesotho.

9. **The Bank will continue to underpin its interventions with analytical work, including economic and sector work, and sectoral studies to inform sectoral and national policies**. Estimated cost of the non-lending program is UA 0.2 million. These activities will be carried out in a targeted approach that will be guided by policy dialogue and demand-driven analytical work. The Bank has supported policy reforms in public finance management and public-private partnership. For all practical purposes, some of the analytical work will be undertaken in collaboration with other development partners depending on the availability of resources, expertise and comparative advantage. In terms of policy dialogue, two key policy reforms to be undertaken with Bank assistance include public–private partnership and public finance management (PFM).

10. The Board of Directors is hereby requested to consider and approve the CSP 2020-2024 for the Kingdom of Lesotho.

1. INTRODUCTION

1. **This Country Strategy Paper (CSP) for Lesotho 2020-2024 follows the expiration of the CSP 2013-2017 and the CSP Update 2018-2019**. The CSP 2013-2017 was updated in June 2018 to run until December 2019 pending the finalization of Lesotho's second National Strategic Development Plan 2018/19-22/23 (NSDP II). Both the CSP 2013-2017 and CSP 2018-2019 Update were anchored on two Pillars: i) Infrastructure Development; and ii) Institutional Capacity Building. The objective of both strategies was to support Lesotho's development goals of achieving high, inclusive and sustainable growth. In approving the CSP Update, the Committee on Operations and Development Effectiveness **(**CODE) emphasized the need to pay more attention to the private sector and the promotion of agricultural value chains with a view to achieving self-sufficiency in food**.** Hence, the need to harness the country's agricultural potential and reduce its dependence on food imports from South Africa.

2. **In July 2019, CODE endorsed the two priority areas proposed in the CSP Completion Report, confirming their relevance to and alignment with Lesotho's development agenda over the next CSP cycle 2020-2024.** The new CSP's main theme/objective is Job Creation Through Private Sector-led Inclusive Growth as outlined in NSDP II. To achieve this objective, the CSP is articulated around the following two priority areas: **i) Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation**; and **ii) Leveraging Technology for Improved Governance and Institutional Capacity**. It is aligned with Lesotho's NSDP II and based on a series of consultations involving the Government, private sector, development partners (DPs) and civil society. It is also aligned with the Southern Africa Regional Integration Strategy Paper 2020-2024 which focuses on (i) Infrastructure Connectivity; and (ii) Market Integration and Industrialization. It is important to note that the design and processing of the CSP for Lesotho was exempted from the preparation of a Country Diagnostic Note (CDN) because the completion report was at a well-advanced stage. (Board document **ADB/BD/IF/2019/168 and ADF/BD/IF/2019/103).**

2. COUNTRY CONTEXT AND PROSPECTS

2.1 Political Context and Prospects

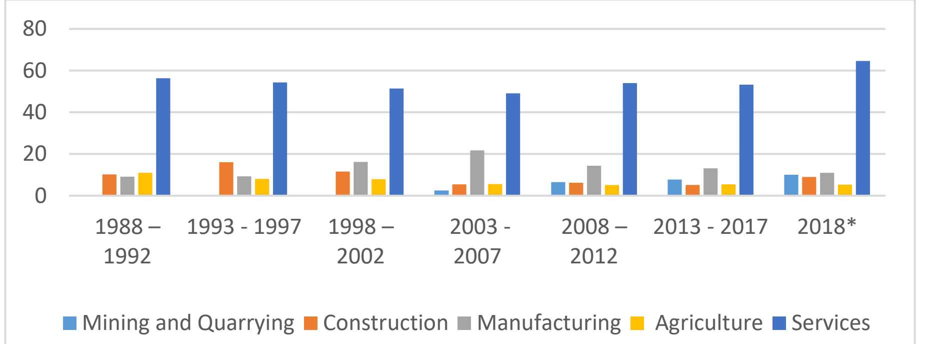
3. **Lesotho has experienced political instability and governance setbacks emanating from a fragile coalition government**. The weak coalition and internal rivalry in the ruling party remains a challenge to the country's political stability and economic development generally resulting in undermining investor confidence. Other governance challenges include politicized civil service and security institutions, unbalanced access to assets, over dependence on migrant labour and decline in SACU revenues. The situation has been exacerbated by political infighting and intense factional struggle for power following the March 2019 election of the new National Executive Committee. It is reflected in the country's Corruption Perception Index of 41 and a rank of 78 in 2018 compared with the rank of Botswana (34), Namibia (52) and South Africa (73). It has done better than only Eswatini with a rank of 89 in 2018. In order to address the issue, there is need to strengthen the Directorate on Corruption and Economic Offences (DCEO)**.**

4. **The Government launched a national dialogue in June 2018 focusing on political governance reforms with support from SADC and the European Union.** These reforms augur well for maintaining political stability, sustaining the economic reform agenda and preserving the country's focus on the implementation of NSDP II**.** It is also important to strengthen the capacity of institutions of governance and partnership with faith-based institutions and Civil Society Organizations (CSOs) that are actively involved in peacebuilding initiatives.

2.2 Economic Context and Prospects

5. **Lesotho is a consumer-oriented and import-dependent country with a small domestic market and a narrow economic base, which makes it vulnerable to external shocks**. It is classified as a lower-middle income country with a GDP per capita of about USD1300. In terms of sectoral contribution to GDP, agriculture contributed about 11% to GDP in the 1980s. However, in recent years, the sector's GDP contribution has declined to 5.3% (figure 1). Yet, the sector remains critical to supporting the livelihoods of those living in rural areas, constituting 67% of the country's population. This situation reflects a structural anomaly characterized by low productivity arising from the use of rudimentary technology, small farm holdings and inadequate access to credit, fertilizers, extension and research, among other factors. It implies that attempts at poverty reduction and employment creation must of necessity involve or focus on agriculture sector transformation and the rural population. In good harvest years, Lesotho is only able to meet roughly 30% of its annual cereal/grains requirements of which more than 40% are lost due to post-harvest losses, thus importing 80% of food requirements. An estimated 433,400 people are in need of food aid placing the country 78 out of 119 in the 2018 Global Hunger Report. In order to address these challenges, the Government has taken a number of initiatives, including the adoption of irrigation and conservation farming, construction of silos to reduce post-harvest losses, provision of subsidies, and the formulation of an Agriculture Master Plan, among others.

Figure 1: Sectoral Contributions to GDP, 2003-2018

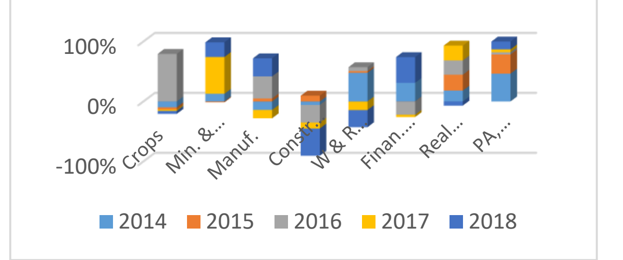


Central Bank of Lesotho and AfDB Statistics
***Estimate**

6. **Manufacturing's contribution to GDP averaged 9.2% during the period 1988-1992, peaked at 21.7% during 2003-2007 owing to the African Growth and Opportunity Act (AGOA)**. However, it subsequently declined to 13.2% during 2013-2017 and further to 11% in 2018 due to strong competition in the US market from Asian producers. In view of this decline, there is need to consider new investments in more efficient textile machines or upstream investment into the animal husbandry industry as AGOA will expire in 2025. During the period 2008-2018, construction, mining and quarrying contributed about 6%-10% to GDP. The service sector, the largest, continues to play an increasingly important role in Lesotho's growth contributing about 65% to GDP, and this trend is expected to continue during implementation of NSDP II. It is thus emerging as a driver of growth with great potential to provide employment opportunities over the medium term.

7. The average growth rates of all the sub-sectors were positive except construction during the period 2014-2018. The sub-sectors with the highest average growth rates during this period include crops (22.5%), followed by mining and quarrying (12.5%), public administration, education and health (9.9%), manufacturing (4.3%), finance and insurance (1.9%), real estate (1.2%), wholesale and retail (0.7%) and construction (-4.3%). Though crops registered the highest average growth rates during the period 2014-2018, it registered negative growth rates in both 2017 and 2018 due to drought. The same is true of construction and wholesale and retail trade both of which registered negative growth rates in 2017 and 2018 owing to the poor investment climate (figure 2). Like mining and quarrying, public administration, education and health also registered positive growth rates in both 2017 and 2018.

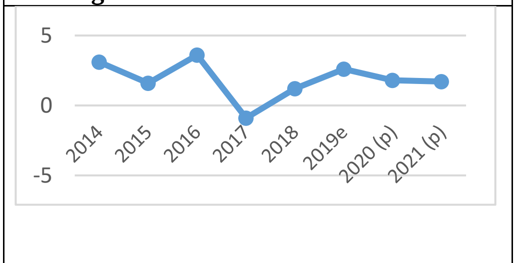
Figure 2: Sub-Sectoral Growth Rates 2014-2018



Central Bank of Lesotho

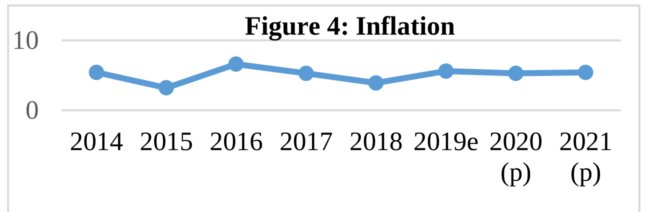
8. **Growth and Growth Drivers**: **Lesotho's growth performance remains sluggish with GDP growth rate averaging 1.72% during 2014-2018.** This average growth rate though positive masks the poor performance of the economy in 2017 with the GDP growth rate plummeting to -0.9% owing to the weak performance of the South African economy on which it is dependent for both exports and imports. The economy picked up at 1.2% in 2018 up from -0.9% in 2017, and estimated to grow by 2.6% in 2019. In 2018, economic growth benefitted from strong performance in the mining sector, and recovery of textiles and clothing in tandem with an increase in global demand (figure 3)**.** Textile and clothing grew by 2.5% in 2018 up from -6.23% in 2017 and contributed 9% to GDP in 2018 while mining grew by 11.86% in 2018 up from -3% in 2017 and contributed 4% to GDP in 2018. The growth projections for 2020 and 2021 are 1.8% and 1.7% respectively. These projections depend on the performance of the South African economy and the trade war between the US on one hand and China, EU on the other hand. Over the next few years, growth is expected to be driven by construction related to the second phase of the Lesotho Highlands Water Project (LHWP-II).

Figure 3: Real GDP Growth Rate



Source: AfDB Statistics data base

9. Monetary Policy: **Lesotho maintains parity between its currency, the Loti and South African Rand and aligns its Policy Interest Rate (PIR) to the Repo Rate of South Africa.** The PIR is currently at 6.75 %, and averaged 6.5 % for the past 12 months. Credit to deposit ratio has averaged 55% over the past 12 months. Expansion in money supply (broadly defined) slowed down in 2018 due to lower growth in private sector credit. Inflation decelerated relative to its peak of 6.6 % in 2016, declined to 5.3% in 2017 and further to 3.9% in 2018. Inflation decelerated relative to its peak of 6.6 % in 2016, declined to 5.3% in 2017 and further to 3.9% in 2018. It is estimated at 5.6% in 2019 and projected at 5.3% and 5.4% in 2020 and 20201 (figure 4). Since Lesotho imports about 80% of its goods from South Africa, the pass-through effects of currency depreciation will be minimal since inflation in the country of import origin, (South Africa) is within the monetary policy target range of 3-6% and is low.



Source: AfDB Statistics Dept. & CBoL

10. Fiscal Policy and Debt: Total revenues and grants have declined from 50% of GDP in 2014 to 41.2% of GDP in 2016 before picking up marginally at 42.9% and 41.3% of GDP in 2017 and 2018 respectively. The overall decline in revenues is attributed to the poor performance in SACU revenues associated with the weak performance of the South African economy. Total revenues are estimated at 43.8% of GDP in 2019 due to expected pick-up in economic activity and improved tax collection by Lesotho Revenue Authority following concerted efforts to streamline tax compliance. Though total expenditures and net lending are on a declining trend, the fiscal situation deteriorated from -1.8% of GDP in 2014 to -3.4% in 2017 and further to -5.1 % of GDP in 2018, reflecting the decline in SACU revenues (figure 5). The fiscal deficit is estimated at -4.0% of GDP in 2019 and projected at -3.9 and 3.6% in 2020 and 2021 respectively. These projections are predicated on the possible recovery of SACU receipts (currently below their historical average of 30% of GDP,) following the successful elections in South Africa, the successful implementation of political governance reforms in Lesotho and the National Dialogue launched in June 2018.

Figure 5: Fiscal Deficit as a % of GDP

Source: AfDB Statistics Department & CBoL

11. Lesotho's total savings as a proportion of GDP averaged 24% while its investment was about 27% during the period 2014-2018. The 2010–2018 averages show that Angola, South Africa, Zambia and Botswana have the highest gross domestic savings rates of 39.3%, 38.9%, 35.3% and 32.7% respectively while Lesotho, Zimbabwe and São Tomé and Príncipe recorded negative domestic savings rates of -19.6%, -4.9, and -1.8% respectively (AEO 2018). The country's low savings rate accounts for its limited fiscal space thus underscoring the need to expand the coverage, competitiveness, and affordability of financial services to bring the unbanked into the mainstream economy. However, Lesotho's gross national savings rate averaged 22% of GDP during the period 2010-2018 suggesting that Basotho save more outside their home countries, possibly due to emigration. Additionally, migrant remittances which have been a major source of foreign exchange have declined from 24.2% of GDP in 2010 to 16% of GDP in 2018.

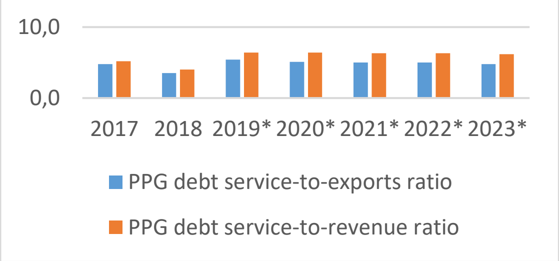
12. The fiscal situation is, however, being challenged by five major factors. These include huge wage bill (24% of GDP and three times the Sub-Saharan average); an over generous bursary scheme (2% of GDP), which is benefitting mostly students from high income families; exorbitant expenses related to governmental vehicle fleet; high cost of international and local travel, and subsistence allowances (3% of GDP); as well as policy uncertainty which undermines investor confidence and hence FDI inflows and revenues. The deficit is likely to be financed by the sale of bonds to commercial banks given the low level of reserves. Currently, there is no IMF program and a subsequent one hinges on the implementation of fiscal consolidation measures outlined in the 2019/2020 budget.

13. **Owing to lack of adequate amount of cash, the Government has accumulated payment arrears to local suppliers amounting to about 1.1 billion Maloti (USD 76 million), (2.6% of GDP), which includes payments dating back to April 2018.** The prolonged accumulation of payment arrears is having a devastating impact on business and bank balance sheets as suppliers fail to service their loans and retain employees. An arrears survey is being undertaken by the Government to ascertain the exact figures.

14. Lesotho's total public debt stock increased from 38.8% of GDP in 2017 to 46.8% of GDP in 2018 owing to limited fiscal space and projected at 49.5% in 2019. External debt averaged about 33% of GDP during the period 2014-2018 and projected at 32% in 2019. Domestic debt is on an upward trend, increasing from 8.1% of GDP in 2017 to 10.7% of GDP in 2018 and projected at 13.4% in 2019. External debt accounts for about 88% of Lesotho's debt while 12% accounts for domestic debt. Lesotho's risk of debt distress has been revised from moderate to low in 2017.

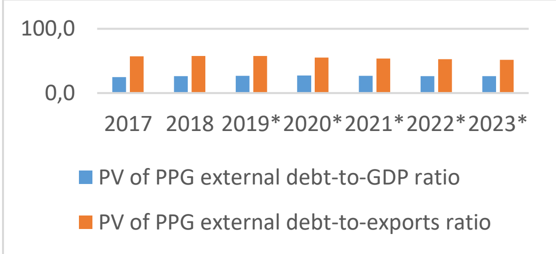
15. All external debt and debt service indicators remain below their respective thresholds (External debt to GDP: 40%; External debt to export: 180%; Debt service to exports: 15%; Debt service to revenue: 18%) (figures 6 and 7). Therefore, there is still limited scope for additional non-concessional borrowing to finance large infrastructure projects with large economic returns. However, maintaining a significant grant element in financing will avoid risks for future

Figure 6: Debt Sustainability Indicators: Liquidity Indicators (%)



Source: World Bank/IMF Debt Sustainability Analysis

Figure 7: Debt Sustainability Indicators: Solvency Indicators (%)

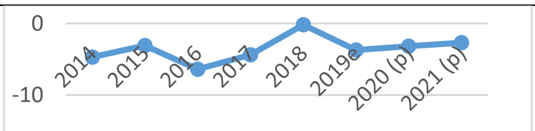


Source: World Bank/IMF Debt Sustainability Analysis

fiscal deficit and international reserves. There is also a need for the Government to prepare a medium-term debt strategy.

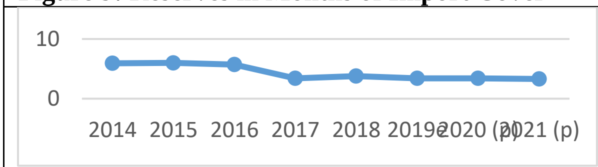
16. External Sector: The current account averaged -4.7% of GDP during the period 2014-2016. However, it improved to -4.4% and -0.2% of GDP in 2017 and 2018 respectively. It is estimated at -3.7% in 2019 and projected at -3.2% and -2.7% in 2020 and 2021 respectively owing to an expected increase in diamond exports (figure 8).

Figure 8: Current Account Balance as a % of GDP



Source: AfDB Statistics Department & CBoL

Figure 9: Reserves in Months of Import Cover



Source: AfDB Statistics Department & CBoL

Therefore, overall, the current account has improved from its 2017 level reflecting the increase in exports from 37.9% of GDP in 2014 to 46.2% of GDP in 2018 and the decline in imports from 87.1% in 2015 to 73% in 2018. International reserves are on a declining trend plummeting from 6 months of import cover in 2015 to 3.8 months of import cover in 2018, estimated at 3.4 months of import cover in 2019 and projected at 3.4 months and 3.3 months in 2020 and 2021 respectively (figure 9).

17. The Government has taken some fiscal consolidation measures on both the expenditure and revenue fronts to enhance macroeconomic stability as outlined in the 2019/2010 budget speech. These include reducing international travel, cost of foreign missions, ministerial gross salaries, freeze on hiring, and abolition of interest free loans to parliamentarians, among others. Revenue side measures include enactment of tax administration bill, value added tax bill, income tax bill, and customs bill.

18. A failure to consolidate the fiscal situation in line with the FY2019/20 budget would force the authorities to choose between a further depletion of government deposits at the Central Bank of Lesotho, (implying adverse consequences for reserves and ultimately for the peg to the rand), or to maintain deposits at the cost of continuing to accumulate arrears, which could further undermine growth and financial stability. On the upside, if structural reforms are accelerated, and the South African economy picks up, growth and SACU revenues could be boosted. Overall, the domestic growth outlook remains subdued due to heightened uncertainty at the global, regional and domestic levels.

19. **Economic and Financial Governance**: **Governance indicators show that Lesotho needs to strengthen transparency and accountability in the use of public funds.** Lesotho's rank in the MO Ibrahim Index of African Governance declined from 15th in 2015 (a score of 57.8) to 16th in 2018 (a score of 57.1) reflecting a marginal deterioration in overall governance**.** Though Lesotho is a not a fragile country as indicated by the CPIA of 3.8, it has some drivers of fragility as revealed by the fragility assessment conducted in 2015, including the politicized civil service and security institutions, and unbalanced access to assets. Lesotho's financial governance is generally weak as evidenced by numerous challenges, including inadequate PFM systems, weak institutional capacities and internal controls, leading to low disbursement rates in Bank-financed operations.

20. Private Sector: **Private Sector**: **This sector accounts for only 20% of GDP and is mostly inward-oriented with 71% of the firms involved in commerce (wholesale and retail)**. The private sector is hamstrung by weak capacity, low productivity, high levels of fragmentation, inadequate access to credit, lack of product standardization, and inadequate infrastructure and resources to develop products to the required global standards, among others. Micro and small firms account for 97% of all local enterprises; yet over half of private sector employment is generated by relatively large (mostly South African) firms. Domestic private sector activity is concentrated in a few firms in sectors such as agriculture and mining as well as textiles and construction with very low value addition along the value chains. The apparel industry accounts for a significant amount of exports (especially to the USA under the AGOA). In order to revitalize the sector, a number of initiatives are underway. These include the establishment of a PPP unit, formulation of a PPP Policy and framework in support of the PPP financing modality. In addition, the legal and regulatory framework for SEZs will be developed.

21. **Value chain development by the private sector in the agro-processing industry to take advantage of the regional market opportunities remains a daunting challenge** on account of declining productivity in the agriculture sector compounded by prolonged droughts. Horticulture presents notable opportunities for the country to scale up participation in regional value chain and agro-processing. However, this has not been developed on a large scale owing to reasons cited in paragraph 20 above.

22. According to the World Bank's Doing Business Report 2019, Lesotho ranks 106 out of 190 countries. Lesotho declined in rank from (100/190) in 2016 to 106/190 in 2019. It ranks behind South Africa (82), Botswana (86) and Zambia (87) but outperforms Namibia (107) and Swaziland (117) in overall ranking despite its implementation of the ASYCUDA for its customs processes. An uncompetitive business environment is one of the most binding constraints on private sector development. The country's lowest rankings are recorded in the sub-indicators for *Dealing with construction permits*, *Getting Electricity, Protecting Minority Investors* and *Resolving Insolvency*. This arises from cumbersome business procedures, insufficient access to finance, inadequate digital infrastructure, and skill gaps, among others.

23. **The Bank Business Development Seminar held in Maseru in October 2019 revealed that the daunting challenge faced by private sector companies**, (especially business start-ups) is inadequate access to finance. The other issues discussed related to training, mentoring and marketing. The Bank will provide a Line of Credit to Lesotho National Development Corporation (with a technical assistance component for training) for on-lending to SMEs.

24. Financial Sector: Banks are the largest component of Lesotho's financial sector of which three foreign-owned banks and one public bank hold 48.8% of the sector's total assets implying the difficulty local enterprises, especially SMEs encounter in accessing funds. Insurance companies represent 18.9% of total assets, public pension funds 16.7%, private collective investment schemes (such as mutual funds and other asset management companies) 10.8%, microfinance 2.6%, and others

2.2%. The proportion of non-performing loans has increased from 3.7% in 2016 to 4.1% in 2018 due to payment arrears to suppliers who have defaulted in paying their loans. The return on equity declined marginally from 30.5% in 2015 to 28.6% in 2018 while the return on assets remained at 3.4% during the same period. Historically, bank capital adequacy ratio in Lesotho reached an all-time high of 22 % in 2005 and an all- time low of 11% in 2017 down from 12.1% in 2013. When compared to Lesotho's main peers, bank capital adequacy ratio in Botswana amounted to 21.9 %, 16.3 % in South Africa and 23.2 % in Swaziland in 2017. The credit-to-GDP ratio declined from 17.8% in 2014 to 16.1% in 2018 reflecting the system's poor capacity to foster financial development and inclusion.

25. **Regional Integration: Regional integration is of particular importance to Lesotho given the country's small population and economy and its dependence on its neighbour, South Africa**. Its central location within South Africa gives the country unimpeded access to South Africa's expertise, advanced technology, developed infrastructure, capital and financial markets, and investment resources. However, this proximity to South Africa is compromised by long delays at major commercial border posts, and an unpredictable business environment with regards to customs and border management.

26. **In addition, Lesotho's African Integration Index is low ranking 10th in SADC, with a score of 0.39.** This reflects the fact that Lesotho has not been able to diversify its export market beyond South Africa and the USA. Given the limited size of Lesotho's domestic market and import-driven economy, transition to a middle–income country will require diversification of both products and markets, addressing trade development constraints such as product quality and standards as well as skills in order to gain access to and take advantage of preferential agreements in the European Union, in addition to AGOA. Some of the initiatives it has taken to enhance integration include the establishment of a dry port, access roads to border posts and modern one-stop border facilities, as well as engagement with South Africa to improve the handling of transit cargo and policy coordination.

27. **Lesotho signed the African Continental Free Trade Area (ACFTA) in July 2018.** The CFTA could enhance Lesotho's participation in regional goods markets and value chains. This is reinforced by the fact that five of the top ten export markets for Lesotho are members of SADC[1]. In order to fully benefit from this, Lesotho has taken several initiatives to improve the trade and business environment, including strengthening regional integration schemes, establishment of the legal and regulatory frameworks, trade logistics, and AGOA Response Strategy focusing on priority sectors such as (a) textile and apparel, (b) footwear products; (c) natural and organic water and canned fruits; and (d) handcraft, leather and leather accessories.

2.3 Sector Context

28. Transport: The transport sector directly contributed about [2]8.43% to Lesotho's GDP in 2017, and is expected to remain the same for the foreseeable future through construction and maintenance of infrastructure outsourced to the private sector, and provision of transport services to growth sectors of the economy, namely, agriculture, manufacturing, and tourism. However, the sector still faces some challenges including, low penetration of the road network, with poor access particularly in the rural areas, and poor road connectivity along international corridors, among others. These challenges contribute to high cost of transportation in Lesotho and perpetuate isolation and poverty in rural areas. The Government has prepared a robust Transport Master Plan to address the above challenges, from which a pipeline of projects and programs has been included in NSDP II.

[1] South Africa, Eswatini, Botswana, Mauritius and Zimbabwe
[2] Central Bank of Lesotho, Economic outlook (2018 – 2020).
https://www.centralbank.org.ls/images/Publications/Research/Reports/Economic%20Outlook/MacroEconomic_Outlook_-_Dec_2018.pdf

29. Water and Sanitation: **The water sector contributes about 8% of GDP and remains a strategic sustainable and renewable resource and one of country's most valuable natural assets which is central to the country's long-term growth prospects.** It has proven also to be a source of revenue for the country (water transfers to South Africa's economic heartland). Although the country has plenty of water, access remains a problem. The reality is that even when water is accessible, affordability remains a challenge. The country's access to water supply services is relatively high compared to other countries in Sub-Saharan. About 95% of urban and 73% of rural households have access to improved sources of drinking water. The increasing industrial demand for water, rapid urbanization growth and dilapidated infrastructure have steadily increased the pressures on water supply services. Another challenge is the need to balance water resources development for export against the national priority of improving water supply infrastructure and services in the country.

30. Access to improved sanitation services in Lesotho is low. Only 44% of the total population has access to improved sanitation (46% and 43% coverage in urban and rural areas, respectively).[3] About 30% of households do not have access to any toilet facilities and therefore practice open defecation.[4] Access to reticulated sewerage is estimated at just 4% of the population in urban areas and mainly in the central business districts of Maseru and larger towns. This poor access has an adverse impact on other sectors, including health, particularly for under-five children, education, etc.

31. Information and Communication Technology Sector /Digital Services: This sector contributes 5% to GDP and features prominently in NSDP II as a catalyst for growth. The KoL has joined the new global awakening of digital transformation aimed at enhancing production and productivity through technological innovations while maximizing economies of scale and enhancing competitiveness of the country's economy. The new impetus is demonstrated in the country's efforts to improve ICT infrastructural connectivity with an estimated 97% of 2nd and 3rd generations mobile coverage and linked to South Africa and the SADC region through three main submarine cables. Furthermore, the Government is determined to move to digital financial services including the e-Payments system aimed at enhancing financial inclusion through technological innovations and development of tailor-made products and services that are broad based and commercially suitable.

32. Energy: **The National Policy 2015-2025 guides the sector and envisions the development of the renewable energy sector**. The total amount of energy available is 75 MW as against a demand of 165 MW, the shortfall being imported from South Africa and Mozambique. Access is concentrated in urban areas (47%), where the infrastructure for transmission and distribution is considerably well developed, while rural areas represent approximately 10.2% of the grid-served areas. Some of the challenges in the sector include limited generation capacity, weak policy and institutional framework lacking holistic approach and incentives for private sector involvement and low awareness of renewable energy technologies, among others.

33. The Government is taking a number of initiatives including the establishment of a Rural Electrification Authority, and promoting renewable energy through Independent Power Producers (IPP) in the wind, solar and hydro sectors to make up for the deficit in power generation.

2.4 Social Context and Cross-Cutting Themes

34. **Poverty**: **Lesotho's poverty rate measured at the national poverty line of Lesotho Maloti LSL 648.88 (2017 prices) per adult equivalent per month declined from 56.6% in 2002 to 49.7% in 2017** (2019 Lesotho Poverty Assessment Report). Urban poverty decreased from 41.5% to 28.5% while rural poverty declined marginally from 61.3% to 60.7% during the same period. Poverty in rural

[3] 2017 United Nations Children's Fund (UNICEF)/World Health Organization (WHO) Joint Monitoring Project (JMP) Report
[4] Improved drinking water source and improved sanitation coverage data are from the UNICEF/WHO JMP 2017

areas (60.7%) is in part due to low agricultural productivity resulting from hostile weather, animal diseases, and lack of inputs. In 2017, 27.3% of Basotho were poor at the international poverty line of USD1.90/day (in 2011 purchasing power parity terms). Inequality as measured by the Gini coefficient declined from 51.9% in 2002 to 44.6% in 2017 underscoring the fact that the benefits of Lesotho's growth have not been equally shared. Therefore, policies tailored towards addressing employment, poverty and inequality remain critical.

35. Youth Unemployment: **The overall unemployment rate declined from 25.9% in 2010 to 23.6% in 2018 while youth unemployment declined from 51.7% in 1998 to 33.2 in 2018**. Generally, the high level of youth unemployment stems from the mismatch between the supply and demand for labour, lack of relevant skills, high burden of disease, especially HIV/AIDS and tuberculosis, poor investment climate and lack of key infrastructure. Furthermore, the bloated public sector has crowded out the private sector which is supposed to create jobs.

36. **Human Development**: **Lesotho's human development index (HDI) of 0.518 (2018) places the country in the low human development category, ranking it at 164 out of 189 countries**. Its human development has been adversely affected by life expectancy at birth (49.8 years) which is far below the Sub-Saharan average of 60.6 years. According to the Lesotho 2015 Millennium Development Goals (MDGs) Report, none of the MDGs were achieved. The unfinished business of the MDGs is being taken up in the context of the Sustainable Development Goals (SDGs) (Annex A.11). It is unlikely that the country will achieve any of the SDGs on account of the fiscal and liquidity crisis and the recurring droughts.

37. **HIV/AIDS: At 25.6% (an estimated 306,000 people living with HIV), Lesotho has the second highest HIV prevalence rate in the world**. Women are disproportionately affected, with a prevalence of 30.4% compared to 20.8% among men. There are currently more than 200,000 orphans in Lesotho, most of whom are HIV/AIDS orphans. HIV is the leading cause of death and contributes to Lesotho having the lowest life expectancy among 193 countries. Some of the challenges in the health sector include the shortage of doctors and nurses, particularly in rural areas, lack of institutional capacity, the hilly and mountainous terrain which makes access to health facilities in the rural areas difficult. Lesotho has developed a National HIV/AIDS Strategic Plan 2018/19 – 2022/23 aimed at eventual elimination of the pandemic by 2030. Some of the programs aimed at combating the pandemic include the President's Emergency Plan for AIDS Relief, NUL-HIV/AIDS program and Doctors without Borders.

38. Civil Society: **The civil society is involved in areas such as HIV/AIDS, human rights, agriculture and food security, climate change, education, health, and water, sanitation, and hygiene** (WASH), among others. It is expected that once the new NGO (Non-State Actors) Policy and Law are approved, there will be a framework for engaging with the Non-State Actors, including the CSOs. This will create opportunities for building lasting relations with the Government and other development actors.

39. Environment and Climate Change: **Lesotho is particularly prone to a number of environmental hazards such as drought, soil erosion, land degradation, deforestation, loss of biodiversity and drying up of the wetlands and mountain sponges**. The depletion of natural resources has deepened poverty in rural areas, contributing to significant rural–urban migration. Climate change has exacerbated the situation, especially in the agricultural sector, thus undermining sustainable development efforts.

40. **Lesotho's National Adaptation Program of Action on Climate Change (NAPACC) and Environmental Act 2008** seeks to enhance management of the environment targeting in particular the energy sector as a major climate change mitigation measure through increasing its renewable energy mix for better rural access, adopting cleaner technologies for energy efficiency and stimulating green growth opportunities. Access to alternative sources (off-grid) of energy is being prioritized, in addition to hydropower (50% of the energy mix) to stimulate economic growth, especially in rural access. The government is committed to reducing GHG emissions by 10% by 2030 and a further 25% reduction can be achieved with additional external resources according to its nationally determined contributions (NDC) commitments to the Paris Agreement. (Ministry of Energy and Meteorology, 2017).

41. Transition to Green Growth: **Lesotho is not a significant emitter of CO2 and polluter of the environment.** It has so far not made any huge capital investments in brown economy ventures that necessitates a transition to the green economy. Therefore, there is no need for strong mitigation plans to reduce CO2 emissions. Instead, the Government is now focused on implementing strategies to conserve the environment, bio-diversity and natural capital, and improve sanitation. The Government is also exploring the possibility of using waste for energy in the future and an opportunity for job creation for the youth. However, the country's inadequate infrastructure and systems pose a risk to the Government's ability to fully implement the NAPACC.

42. Gender: Lesotho is also a signatory to a number of international conventions on gender, including the Convention on the Elimination of All Forms of Discrimination Against Women (CEDAW). In 2018, the Gender and Development Policy was promulgated into an Act, and includes updates to incorporate gender emerging issues as contained in the SDGs.

43. **A number of laws have also been promulgated to promote gender equality, including**

- The Legal Capacity of Married Persons Act, which has done away with the minority status of women in Lesotho;
- The Sexual Reproductive Health Act;
- The Ministry of Gender has put in place 2018-2030 Gender and Development Policy which provides for free and compulsory education for both boys and girls and prohibits expulsion of female students who fall pregnant and mandates schools take them back after delivery;
- The Land Act; and
- Access to Finance for Women Act, among others.

44. **The Gender Department in Lesotho focuses on three key gender empowerment dimensions, namely, political, economic and social empowerment:**

- Political empowerment addresses issues relating to the dissemination of legislation, human rights and political empowerment of women.
- The economic dimension provides business training and seed capital for women economic empowerment.
- The social empowerment component deals with issues such as capacity building, dissemination of laws on GBV, and participation in the 16 days of Activism against GBV.

45. **Despite the country's progress in gender empowerment, a number of challenges still persist**. These include inadequate gender mainstreaming at the institutional and community levels due to past patriarchal tendencies, inadequate human resource and institutional capacities and well entrenched cultural rigidities, which prevent behavioural change. These challenges account for the poor performance of Lesotho compared to other SACU member countries (table 1). The Bank will provide training in gender mainstreaming.

Table 1: SACU Countries: Global Gender Rankings and Scores

	Lesotho	Swaziland	Botswana	South Africa	Namibia
Rank	81/149	80/149	55/149	19/149	10/149
Score	0.693/1	0.694/1	0.715/1	0.755/1	0.789/1

Source: Global Gender Gap Report 2018

2.5. Country Strategic Framework

46. **The Government's latest overarching national development agenda is NSDP II. Its four priority areas include** i) Promoting Inclusive and Sustainable Economic Growth and Private Sector–led Job Creation; ii) Strengthening Human Capital (through developing human capabilities in Health, Education, Nutrition and Social Protection); iii) Building Enabling Infrastructure; and iv) Strengthening National Governance and Accountability Systems. Its theme is ***Employment and Inclusive Growth: In Pursuit of Economic and Institutional Transformation for Private Sector-led Jobs and Inclusive Growth***. NSDP II aims to transform Lesotho from a consumer-based economy to a producer- and export-driven economy. It will serve as the blueprint for all development efforts over the plan period, and implement the SDGs, the AU Agenda 2063 Goals, and Vision 2020. NSDP II emphasizes private sector development and gives priority to pursuing people-centred development.

47. **Additionally, the Government has initiated the Economic Laboratories**, an initiative launched in March 2019 emanating from the desire to effectively and efficiently implement NSDP II, following a strategic review of the preceding plan, NSDP I. It is an investment dialogue platform between government and the private sector to discuss how specific investment projects can be implemented through directly addressing prohibiting obstacles. It is anchored on NSDP II and prioritizes the four productive sectors, including agriculture, manufacturing, tourism and creative arts and technology and innovation. The key features of each sector and its contribution to GDP, challenges and policy palliatives being taken are available in Annex A.13.

2.6 Aid Coordination Mechanisms, Bank Positioning and Comparative Advantage

48. Lesotho is a signatory to the 2005 Paris declaration, Accra and Busan commitment implying that donor interventions are generally aligned with the Government's priorities. A formal donor-government coordination platform has been introduced which meets twice a year providing a platform for information sharing on government policies, aid modalities and coordination in general. The last meeting which the Bank attended was held in September 2019 where issues relating to NSDP II monitoring and evaluation, poverty study report, and Lesotho development cooperation report were discussed, among others. The Bank's long standing engagement with Lesotho has given it visibility and is a key member of the Public Sector Improvement and Reform Steering Committee aimed at monitoring and providing policy guidance in the implementation of the PFM Reform. Annex A.7 provides a list of donor interventions.

49. Plans are already underway to strengthen the donor coordination mechanism by establishing a Development Partners' Group (DPG) which will bring together all the donors under one umbrella. The Bank has drafted the TOR for the proposed DPG. It participated in the last donor coordination meeting convened by the UN in November 2019 focusing on the implementation of the United Nations Development Assistance Framework 2019-2023, a common programming instrument for all UN agencies in Lesotho.

2.7 Challenges and Weaknesses, Strengths and Opportunities

50. **Lesotho's overarching development challenge is lack of structural transformation.** As the context analysis above has shown, the country enjoys several strengths and opportunities, which it can exploit to advance its development agenda. However, it also faces significant challenges and weaknesses, notably a lack of value addition, limited diversification of the economy and limited participation of the private sector in economic activities. Box 1 below summarizes Lesotho's strengths, opportunities and challenges and weaknesses.

Box 1: Strengths, Opportunities and Challenges, Weaknesses

Strengths and Opportunities

- **Unimpeded access to the range of South Africa's expertise**, advanced technology, etc.;
- **Potential for collaborative efforts of donors in the digital transformation space**;
- **The CFTA** can provide a massive market for its goods and services, boost its GDP, and create jobs, etc.;
- **High potential for tourism** given picturesque landscape and snow covered mountain slopes ideal for skiing;
- **Fertile soils** supported by an abundant amount of water conducive for agricultural production**;**
- **Cost effective supplier of water** to South Africa and Botswana; and,
- **Potential for mohair and value addition in diamond processing.**

Challenges and Weaknesses

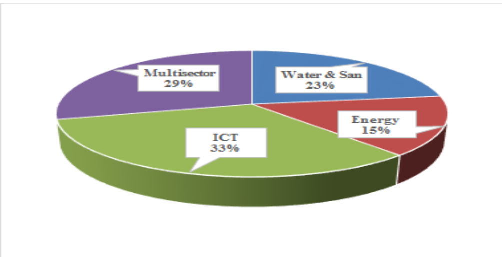
- **Persistent income inequality and high unemployment and poverty levels**;
- **Macroeconomic instability** arising from a prolonged period of slow growth in South Africa;
- **Political uncertainty and lack of consensus in the coalition government**;
- **Environmental degradation due to climate change;**
- **Inadequate access to credit from the formal banking sector**;
- **An unconducive business environment** for leveraging technology including incubation and innovation facilities, intellectual property and industrial standards;
- **Inadequate national digital financial literacy policies and strategies** to boost financial inclusion;
- **Inadequate and poor quality infrastructure** hinders competitiveness; and,
- **Weak human capital and skill gaps** which affect service delivery and stifles the growth of enterprises.

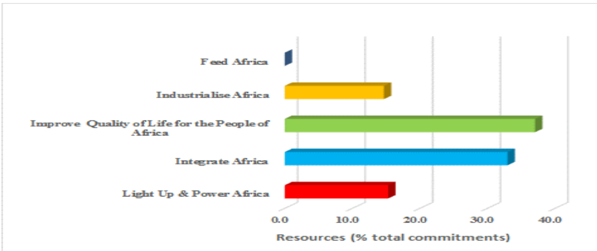
3. KEY FINDINGS OF COUNTRY PORTFOLIO PERFORMANCE REVIEW

3.1 Ongoing Portfolio

51. **The Bank's total net commitment to Lesotho as of 31 December 2019 is UA 53.64 million supporting 9 ongoing operations (Annex A.6.1).** These operations are funded through 69% by ADF loans and 31% by grants from ADF, SCF, FAPA, GEF and RWSSI. The sectoral distribution in figure 10 reflects the strategic alignment of the portfolio with the country's development priorities (2018/19-2022/23 NSDP II), the Bank's current CSP 2013-2019 for Lesotho and the Bank's Ten-Year Strategy for 2013-2022, as well as the Bank's High 5 priorities.

Figure 10: Portfolio Distribution by Sector and High 5 priorities (UA 53.64 million).





3.2 Portfolio Performance

52. **Key performance indicators show that portfolio performance has improved over the years since the portfolio reviews of 2015 and 2017 and 2019 (Annex A.6.2).** More specifically, the overall portfolio rating has improved to 3.0 (on a scale of 1-4, with 1 being highly unsatisfactory and 4 highly satisfactory) in 2019 from 2.7 in 2017, and 2.1 in 2015. The disbursement rate for public sector operations increased from 26.2% in December 2017 to 34.8% in December 2018 and to 46.4% in December 2019. This is due to improved supervision of projects, coaching and fiduciary clinics. The portfolio is relatively young with an average age of 3.3 years, and has no projects at risk. The percentage of projects flagged with 'red alerts' in the *Bank's Portfolio Flashlight Report* has also declined from 50%% in December 2017 to 9% in December 2018 and to 7% in December 2019, which is well below the Bank corporate target of 20% for flagged projects. There are currently four projects on 'closed watch' alerts related to slow disbursements. More specifically, *the e-Government Infrastructure Phase I Project and the Lesotho Lowlands Rural Water Supply and Sanitation Project* have disbursement closing dates expiring in 1 to 6 months and less than 80% disbursed. The *Renewable Energy Integration*

Study (3.3% disbursed) has disbursement closing in 13 to 15 months and less than 60%. There is need to expedite procurement processes in these projects, award contracts, improve the provision of services and supply of goods with a view to boosting disbursement rates. The *e-Government Infrastructure Phase II Project was approved on 18 October 2019 and remained unsigned for 60 days.* It is important to note that at time of writing both the Government and RDGS have signed the loan/grant agreements and the internal process is being finalized.

53. **Several initiatives were undertaken to further improve portfolio performance, including conduct of fiduciary clinics for PIUs, EAs on procurement and disbursement rules and procedures**. In addition, environmental and social safeguard requirements were adequately incorporated in Bank Group infrastructure operations in the country. Finally, the active engagement of Task Managers with the EAs, and continuous follow-up by the Bank and Government on implementation of the 2019 CPIP (Annex A.6.3) improved the quality of the portfolio. The key messages from the CSP CR and CPPR are available in Annex A.3.1.

3.3 Portfolio Issues

54. **In spite of these positive developments in portfolio management, there is still room for improvement.** There is need to enhance quality at entry, adherence to the Presidential Directive PD 02/2015. This calls for continuous application of a 'readiness' filter, on new operations going forward (as in the recently approved e-Government Infrastructure Phase II Project on 18th October 2019). This approach will minimize project start-up delays arising from challenges in design and lack of requisite capacity, especially absence of procurement specialists in some instances. In particular, RDGS will continue to work closely with Government to ensure that all conditions related to first disbursement are fulfilled within three months after Board approval. Other challenges include late submission of annual financial audit reports to the Bank, and inadequate justification of utilization of funds in special accounts. On the Bank side, delays have been encountered in responding to disbursement and procurement requests. The Bank will strengthen dialogue with the Government to address these challenges and implement the 2019 CPIP (Annex A.6.3).

4. LESSONS LEARNED

Experiences and Lessons for the Bank

55. The Bank should ensure the readiness of feasibility studies and/or detailed design studies for pipeline operations. The development of a readiness filter is encouraged and task teams should be encouraged to utilize advance procurement to speed up project start-up.

56. The lack of dedicated resources posed a challenge in undertaking ESWs. Earmarking resources for ESWs at the country level will enhance the Bank's ability to plan its interventions.

Experiences and Lessons for the Government

57. Start-Up delays: A s**tronger level of commitment from the senior level of Government** is critical to ensuring that effectiveness conditions are met in time to avoid start-up delays.

58. The Government could consider standardizing remuneration for all staff working on donor-funded projects in order to retain project officials, especially procurement specialists who are in high demand.

Experiences and Lessons for Development Partners

59. **There is also a need to strengthen donor coordination** to enhance complementary and synergies in interventions.

5. BANK GROUP STRATEGY FOR LESOTHO

5.1 Strategy Rationale, Objective and Priority Area(s) for Bank Support

60. According to the 2019 CSP CR and CPPR, the Pillars of the 2013-2017 CSP and the 2018-2019 CSP Update CSP were relevant and aligned to Lesotho's development priorities. Some of the achievements under the previous CSP include an increase in access to electricity, safe drinking water, adoption of a new internal audit manual, approval of a new Audit Act of 2017, and audit regulation, approval of a new human resource strategy and operational manual, adoption of a new public procurement policy, new standard bidding document and manual and an increase in revenue collection. The performance of the Bank portfolio was satisfactory. Most of the recommendations in the CPIP 2017 were either fully implemented, or partially implemented by end-December 2019.

61. **However, issues relating to value addition, an enabling environment for private sector private sector activities, agricultural productivity, linkage between agriculture and industry** to bring about the necessary structural transformation.

62. **On account of this situation, there is need for a shift in strategy focusing on developing value chains in support of employment creation and poverty reduction while enhancing institutional capacity for economic and financial governance and improving the enabling environment for private sector development.** This will help restore macroeconomic stability, exploit new sources of growth, define a more streamlined role for the state, and position itself to take advantage of potential regional opportunities in SADC and CFTA.

63. The Bank's support as a catalyst, convener, connector, and financier will absolutely be crucial in the implementation of NSDP II and hence the main rationale for the Bank's engagement in Lesotho. The basis for the Banks Group's engagement with Lesotho rests on (i) the Bank's comparative advantage, (ii) alignment with NSDP II and guided by the available resources, (iii) selectivity and relevance in the choice of priority areas guided by the TYS and the High 5s, (iv) consolidation of achievements made under the previous CSP, (v) synergy with other DPs, and (vi) promotion of green and inclusive growth.

64. **In view of the aforementioned facts, the CSP's main theme/objective is Job Creation Through Private Sector-led Inclusive Growth as outlined in NSDP II**. To achieve this objective, the CSP is articulated around the following two priority areas: **i) Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation; and ii) Leveraging Technology for Improved Governance and Institutional capacity.** In the following paragraphs, the Bank's assistance strategy under each Priority Area is presented.

5.2 Strategy and Expected Results

Priority Area I: Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation

65. The objective of the Bank under this priority area is to support value chain development, the establishment of rural agriculture enterprises for women and youth in support of economic growth through a private-sector driven but public sector-enabled environment. The Bank will work with the government to address bottlenecks in agriculture, manufacturing, textiles, and skills as well as other policy and institutional constrains on growth. In addition, the Bank will use its range of instruments to catalyze private sector investments in value chains, especially agriculture and agro-processing. The intervention will contribute to enhancing social inclusion and climate protection by creating economic opportunities for women and youth using climate adaptive practices.

66. **Key Results Area 1**: **Support to the development of value chains:** In line with the goals of the 'Feed Africa', 'Industrialize Africa' and "Improve the Quality of Life of the People of Africa", the Bank will support the agriculture sector as a means of addressing poverty and unemployment in support

of inclusive growth, through climate smart interventions. Development of value chains will primarily focus on increasing production and productivity to satisfy domestic demand which is currently being met by imports. The value chains will be scaled up within the context of Special Economic Zones (SEZs), which will cover special agricultural economic zones. In addition to generating growth and creating employment, SEZs draw foreign direct investment (FDI) for export-oriented industries, which generate employment opportunities for the country, enhance skills, promote exports and attract multinational companies (MNCs) in high technology industries which will encourage technology transfer and the gradual development of competencies in the managerial and technical fields for Basotho. Cognizant of this, the Bank is financing a feasibility study for the establishment of SEZs to take advantage of AGOA and the CFTA.

67. Value chain development, including horticulture, water bottling, wool and mohair, sandstone, poultry, piggery, horticulture fisheries, and beef. In developing these value chains, the focus will be on developing the requisite and associated soft and hard infrastructure while addressing issue relating to capacity, de-risking facilities, access to credit and markets, and policy and regulatory environment. It will support market linkages and mentorship to smallholder farmers through apprenticeship and also out-grower contract schemes. To ensure impact, the Bank will leverage complementary sources of finance in projects financed by other development partners such as the Smallholder Agriculture Development Project Phase I and II to maximize impact.

68. **Key Results Area 2**: **Support to Youth-led Micro, Small and Medium Enterprises (MSMEs):** The Bank will support MSMEs, particularly youth-led enterprises in key value chains prioritized by the Government of Lesotho through the Economic Laboratories. MSMEs play a crucial role in development and sustainability of the Lesotho economy. Using sovereign concessional resources, Bank support to youth-led SMEs will contribute to inclusive growth and job creation. The support will focus on business incubation, training, coaching and technical assistance to young male and female entrepreneurs, while increasing their access to markets and finance. The support will also strengthen the capacity of cooperatives and rural farmers as entrepreneurs in the context of the overall value chain, help enhance innovation to improve productivity, and increased income and employment opportunities for youth entrepreneurs. From the High 5s perspective, the intervention will enable Lesotho operationalize the Enable Youth Program and effectively participate in rolling out the Jobs for Youth in Africa (JfYA) Strategy to create employment for youths and women in agriculture and other value chains. It will also contribute to the implementation of the Strategy for Agricultural Transformation in Africa 2016-2025, with a focus on increasing agricultural production and value addition in the sector.

69. **Main Outcomes/Key Results under Priority Area 1:** The Key Results expected to be achieved under the CSP Priority Area 1 include: increased horticulture and crop production and productivity; increased youth employment, and increased private sector investments. The main outcomes will include improved productivity in selected value chains, increased income of value chain actors and increased private sector investment in priority value chains. In agriculture, the interventions under the CSP aim to contribute to improved crop production and productivity in the project area from 0.5 T/ha in 2019 to 2.5 T/ha by end of the CSP cycle in 2024. Under the youth empowerment and job creation support program, the proposed intervention will increase the establishment of new agriculture related businesses (50% women owned) from 0 in 2019 to 500 at the end of the cycle in 2024. Energy interventions are expected to increase access from 42% of the population in 2019 to 50% by end of the CSP period; as well as reduce technical (transmission and distribution) losses from 14% in 2020 to 10% at the end of CSP period in 2024. In water, the CSP intervention is expected to contribute to improvement in access to clean water from 82% of the national population in 2019 to at least 90% at the end of the CSP period.

Priority Area II: Leveraging Technology for Improved Governance and Institutional Capacity.

70. **This priority area will cover technological innovations of applications and digital financial services that will improve financial and economic governance** as well as development of value chains in Priority area I. In that context, it will help improve financial accountability by strengthening systems for monitoring and evaluation and expenditure control. Though this priority area has only one project in the indicative lending program, it is important to note that it also has five ongoing operations thus strengthening its need.

71. Results Area 1: Strengthening technology innovation of applications and digital financial services will entail strengthening of the Innovation Hub at the National University of Lesotho (NUL)-Lesotho National Development Corporation (LNDC) and the establishment of the NUL-LNDC Industrial Park. The support will strengthen the incubation and acceleration programs at NUL that will focus on innovations in ICT platforms and applications, Fintech technologies, Advanced Forth Industrial Revolution Technologies (block chains, Internet of things, remote sensing, dig data, Artificial Intelligence, drones) and technology related to agro-business. Once the innovations graduate from the Innovation Hub, they will be considered for relocation to the NUL-LNDC Industrial Park which will be established through co-financing with other donors (e.g. MCC under the Lesotho Impact Investment Fund). The support will also address the legal and regulatory aspects relating to intellectual property and industrial standards. With the improved rural mobile coverage of almost 99% through the Bank-financed Lesotho e-Government Infrastructure Phase II project, the potential for bridging the knowledge gaps in value chain, particularly in agriculture will be achieved.

72. **Results Area 2: Strengthening economic and financial governance**: The Government's PFM Reform Policies remain a priority to strengthen the legal framework, systems and institutional capacity. The Bank will provide institutional support to enhance the efficiency, effectiveness, transparency and accountability in the use of public resources, address fiduciary shortcomings through strengthening the public finance regulatory framework, internal control and audit, and corporate governance practices as well as the oversight institutions such as the Office of the Auditor General, Directorate on Corruption and Economic Offences (DCEO), and Public Accounts Committee (PAC). In the area of procurement, additional technical assistance and capacity building support will be provided by the Bank to operationalize the new one when the current draft Public Procurement Bill is enacted into law. This will help create a transparent and competitive procurement system in order to align expenditures to the approved budget and improve the quality of public expenditure that is necessary for the fiscal consolidation plan.

73. **Results Area 3: Improving the business environment and entrepreneurship for private sector–led growth and job creation.** It will support reforms to reduce the cost of doing business, facilitate access to finance by local enterprises, enhance the ability of local enterprises to take advantage of regional opportunities, and facilitate increased private investment in the productive sectors. The business environment will be further improved by the development of the necessary policy, legal and institutional regimes for PPPs that unlock private investment, building on the gains made under the Bank-financed Economic Diversification Support Project. There is need to consolidate the gains made in business climate reforms with the establishment of a One-Stop Business Facilitation Centre, improvements in legal and regulatory framework, PFM reforms, and corporate governance. The Bank has supported the development of an enabling policy environment in the tourism sector (e.g. Tourism Policy, and Master Plan), business incubation strategy and entrepreneurship program to build the productive capabilities of SMEs. This will unlock the potential of the private sector, help restore macroeconomic stability, and spur economic growth, a sine qua non for job creation. This priority area will contribute to *"Improve the Quality of the Life of the People of Africa" and "Industrialize Africa* of the High 5s priorities.

74. **Main Outcomes/Key Results under Priority Area II:** The Bank's support to technological innovation of applications and financial services to economic governance is expected to increase broadband penetration from the current 56% of penetration for the population to 57.5% by the end of the CSP period in 2024. In addition, the electronic financial transactions in the country are expected to increase from the current 40% to about 90% in 2024. Other key outcomes include improved World Bank Ease of Doing Business Ranking from the current ranking of 106 out of 193 countries to a ranking of less than or equal to 100 in 2024, while tax to GDP ratio is expected to increase from 23% in 2019 to 25% in 2024. The Bank's support to PFM will help improve (i) transparency and oversight of the budget; (ii) competition, value for money and controls in procurement; (iii) effectiveness of internal audit and internal control; and (iv) quality and timeliness of annual financial statements. **The private sector will play a major role in both priority areas I and II and serve as the engine of growth.** The Bank will strengthen its capacity in terms of providing credit, training and mentorship and creating a business friendly environment.

5.3 Indicative Lending Program and Non-Lending Program

75. The Bank has developed a rolling indicative lending program (ILP) (2020-2024) that is aligned to the priority areas of the CSP, NSDP-II, TYS and High 5 priorities. It includes 5 operations: i) an agriculture value chain development project, ii) a youth empowerment project, iii) a Line of Credit to LNDC, iv) technology innovation project, and v) an institutional support project. The total cost is UA 25 million broken down as follows: UA 15 million (sovereign operations) and UA 10 million (non-sovereign operations) - Annex A.2.1. There is a strong possibility that the agriculture value chain project will be co-financed with other DPs, notably the World Bank. In terms of sectoral distribution of the ILP, *agriculture and finance sectors are the largest beneficiaries accounting for 40% each of the total commitment, followed by social sector (12%) and institutional support (8%).* In terms of distribution of resources as per the High 5s, the ILP is dominated by *'Feed Africa' and 'Industrialize Africa' each with 40% of the total commitments, followed by 'Improve the Quality of Life of the People of Africa' (20%).*

76. In terms of demand-driven analytical work (Annex A.2.2), the Bank will undertake studies in domestic resource mobilization, youth unemployment and value chain development as well as training in gender mainstreaming. The estimated cost of non-lending program is UA 0.2 million.

5.4 Country Dialogue Issues

77. **The proximity to Lesotho has facilitated country dialogue and engagement with key stakeholders**. The following have been identified as potential dialogue issues:

i. Dialogue on debt and payment arrears is important to restore macroeconomic stability. A study on domestic resource mobilization will be undertaken in view of the fiscal crisis;
ii. Dialogue on portfolio management focusing on issues relating to project implementation and portfolio quality**;**
iii. **Youth unemployment**: Youth unemployment poses a serious challenge. Therefore, the Bank will undertake a study in this area; and,
iv. **Two key policy reforms** to be undertaken include public–private partnership and PFM**.**

5.5 Financing Strategy

78. **This CSP is being prepared at a time when the Bank is scaling up interventions to be aided by a new capital increase.** This is a unique opportunity for Lesotho as GCI VII will help leverage non-sovereign operations. Historically, Lesotho's ADF resources hovers around UA 15 million (USD 21) million) per cycle. This amount is not sufficient to meet the priority needs of the country. The Bank will leverage its position as a trusted partner to explore local currency lending, co-financing, PPP financing modality, and financing opportunities with the African Investment Forum and attract regional funds, trust

funds, as well as the African Legal Support Facility. A risk assessment will be undertaken to determine whether Lesotho can be upgraded from a GAP to a blend country in order to benefit from both ADF and ADB resources thus enabling the Bank to scale up its operations.

5.6 Implementation Arrangements, Monitoring and Evaluation

79. **The Result-based Activity Framework in Annex A. 1.1 will serve as the main monitoring tool. Given the fluid political situation in Lesotho, close monitoring, regular updates and reviews will be undertaken**. A mid-term review report will be prepared for the Board as well as a CSP Completion Report. At the project level, there will be timely submission of quarterly progress reports, routine supervision missions and Project Completion Reports.

5.7 Risks and Mitigation Measures

80. **The following risks may affect the achievement of CSP and NSDP II objectives:**

i. **Weak implementation capacity** poses fiduciary risks to CSP implementation. The Bank will improve the capacity of PIUs and institutions under priority area 2;

ii. **Political uncertainties** remains a threat to political stability. RDGS will provide early warning signals of shifting government priorities, if any, through close monitoring; and,

iii. **The current drought** might divert the country's resources meant for supporting the strategy. At the request of the government, the Bank will provide emergency assistance.

6. CONCLUSIONS AND RECOMMENDATIONS

6.1 Conclusion

81. **Lesotho has made progress on both the economic and political fronts since independence in 1966**. However, it has been plagued by a slew of coalition governments involving costly elections since 2012 and more recently a liquidity and fiscal crisis. The CSP is timely, focusing on employment creation, inclusive growth and hence an ideal framework for addressing Lesotho's development challenges. It will promote an integrated approach to ensuring that interventions have spin-offs into other sectors. In order to complement the KoL's efforts, the CSP for 2020-2024 identifies two complementary and mutually reinforcing priority areas: **i) Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation; and ii) Leveraging Technology for Improved Governance and Institutional Capacity**.

6.2 Recommendation

82. The Board of Directors is hereby requested to consider and approve the CSP 2020-2024 for the Kingdom of Lesotho.

ANNEXES

ANNEX A.1.1: CSP STRATEGIC ALIGNMENT MATRIX.

CSP Priority Area I: Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation.	
Lesotho National Strategic Development Plan II (2018/19 - 22/23).	**African Dev. Bank Corporate Policies.**
• **Theme of NSDP-II: Economic and Institutional transformation for private sector led-jobs and inclusive growth. Key Priority Areas: (i)** Enhancing Inclusive & Sustainable Econ. Growth & Private Sector Job Creation; (ii) Strengthening Human Capital; and (iii) Building Enabling Infrastructure.	**Ten Year Strategy (2013-2023).** Operational Priorities: Infrastructure Development, Private Sector Dev, Skills and Technology. Areas of special emphasis: (i) Agriculture; (ii) Finance; and (iii) Gender High Five Priorities: (i) Feed Africa: (ii) Industrialize Africa and (iii) Improve the Quality of Life of the People of Africa
Country Sector Strategy.	**Bank Sector Strategy.**
• Energy: The Kingdom of Lesotho Energy Policy 2015-2025. • Agriculture: National Medium Term Investment Program and Lesotho Integrated Plan for Agricultural Development 2019-2023. • Water and Sanitation Policy 2007. • Water and Sanitation Operational Strategy 2016.	• Energy Sector Policy; New Deal on Energy for Africa (2016-25). • Agriculture: Strategy for Agricultural Transformation in Africa 2016-2025; Staple Crops Processing Zones: A Flagship Program of the Feed Africa Strategy. • Jobs for Youth in Africa Strategy (2016-2025). • Private Sector Development Policy (2013) – focusing on enterprise development. • Policy for Integrated Water Resource Management (2000).

Country Development Results.			**Bank Interventions.**	
Indicators	**Baseline 2019**	**Target 2024**	**Investments/Sectors**	**Amount (UA m)**
Agriculture Value Chain				
• Increased crop production & productivity (t/ha). • Increased skilled & unskilled jobs created (#).	0.5 0	2.5 1,500	Agriculture Value Chain Project – 2020.	10.0
Social – Enable Youth Program				
• Increased establishment of new agriculture related businesses (#). • Increased youth employment created (#).	0 0	500 750	Youth Empowerment and Job Creation Support – 2021.	3.0
Non-Sovereign Operation				
• Increased SMEs with access to finance (%).	10	30	LoC to Lesotho National Dev. Corporation – 2022.	10.0
Energy				
• Reduced transmission & distribution energy losses (%). • Increased access to electricity (%).	14 42	10 60	Energy Projects – Ongoing and to be completed in 2022.	8.2
Water and Sanitation				
• Increased access to safe drinking water (% of population). • Increased access to improved sanitation facilities (% of population).	82 45	=>90 55	Water & Sanitation Projects – ongoing and to be completed in 2022.	12.3

Annex A.1.1 (cont.).

CSP Priority Area II: Leveraging Technology for Improved Governance and Institutional Capacity.					
Lesotho National Strategic Dev. Plan II (2018/19 -22/23).				**African Dev. Bank Corporate Policies.**	
Theme of NSDP-II: Economic and Institutional transformation for private sector led-jobs and inclusive growth. Key Priority Areas: (i) Strengthening National Governance and Accountability Systems; and (ii) Strengthening Technology Innovation of Applications and Digital Finance Service.				**Ten Year Strategy (2013-2023)** Operational Priorities: Industrialization; Governance & Accountability; and Skills and Technology. Areas of special emphasis: ICT; Governance and Institutional Capacity. High Five Priorities: (i) Improve the Quality of Life of the People of Africa; and (ii) Industrialize Africa.	
Country Sector Strategy.				**Bank Sector Strategy.**	
Lesotho ICT Policy 2005. Lesotho Communication Policy 2008. National Broadband Policy 2014.				ICT Operational Strategy (2008 – 2014). Bank Industrialization Strategy for Africa (2016-2025).	
Dialogue and Reforms for National Transformation 2017				Governance Strategic Framework and Action Plan (GAP-II).	
PFM Reform Action Plan (2019-2023). Lesotho Revenue Authority Strategy (2018-2023).				Governance Strategic Framework and Action Plan (GAP-II).	
Country Development Results.				**Bank Interventions.**	
Indicators	**Baseline 2019**	**Target 2024**		**Investments/Sectors**	**Amount (UA m)**
Building E-Government infrastructure, services and capacity					
• Increased broadband penetration (% of penetration per population). • Increased Govt. digital services in rural areas (# of services available to citizens in rural areas).	56 50	57.5 150		e-Government Infrastructure II – approved 18 October 2019.	10.2 (ADF)
Institutional Support and Capacity Building					
• Increased external audit coverage (%). • Increased internal audit coverage (%).	80 65	100 85		Inst. Support Project – 2022; & ISP for Enhancement of the PFM system– ongoing and to be completed June 2020.	2.0; and 2.6 (ADF-Grants)
Building Revenue Collection Capacity					
• Increased revenue collection (tax to GDP ratio), (%).	23	26		Tax Modernization Project to be completed in 2022.	5.0 (ADF)
Developing SMMEs and diversifying range of business services.					
• Improved World Bank Ease of Doing Business Ranking (# out of 193 countries). • Increased per capita income (%).	106 0	<100 10		Economic Diversification Support Project – ongoing & to be competed in 2022.	7.9 (ADF)
				Knowledge products (DRM, etc.)	0.2

ANNEX A.1.2: PERFORMANCE MATRIX.

Performance Area	Monitoring Indicators	Baseline (2019)	Target (2024)	Data Source
Operational Results from Projects (including carried over projects from CSP 2013-2017 and CSP Update (2018-2019). **OUTCOMES**	**Agriculture Value Chain**			
	• Increased crop production and productivity (T/ha) • Increased skilled and unskilled jobs created (#).	0.5 0	2.5 3000	MoA Annual Report
	Social			
	• Increased establishment of new agric. related businesses (#). • Increased youth employment on skilled & unskilled jobs (#).	0 0	500 750	Statistics Bureau Rept.
	Energy			
	• Reduced transmission & distribution energy losses (%). • Increased access to electricity (%).	15 42	10 60	MoE and LEC Reports
	Water and Sanitation			
	• Increased access to safe drinking water (% of population). • Increased access to improved sanitation facilities (% of pop).	82 45	>90 55	MoW annual report
	ICT – e-Government infrastructure and innovation technology			
	• Increased broadband penetration (% penetration per pop.). • Increased government digital services in rural areas (# services available to citizens). • Increased electronic financial transactions (%).	56 50 40	57.5 150 90	Lesotho Communication Authority
	Institutional support and capacity building in financial management and governance			
	• Increased internal audit coverage (%) • Increased external audit coverage (%)	80 65	100 85	
	Building Revenue Collection Capacity			
	• Increased revenue collection (tax to GDP ratio), (%).	23	26	
	Developing SMMEs & diversifying range of business services.			
	• Improved World Bank Ease of Doing Business (Ranking out of 193 countries). • Increased per capita income (%)	106 0	<100 10	
OUTPUTS (Outputs from projects proposed in CSP)	**Agriculture Value Chain**			
	• Certified nurseries/greenhouses established (#). • Rural access roads upgraded (km). • Rural markets constructed/upgraded and equipped (#).	0 0 0	6 20 5	IPR Reports and Project Quarterly Reports
	Social – Youth Empowerment & Job Creation Support			
	• Operational One-Stop-Shops established (#). • Start-ups established (50% women), (#). • Youth Agri-Business Incubation Centers upgraded and/or equipped (#).	0 0 0	3 500 3	IPR Reports and Project Quarterly Reports
	Energy			
	• New distribution lines rehabilitated. • 1 substation upgraded & 13 switching stations rehabilitated (No/Yes).	120 No	188 Yes	IPR Reports and Project Quarterly Reports
	Water			
	• New water pipeline completed (km) • Public water points constructed (#) • New water supply systems completed (#)	120 100 4	200 450 9	IPR Reports and Project Quarterly Reports
	ICT – e-Government Infrastructure II			
	• Mobile towers in unserved rural areas constructed (#). • Fibre optic cable installed (km). • e-Parliament system established (No/Yes). • ICT officers trained (50% female) (#).	420 0 No 300	468 96 Yes 1000	IPR Reports and Project Quarterly Reports

Performance Area	Monitoring Indicators	Baseline (2019)	Target (2024)	Data Source
OUTPUTS (Outputs from projects proposed in CSP)	**Institutional support and capacity building in financial management and governance**			
	• New internal audit manual adopted and audit committee established and operational (No/Yes).	No	Yes	IPR Reports and Project Quarterly Reports
	• New Audit Act of 2017 and audit regulation approved (No/Yes).	No	Yes	
	• OAG, IAD, and Public Procurement Officers completed a certified professional development program (#).	100	150	
	Building Revenue Collection Capacity			
	• E-taxation, and VAT compliance technology installed and operational (No/Yes).	No	Yes	IPR Reports and Project Quarterly Reports
	• Tax officers received training in professional development courses (#).	0	200	
	Developing SMMEs & diversifying range of business services.			
	• Enhanced entrepreneurial skills for SMMEs (No/Yes).	No	Yes	IPR Reports and Project Quarterly Reports
	• Improved capacity for standards and certification of products (No/Yes).	No	Yes	
CROSS – CUTTING (climate change & gender)	• Training of ICT officers (#), of which	0	700	• Project Implementation Reports.
	➢ Female	0	350	
	➢ Youth	0	100	
	• Training of tax officers (#), of which	0	200	
	➢ Female	0	100	
	➢ Youth	0	20	
	• Jobs created in Agriculture Value Chain and Youth Empowerment Projects (#), of which	0	3000	
	➢ Female	0	750	
	➢ Youth	0	1500	
POLICY ADVICE & KNOWLEDGE	• Domestic Resource Mobilization	No	Yes	• ESW Reports.
	• Youth Unemployment	No	Yes	
	• Agriculture Value-Chain Developments	No	Yes	
FINANCIAL LEVERAGING	• Co-financing (UA m) - n new agric. project	0	10	• Project Appraisal Reports.
	• Parallel financing (UA m) – EU, WB on ongoing projects.	27	35	
	• Increased PPP Transactions (#).	0	1	
PORTFOLIO PERFORMANCE	• Time lapse approval to signature (months).	2.6	< 3	• Standalone CPPRs • Combined CSP MTR & CPPR.
	• Time lapse approval to first disbursement (months).	15.6	< 6	
	• Disbursement Rate (%).	45	>60	
	• Flagged (RED) projects in Flashlight Report.	0	<20	
	• Portfolio Rating (1 – highly unsatisfactory, 4 – highly satisfactory).	3.0	>3.0	
DEVELOPMENT COORDINATION AND HARMONIZATION	• Sector working groups chaired by the Bank (#).	0	1	BTOR and Donor Coordination Reports
	• Sector working groups participated by the Bank (#).	1	2	
SUSTAINABILITY & CAP. BUILDING	• Annual Portfolio Improvement Reviews Conducted (#).	0	5	• Project Reports.
	• Fiduciary Clinics undertaken (#).	0	2	

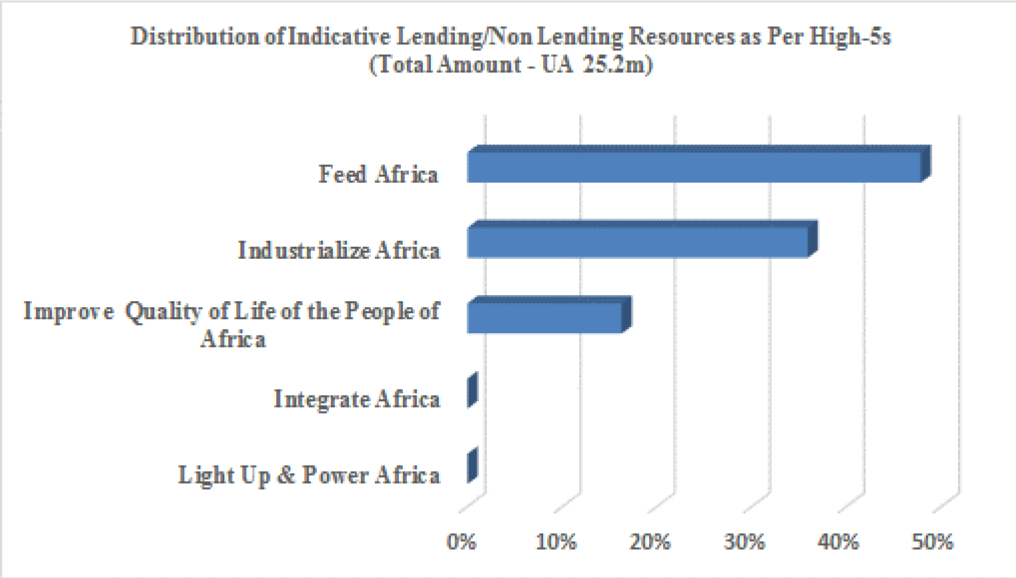
ANNEX A.2.1: INDICATIVE LENDING PROGRAM (2020-2024)

No	Name of Operation	Funding Source	Amount (UA m)	Sector	Contribution to High-5s	Planned Approval Date
Priority area I: Strengthening Value Chains for Sustainable and Inclusive Growth and Job Creation						
1	Agriculture Value Chain	ADF	10.0	Agriculture	Feed Africa	2020
2	Youth Empowerment and Job Creation Support Program	ADF	3.0	Social	Improve the Quality of Life of the People of Africa	2021
3.	Technology Innovation	ADB	2.0	ICT	Industrialize Africa	2021
4.	Line of Credit to LNDC	ADB	8.0	Finance	Industrialize Africa	2023
		sub-total	23.0			
Priority area II: Leveraging Technology for Improved Governance and Institutional Capacity.						
4.	Institutional Support Project	ADF	2.0	Multisector	Improve the Quality of Life of the People of Africa	2022
		sub-total	2.0			
		Total	25.0			

ANNEX A.2.2: INDICATIVE NON-LENDING PROGRAM (2020-2024.

No	Name of Operation	Funding Source	Amount (UA m)	Sector	Contribution to High-5s	Planned Approval Date
1	Domestic Resource Mobilization	ECVP/ Admin	0.05	Finance	Improve the Quality of Life of the People of Africa	2020
2	Youth Unemployment	ECVP/ Admin	0.05	Social	Improve the Quality of Life of the People of Africa	2021
3.	Value Chain Development	ECVP/ Admin	0.05	Multisector	Industrialize Africa	2022
4.	Training in gender mainstreaming	Trust Funds	0.05	Multisector	Improve the Quality of Life of the People of Africa	2022
		Total	**0.20**			

ANNEX A.2.3: CONTRIBUTION OF THE INDICATIVE LENDING/NON-LENDING PROGRAM TO THE HIGH 5S.



ANNEX A .3.1: KEY MESSAGES FROM THE 2013-2017 & 2018-2019 CSP COMPLETION REPORT AND 2019 CPPR
The Boards of Executive Directors of the African Development Bank Group approved the Country Strategy Paper (CSP) for the Kingdom of Lesotho (KoL) covering 2013-2017 in March 2013**.** The CSP was updated on 5th June 2018 to run until December 2019 pending the finalization of the second National Strategic Development Plan 2018/19-22/23 (NSDP II). It was anchored on two Pillars: **i) Infrastructure Development; and ii) Institutional Capacity Building.** The objective of the CSP was to support Lesotho's development objectives of achieving high, inclusive and sustainable growth. The CSP's pillars and main objectives were closely aligned with Lesotho's first five-year National Strategic Development Plan (NSDP) I 2013-17, notably its focus areas on infrastructure development, promotion of peace and democratic governance, and building effective institutions. **Outcomes and Outputs**: The Bank's total net commitment to Lesotho as at 31 March 2019 was UA 40.32 million supporting 8 ongoing operations with a cumulative disbursement ratio of 37.6%. In terms of overall attainment of outcomes, 76% of outcome targets had either been met or there was significant progress made towards achieving them. The remaining 25% has shown limited progress in achieving targeted outcomes. For the output indicators, 80% of output targets have either been met or significant progress has been made towards achieving targeted outputs. The remaining 20% has shown limited progress in achieving targeted outputs. The main reason for not achieving the planned outcome and output targets is due to the fact that four operations are relatively new (approved between 2016 and 2018) and are at different initial start-up phases. The outputs and outcomes targets for these operations can only be expected to be achieved during the next CSP cycle. Portfolio performance was assessed to be satisfactory as at 31st March 2019. More specifically, the overall portfolio rating improved to 3.0 (on a scale of 1-4, with 1 being highly unsatisfactory and 4 highly satisfactory) in 2019 from 2.7 in 2017, and 2.1 in 2015. **Lessons Learnt**: **Institutional and human capacity weaknesses were a major challenge to quality portfolio management**. Thus, it is recommended that the Government and Bank continue to closely monitor project implementation through institution of joint quarterly reviews of CPIPs, and follow-up of outstanding portfolio issues. **Start-Up delays: Stronger level of commitment from senior level of Government** is critical to ensuring that effectiveness conditions are met in time to avoid start-up delays and cancellations in compliance with PD02/2015. **High Attrition rates of procurement specialists due to scouting for greener pastures is adversely impacting on portfolio performance.** The Government could consider standardizing remuneration for all staff working on donor-funded projects in the country. The lessons for the DPs include the need for continued assistance which is critical for both economic and political stability; the need to balance selectivity with relevance; and need to strengthen donor coordination to enhance complementary and synergy.

ANNEX A.4.1: CODE'S COMMENTS, RECOMMENDATIONS AND ACTIONS TAKEN	
CODE Comments / Recommendations	Response /Actions Taken
Board members supported the choice of the two priority areas but recalled meagre ADF 3-year allocation of UA 15 million and advised Management to be selective and to coordinate with donors to crowd in additional financing and where possible deploy other meaningful ways to complement the limited ADF financing.	The Bank will leverage its position as a trusted partner to attract regional funds, internal and external trust funds, enclave funds, and grants. The PPP financing modality will be explored, as well as tapping into the ADB resources allocated to the country under the revised credit policy which are commensurate with the reclassification of Lesotho as a GAP country[5]. In addition, under priority area II, the African Legal Support Facility which provides funds for at least three key areas (commercial creditor litigation, the negotiation of complex commercial transactions, and capacity building) will be useful.
Board members called for enhanced policy dialogue to support the country in terms of broadening of and accessibility to regional markets They encouraged Management to focus on energizing the private sector and attract private investments to Lesotho and the extended Southern Region	The private sector will play a major role in both priority areas I and II and serve as the engine of growth. The Bank will strengthen its capacity under priority area II in terms of training and mentorship while at the same time benefitting from credit from one of the local banks to catalyze investment. In addition, the Economic Laboratories established by the Government will help catalyze private sector activity to develop value chains in support of inclusive growth and poverty reduction. In order to revitalize the sector, a number of initiatives are underway, including formulation of a PPP Policy and framework; establishment of a PPP unit; and development of a legal and regulatory framework for SEZs, among others.
Board members called for monitoring the macro-economic situation of the country, the results of the credit-worthiness assessment, and the potential of graduation into a blend country as these would guide the type and amount of financial resources available to implement the next CSP. In this regard, Management should adopt a scenario-based approach to the planning of resource mobilization for the new CSP with or without a blend country status.	Macroeconomic stability is one of the areas of policy dialogue in the CSP. Management will closely monitor the situation to ensure that the fiscal consolidation measures outlined in the 2019/2020 budget are fully implemented. A risk assessment will be undertaken to determine whether Lesotho can be upgraded from a GAP to a blend country in order to benefit from both ADF and ADB resources thus enabling the Bank to scale up its operations. Regarding the fiscal and liquidity situation, a study on domestic resource mobilization is being undertaken. It has been included in the non-lending program.
Board members called for exploring ways to ensure linkage between the new CSP with the Southern Africa RISP that is currently under preparation	The CSP will benefit from the RISP as the two are being prepared in tandem

[5] A GAP country is one whose Gross National Income (GNI) per capita has exceeded for three consecutive years the World Bank's Operational cut-off which is USD1145 for fiscal year 1st July 2018 -30th June 2019.

Continue its efforts to improve the capacity of project implementation units, enhance project quality at entry and fiduciary performance and sustain the progressing trajectory of disbursements.	The strengthening of project implementation units, enhancing project quality at entry and fiduciary performance and sustaining the progressing trajectory of disbursements are all part of the Country Portfolio Improvement Plan as annex A. 6.3
Board members called for engaging in policy dialogue with the authorities to improve governance and fight corruption.	Priority area II of the CSP focuses on economic and financial governance with special emphasis on strengthening the capacity of oversight institutions such as the Auditor General's office, the Public Accounts Committee, Accountant General's Office, and Directorate on Corruption and Economic Offences.

ANNEX A. 4.2: SUMMARY OF FINDINGS OF EXECUTIVE DIRECTOR'S VISIT TO LESOTHO
In January 2019, the Executive Director for Lesotho, Ms. Mmakgoshi Lekhethe undertook a visit to Maseru, Lesotho.
Discussions focused on the following issues: • The reclassification of Lesotho as a gap country in July 2015, its justification and implications for borrowing; • The visibility of the Bank in Lesotho in terms of local representation such as a liaison office or a non-resident economist; • Provision of technical assistance by the AfDB to strengthen the capacity of the Ministry of Finance in financial management, especially in debt management using "making finance work for capacity building" facility; • Organization of a Business Information Seminar to understand the Bank's various windows and lending opportunities; • The new CSP for Lesotho covering the period 202-2024 which will be anchored on NSDP II; • A study on opportunities for non sovereign lending operations (private sector) using the middle income country grant; • Provision of a line of credit by the AfDB for on-lending to SMMEs; • Provision by the AfDB of samples of private sector projects in other countries covering the nature, source of funds, including FAPA, and duration; • Assessment by the AfDB of the feasibility of merging LNDC and BEDCO for purposes of consolidation and effectiveness; • Provision of technical assistance by the AfDB on the viability of local development institutions; and, • Possibilities of Lesotho having a follow-up infrastructure project, in particular Metolong water project. This follow-up project will begin with a project preparation and feasibility studies to be financed by the middle income country grant.

ANNEX A.5: FINDINGS OF STAKEHOLDER CONSULTATIONS		
The CSP is a culmination of a series of consultations involving the Government, private sector, development partners (DPs) and civil society		
Category of Institutions	Parties consulted	Summary of outcomes of consultations
Government	**Ministries, Departments and Agencies (MDAs)**	• Fiscal and liquidity challenges stemming, in part, from the poor performance of the South African economy • High levels of poverty, unemployment and inequality • High rural poverty relative to urban poverty • Large disparities between rural and urban areas in terms of income levels and social amenities • Rural-urban migration owing to lack of job opportunities in rural areas • Low agricultural productivity arising from the use of rudimentary technology, small farm holdings and inadequate access to credit, fertilizers, extension and research, among other factors. • Political uncertainty due to internal rivalry in the ruling party and a weak coalition.
Development Partners	WB, UN Agencies, IMF, EU.	• Poor coordination among DPs • Low level of collaboration and limited co-financing • Need to use country systems to avoid stretching the capacities of the government • Need to share lessons and experiences • Need to align interventions with government strategies • Need to balance selectivity with relevance • Need for continuous engagement with Government
Civil Society Organizations	Lesotho Council of NGOs	• Civil society needs to strengthen partnership with the Government, DPs, and private sector • Need to strengthen the capacity of civil society to engage more effectively in peace building and development in general.
Private Sector	Post-Bank, Chamber of Commerce and Industry, Lesotho National Development Corporation, Basotho Enterprise Development Corporation	• A small private sector constituting only20% of GDP. • Inadequate access to land, market information and finance, as most of the banks are foreign owned. • The private sector is mostly inward-oriented with 71% of the firms in wholesale and retail. • Micro and small firms account for 97% of all firms; yet over half of employment is in large firms. • Economic activity is concentrated in a few industries with low value added. • The apparel industry accounts for the bulk of employment & exports. the top four accounting for 45%; • There are very little backward and forward linkages between small and large firms. • Difficulty in registering businesses, especially SMMEs. • Inadequate storage facilities. • Lack of development banks. • Poor transport infrastructure to move goods from production to marketing centers. • Low labour productivity of Basotho compared to Bangladeshis. • Minimum wages which discourages investors. • Cumbersome bureaucratic procedures in the borders. • Poor coordination among different institutions dealing with the private sector. • Inadequate skills and resources to develop products to the required global standards.

ANNEX A.6.1: ONGOING PORTFOLIO AS OF 31 DECEMBER 2019.

Project Name	Status	Finance Source	Approval Date	Project Closing Date	Amount Approved (UA)	Disb. Ratio	Disbursed Amount (UA)	Age (yrs)	Project Status	Alert - Flaslight Report	Remarks/Comments as per Flashlight Report
LESOTHO LOW LANDS RURAL WATER SUPPLY & SANITATION	OnGo	ADF	03/10/2013	30/06/2020	6.52	65.3%	4.26	6.3	NPPP		Disb. Closing date expires 1-6 mnths & less than 80%.
	OnGo	RWSSI	03/10/2013	30/06/2020	2.61	55.7%	1.45	6.3	NPPP		Disb. Closing date expires 1-6 mnths & less than 80%.
ADDITIONAL FINANCING - LOWLANDS RURAL WATER & SAN	APVD	GEF	30/05/2019	30/06/2024	3.14	0.%	0.00	0.6	NPPP		Signed & undibursed for over 3 months.
Sub-total Water & Sanitation	1	3			12.27	46.5%	5.71	4.4	NPPP		
EGOVERNMENT INFRASTRUCTURE PHASE 1	OnGo	ADF	21/10/2013	29/02/2020	2.70	66.2%	1.79	6.3	NPPP		Disb. Closing date expires 1-6 mnths & less than 80%.
	OnGo	ADF-G	21/10/2013	29/02/2020	4.80	75.5%	3.62	6.3	NPPP		Disb. Closing date expires 1-6 mnths & less than 80%.
E-GOVERNMENT INFRASTRUCTURE PHASE 2		ADF	18/11/2019		10.11	0.%	0.00	0.2	NPPP		Approved and unsigned for 60 days
		ADF-G	18/11/2019		0.07	0.%	0.00	0.2	NPPP		Approved and unsigned for 60 days
Sub-total Communication	2	4			17.68	30.6%	5.41	3.2	NPPP		
URBAN DISTRIBUTION REHAB & TRANSMISSION EXPANSION	OnGo	ADF	14/12/2016	30/06/2021	7.78	41.4%	3.22	3.1	NPPP		Satisfactory
RENEWABLE ENERGY INTEGRATION STUDY	OnGo	SCF	14/03/2018	31/12/2020	0.43	3.3%	0.01	1.9	NPPP		Disbursement closing in 13 to 15 months and less than 60%.
Sub-total Energy	2	2			8.21	39.4%	3.24	2.5	NPPP		
LESOTHO TAX MODERNISATION PROJECT	OnGo	ADF	22/11/2017	31/12/2020	5.00	22.7%	1.14	0.2	NPPP		Satisfactory
INST SUPPORT FOR ENHANCEMENT OF THE PFM SYSTEM	OnGo	ADF-G	14/10/2013	20/06/2020	2.60	86.3%	2.24	6.3	NPPP		Satisfactory
ECONOMIC DIVERSIFICATION SUPPORT PROJECT	OnGo	ADF	16/12/2016	31/12/2020	5.00	30.4%	1.52	3.1	NPPP		Satisfactory
	OnGo	ADF-G	16/12/2016	31/12/2020	2.22	35.3%	0.78	3.1	NPPP		Satisfactory
ECON. DIVERSIFICATION SUPPORT TECHNICAL ASSISTANCE	OnGo	FAPA	20/12/2017	06/06/2022	0.66	20.5%	0.13	2.1	NPPP		Satisfactory
Sub-total Mutisector/Governance	4	5			15.48	37.6%	5.82	3.0	NPPP		
Grand Total/Average	9	14			53.64	46.4%	20.18	3.3	NPPP		Satisfactory

Legend:	Flagged	Close Watch	Satisfactory
	7%	50%	43%

ANNEX A.6.2: PORTFOLIO PERFORMANCE: KEY PERFORMANCE INDICATORS AS OF 31 DECEMBER 2019.

Performance Indicator	2015	Dec.. 2017	Dec. . 2019
Active and Recently Approved Operations (No.)	4	6	9
Average Project Size (UA million)	6.6	6.5	6.0
Cumulative Disbursement Ratio (%)	25.6	26.2	46.4
Average Age of Portfolio (years)	3.8	2.8	3.3
Aged Projects (%)	0	0	0
Flagged (Red) Projects in Flashlight Report (%)	N/A	50	7
Closed Watch (Yellow)) in Flashlight Report (%)	N/A	0	50
Satisfactory (Green) Projects in Flashlight Report (%)	N/A	50	43
Problem Projects, PP (No.)	1	0	0
Potentially Problematic Project, PPP (No.)	0	1	0
Projects-at-Risk, PAR (%)	25	17	0
Commitments-at-Risk, CAR (%)	33	19	0
Time Lapse: Approval to Signature (months)	5.5	5.0	3.3
Time Lapse: Signature to Effectiveness (months)	11.1	7.6	1.0
Time Lapse: Effective to 1st Disbursement (months)	9.4	7.0	3.7
Overall Portfolio Rating (4 - Highly Satisfactory)	2.1	2.7	3.0

ANNEX A.6.3: 2019 COUNTRY PORTFOLIO IMPROVEMENT PLAN (CPIP).

Challenges/Problems Identified	Required Action	Responsibility	Timeframe
Inadequate Quality at Entry			
Limited implementation capacity at country level to execute the number of small size projects funded by the Bank. Absence of detailed design studies prior to project approval dates. Delays in loan signature by Government due to delay in parliamentary approval and ratification of loan agreement.	Develop fewer large size projects to have maximum impact of Bank interventions as well as to mobilize country's limited capacity. Bank to mobilize/leverage resources for large sized operations.	Bank and Government (MoDP).	Ongoing
	Feasibility studies and/or detailed designs studies for pipeline operations to be financed by PPF or resources from current ongoing operations in the sector..	Bank and Government (MoDP).	Immediate
	Sequencing of Bank project loan approval and Parliament ratification.	Bank and Government (MoDP)	Ongoing
	Conditions precedent to the first disbursement to be fulfilled within 6 months and the first disbursement within 6 months from the date of approval of the financing, which complies with Presidential Directive, PD 02/2015.	Bank and MoPD.	Immediate
Limited Ownership and Oversight			
Limited ownership and oversight at decision making level, which has hampered timely implementation of projects.	Ensuring project steering committees (PSCs) are functional for all projects in line with Loan/Grant agreements.	MoDP and Bank.	starting January 2018
	Undertake Joint Government and AfDB Quarterly Portfolio Review to be Chaired by MoDP and attended by relevant Directors of line Ministries, project staff and Bank Team. The meeting to be co-chaired by the Bank.	Government and Bank	Quarterly
Inadequate Implementation Capacity			
Frequent transfer of Project Staff (procurement, accountant, M&E officers) at Center and District level which has led to capacity constraints Limited implementation capacity at project execution level.	Bank to continue to undertake capacity building support on project management, M&E, procurement and FM.	Bank	2019
	Ensure all Bank funded operations have dedicated staff assigned for duration of the project life.	MoF, MoPD and EAs.	Immediate
	Undertake performance evaluation of procurement units and Government staff responsible for project implementation and disclose results to interested parties.	MoPD and EAs.	Annually
Challenges/Problems Identified	**Required Action**	**Responsibility**	**Timeframe**
Procurement			
Procurement capacity constraints coupled with high attrition rate of procurement staff at project level.	Continue to organize regular training courses for project procurement staff, relevant consultants and contractors on the Bank's procurement rules and procedures and contract management.	Bank	Annually

Delay in issuance of no-objections by the Bank mainly due to poor quality of bid evaluation reports.	Ensure no-objections issued within two weeks of submission.	Bank	Ongoing
	Improve the quality of bid evaluation reports submitted to the Bank.	Executing Agencies	Ongoing
Financial Management			
Poor follow up on the recommendations made in audit reports	Quarterly progress reports submitted to the Bank to include implementation status of audit recommendations.	Executing Agency	Quarterly
Delays in submission of annual audit reports	Ensure that annual audit reports are submitted on time – six months after close of financial year.	Executing Agency & AGO	Annually
Delay in justification of funds disbursed to special accounts.	Ensure the closure of special accounts, and any special account balances to be reimbursed as accounts are closed.	MoDP / EAs)	Quarterly
	Enforce/invoke the Bank's requirements as agreed with Government in the Loan/ Grant Agreements.	Bank	Immediate
FM capacity constraints	Continue to organize regular training courses for project FM staff on the Bank's financial management and disbursement rules and procedures.	Bank	Annually

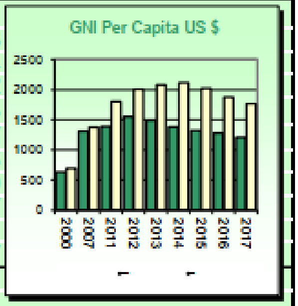
ANNEX A.7: DEVELOPMENT PARTNERS AND AREAS OF FOCUS

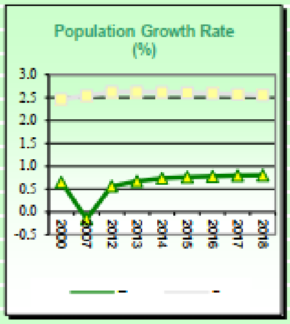
ANNEX A.7: DEVELOPMENT PARTNERS AND AREAS OF FOCUS

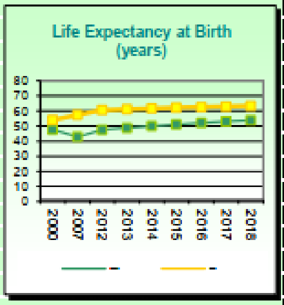
Name of Development Partner / Thematic Area	Capacity Building and Inst. Support	Budget Support and PFM	Investment Climate	Education	Health (HIV/AIDS)	Other - Health	Agriculture	Food Security and Development	Water Sector	Energy Sector	Transport	Public Private Partnerships (PPP)	Trade	Governance
African Development Bank Group		X		X		X			X	X				X
Dept. for International Development	X	X	X		X									
European Commission		X						X	X		X		X	X
Global Fund					X									
GTZ	X													X
Government of Japan				X										
International Finance Cooperation		X	X						X			X		X
International Fund for Agriculture Dev.							X							
Irish Aid	X	X			X									X
Republic of South Africa									X					
United Nations Agencies					X			X		X				X
United States of America - PEPFAR					X									
World Bank		X	X				X		X					

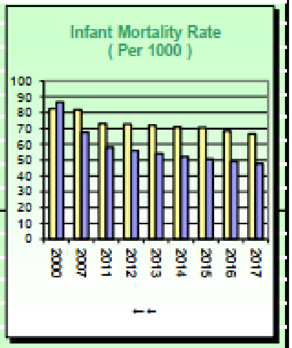
ANNEX A.8: COMPARATIVE SOCIO-ECONOMIC INDICATORS

	Year	Lesotho	Africa	Develo-ping Countries	Develo-ped Countries
Basic Indicators					
Area ('000 Km²)	2018	30	30 067	94 808	37 228
Total Population (millions)	2018	2.1	1 274.2	6 306.6	1 204.4
Urban Population (% of Total)	2018	30.2	42.9	49.8	81.2
Population Density (per Km²)	2018	72.8	43.4	68.4	34.3
GNI per Capita (US $)	2017	1 210	1 767	4 525	41 387
Labor Force Participation *- Total (%)	2018	67.0	63.5	61.8	60.6
Labor Force Participation **- Female (%)	2018	59.8	54.6	47.0	53.0
Sex Ratio (per 100 female)	2018	97.2	99.8	100.6	98.7
Human Develop. Index (Rank among 189 countries)	2017	159	...	...	...
Popul. Living Below $ 1.90 a Day (% of Population)	2007-17	59.6	31.2	11.8	0.7
Demographic Indicators					
Population Growth Rate - Total (%)	2018	0.8	2.5	1.3	0.5
Population Growth Rate - Urban (%)	2018	2.9	3.6	2.4	0.7
Population < 15 years (%)	2018	32.7	40.8	27.7	16.6
Population 15-24 years (%)	2018	19.9	19.3	16.5	11.9
Population >= 65 years (%)	2018	4.9	3.4	7.0	17.7
Dependency Ratio (%)	2018	60.3	79.2	54.6	52.6
Female Population 15-49 years (% of total population)	2018	26.1	24.1	25.4	22.4
Life Expectancy at Birth - Total (years)	2018	53.7	63.2	70.6	80.7
Life Expectancy at Birth - Female (years)	2018	57.0	65.0	72.7	83.4
Crude Birth Rate (per 1,000)	2018	26.8	33.5	20.3	10.6
Crude Death Rate (per 1,000)	2018	14.2	8.1	7.4	8.8
Infant Mortality Rate (per 1,000)	2017	66.5	47.7	31.9	4.6
Child Mortality Rate (per 1,000)	2017	85.9	68.6	42.6	5.4
Total Fertility Rate (per woman)	2018	3.1	4.4	2.6	1.6
Maternal Mortality Rate (per 100,000)	2015	487.0	444.1	237.0	10.0
Women Using Contraception (%)	2018	61.2	38.5	61.6	69.0
Health & Nutrition Indicators					
Physicians (per 100,000 people)	2010-16	6.8	33.6	119.9	297.4
Nurses and midwives (per 100,000 people)	2010-16	65.1	123.3	233.9	891.1
Births attended by Trained Health Personnel (%)	2010-17	77.9	61.7	78.5	99.0
Access to Safe Water (% of Population)	2015	81.8	71.6	89.4	99.5
Access to Sanitation (% of Population)	2015	30.3	39.4	61.5	99.4
Percent. of Adults (aged 15-49) Living with HIV/AIDS	2017	23.8	3.4	1.1	...
Incidence of Tuberculosis (per 100,000)	2016	724.0	221.7	157.0	12.0
Child Immunization Against Tuberculosis (%)	2017	98.0	82.1	84.5	91.0
Child Immunization Against Measles (%)	2017	90.0	74.4	84.0	93.8
Underweight Children (% of children under 5 years)	2010-16	10.3	17.5	15.0	0.9
Prevalence of stunding	2010-16	33.2	34.0	24.6	2.5
Prevalence of undernourishment (% of pop.)	2016	12.8	18.5	12.3	2.7
Current health expenditure (% of GDP)	2015	8.4	5.3	5.4	12.6
Education Indicators					
Gross Enrolment Ratio (%)					
Primary School - Total	2010-17	104.8	99.7	104.3	102.6
Primary School - Female	2010-17	103.0	97.6	104.8	102.5
Secondary School - Total	2010-17	56.0	52.1	72.4	108.5
Secondary School - Female	2010-17	64.5	49.8	71.9	108.3
Primary School Female Teaching Staff (% of Total)	2010-16	75.0	48.7	62.1	81.5
Adult literacy Rate - Total (%)	2010-16	76.6	64.3	83.5	...
Adult literacy Rate - Male (%)	2010-16	67.7	77.0	87.9	...
Adult literacy Rate - Female (%)	2010-16	84.9	61.3	79.2	...
Gouvernment expenditure on Education (% of GDP)	2010-17	...	4.4	4.3	5.2
Environmental Indicators					
Land Use (Arable Land as % of Total Land Area)	2016	11.6	8.7	11.4	10.1
Agricultural Land (as % of land area)	2016	77.6	41.8	38.3	35.1
Forest (As % of Land Area)	2016	1.6	23.1	31.9	29.0
Per Capita CO2 Emissions (metric tons)	2014	1.2	1.2	3.5	10.9





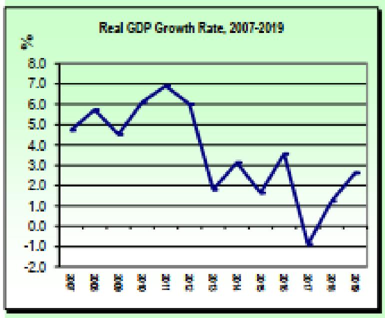


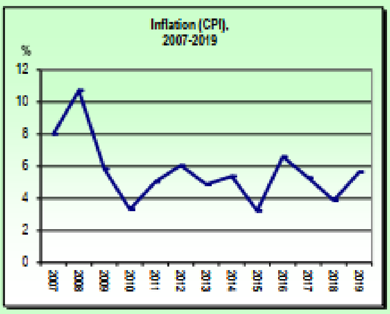


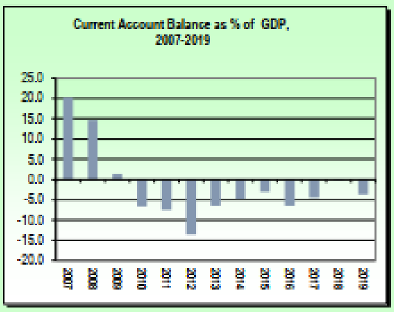
Sources : AfDB Statistics Department Databases; World Bank: World Development Indicators

ANNEX A.9: SELECTED MACROECONOMIC INDICATORS

Indicators	Unit	2010	2014	2015	2016	2017	2018 (e)	2019 (p)
National Accounts								
GNI at Current Prices	Million US $	2 674	2 961	2 871	2 821	2 702	...	...
GNI per Capita	US$	1 310	1 380	1 320	1 280	1 210	...	...
GDP at Current Prices	Million US $	2 386	2 615	2 465	2 305	2 579	2 632	2 209
GDP at 2000 Constant prices	Million US $	2 386	2 838	2 917	3 009	2 941	2 967	3 003
Real GDP Growth Rate	%	6.1	3.1	1.6	3.6	-0.9	1.2	2.6
Real per Capita GDP Growth Rate	%	5.0	2.4	0.9	2.8	-1.7	0.4	1.8
Gross Domestic Investment	% GDP	28.4	31.4	26.8	26.8	26.8	25.4	26.4
Public Investment	% GDP	13.9	14.0	11.0	12.5	10.3	9.7	10.4
Private Investment	% GDP	14.5	17.4	15.8	14.3	16.6	15.7	16.0
Gross National Savings	% GDP	17.9	25.8	24.2	20.5	25.6	24.5	24.1
Prices and Money								
Inflation (CPI)	%	3.3	5.4	3.2	6.6	5.3	3.9	5.6
Exchange Rate (Annual Average)	local currency/US$	7.3	10.9	12.8	14.7	13.3	13.2	14.2
Monetary Growth (M2)	%	11.7	49.9	45.8	44.9	52.4	75.9	...
Money and Quasi Money as % of GDP	%	46.8	2.7	3.7	4.5	16.9	13.4	...
Government Finance								
Total Revenue and Grants	% GDP	52.2	50.0	47.8	41.2	42.9	41.3	43.8
Total Expenditure and Net Lending	% GDP	55.5	51.8	49.0	49.2	46.3	46.5	47.8
Overall Deficit (-) / Surplus (+)	% GDP	-3.3	-1.8	-1.2	-8.0	-3.4	-5.1	-4.0
External Sector								
Exports Volume Growth (Goods)	%	6.0	-3.5	9.7	6.3	9.9	9.4	4.0
Imports Volume Growth (Goods)	%	2.7	1.8	6.8	-0.7	3.7	3.2	11.4
Terms of Trade Growth	%	0.4	10.7	12.6	-6.9	0.5	-0.8	1.8
Current Account Balance	Million US $	-159	-12 319	-7 755	-14 837	-11 455	-645	-8 243
Current Account Balance	% GDP	-6.7	-4.7	-3.1	-6.4	-4.4	-0.2	-3.7
External Reserves	months of imports	5.2	5.9	6.0	5.7	3.4	3.8	...
Debt and Financial Flows								
Debt Service	% exports	3.5	4.4	4.7	4.7	4.8	3.9	5.4
External Debt	% GDP	29.0	31.2	35.8	34.8	32.7	30.5	32.0
Net Total Financial Flows	Million US $	240	117	80	121	133	...	...
Net Official Development Assistance	Million US $	256	107	83	112	147	...	...
Net Foreign Direct Investment	Million US $	51	66	41	48	43	39	...







Source : AfDB Statistics Department: African; IMF: World Economic Outlook ,October 2018 and International Financial Statistics, April 2019; AfDB Statistics Department: Development Data Portal Database, October 2019. United Nations: OECD, Reporting System Division

ANNEX A.10: ARRANGEMENT WITH THE IMF

IMF Press Statement April 30, 2019

An International Monetary Fund (IMF) team, visited Maseru, Lesotho in April 2019 to discuss recent developments and the economic outlook in the context of the Article IV Consultations.

At the end of the visit, the mission released this statement:

"A four-party coalition government took office in June 2017 and, with support from a regional peacekeeping force, has brought peace and stability. However, with SACU revenues below historical averages and government expenditures remaining high, the fiscal situation has deteriorated, leading to the emergence of government payment arrears. While international reserves are at adequate levels and banks remain well-capitalized, domestic arrears are beginning to impact the broader economy, exacerbating growth challenges posed by structural impediments. Unemployment, particularly among the youth, is a major concern".

Currently, the Kingdom of Lesotho does not have an IMF Program. It conducts the usual Article IV consultations annually.

ANNEX A.11: PROGRESS TOWARDS SDGS

Indicators	2016 Baseline (or nearest year)	Data Source	Indicator Type
SDG 1: End Poverty in All its Forms Everywhere			
Target 1.1: By 2030, eradicate extreme poverty for all people everywhere, currently measured as people living on less than $1.25 a day			
Proportion of population below the international poverty line by sex, age, employment status and geographical location (urban/rural)	59.6% at international poverty line $1.90 a day (2010)	World Bank, Dev. Research Group	SDG
SDG 2: End Hunger, Achieve Food Security and Improve Nutrition and Promote Sustainable Agriculture			
TARGET 2.1: By 2030, end hunger and ensure access by all people, in particular the poor and people in vulnerable situations, including infants, to safe, nutritious and sufficient food all year round			
2.1.1: Prevalence of undernourishment	52.1%	World Bank Portal - Food and Agriculture Organization (fao.org/publications/en).	SDG
SDG 3: Ensure Healthy Lives And Ensure Well Being For All At All Ages			
TARGET 3.1: By 2030, reduce the global maternal mortality ratio to less than 70 per 100,000 live births			
3.1.1Maternal Mortality Ratio	1,024 per 100,000 live births (2014)	Lesotho Demographic and Health Survey (2014)	SDG
SDG 4: Ensure Inclusive and Equitable Quality Education and Promote Life-Long Learning Opportunities for All			
TARGET 4.1: By 2030, ensure that all girls and boys complete free, equitable and quality primary and secondary education leading to relevant and effective learning outcomes			
4.1.1D: Grade 6th SACMEQ Reading and Mathematics Achievement Scores	SACMEQ III Maths Score = 476.9 SACMEQ III Reading Score = 451.2	SACMEQ 2007	Domesticated
SDG 5: Achieve Gender Equality and Empower All Women and Girls			
Target 5.1: End all forms of discrimination against all women			
5.1.1: Whether or not legal frameworks are in place to promote, enforce and monitor equality and non-discrimination on the basis of sex	Lesotho has multiple laws and policies that promote, enforce and monitor equality and non-discrimination on the basis of sex.		SDG
SDG 6: Ensure Availability and Sustainable Management of Water and Sanitation for All			
TARGET 6.1: By 2030, achieve universal and equitable access to safe and affordable drinking water for all			
6.1.1: Proportion of population using safely managed drinking water services	Urban = 79% Rural = 77% (2014)	Lesotho Demographic and Health Survey (2014)	SDG
SDG 7: Ensure Access to Affordable, Reliable, Sustainable and Modern Energy for All			
TARGET 7.1: By 2030, ensure universal access to affordable, reliable and modern energy services			
7.1.1: Proportion of households with	Urban = 61.5% Rural = 11.8%	Lesotho Demographic and Health Survey 2014)	SDG
SDG 8: Promote Sustained, Inclusive and Sustainable Economic Growth, Full and Productive Employment and Decent Work			
Target 8.1: Sustain per capita economic growth in accordance with national circumstances and, in particular, at least 7 per cent gross domestic product growth per annum in the least developed countries			
8.1.1: Annual growth rate of real GDP per capita	2.4%	Lesotho National Accounts (2016)	SDG
SDG 9: Build Resilient Infrastructure; Promote Inclusive and Sustainable Industrialization and Foster Innovation			

TARGET 9.2: Promote inclusive and sustainable industrialization and, by 2030, significantly raise industry's share of employment and gross domestic product, in line with national circumstances, and double its share in least developed countries.			
9.2.1: Manufacturing value added as a proportion of GDP and per capita	17.35%	World Dev. Indicators Database (2016)	SDG
SDG 10: Reduce Inequality within and among Countries			
TARGET10.7: Facilitate orderly, safe, regular and responsible migration and mobility of people, including through the implementation of planned and well-managed migration policies			
10.7.2D: Migration Governance Indicator	54.5	Migration data portal	Domesticated
SDG 11: Make Cities and Human Settlements Inclusive, Safe, Resilient and Sustainable			
Target 11.1: By 2030, ensure access for all to adequate, safe and affordable housing and basic services and upgrade slums			
11.1.1D: Proportion of households living in informal housing structures by	Urban = 3% Peri-Urban = 2.77% Rural = 1.95% Total = 2.43%	Lesotho Housing and Population Census, BOS (2016)	Domesticated
SDG 12: Ensure Sustainable Consumption and Production Patterns			
TARGET 12.4: By 2020, achieve the environmentally sound management of chemicals and all wastes throughout their life cycle, in accordance with agreed international frameworks, and significantly reduce their release to air, water and soil in order to minimize their adverse impacts on human health and the environment.			
12.4.1D: Percentage of international multilateral environmental agreements on hazardous waste, and other chemicals that Lesotho is party to	100% (2015)		Domesticated
SDG 13: Take Action to Combat Climate Change			
TARGET 13.1: Strengthen resilience and adaptive capacity to climate-related hazards and natural disasters in all countries			
13.1.1D: Existence of national and local disaster risk reduction strategies	Lesotho has a National Risk Reduction Strategy		Domesticated
SDG 15: Protect, Restore and Promote Sustainable Use of Terrestrial Ecosystems, Sustainably Manage Forests, Combat Desertification, and Halt and Reverse Land Degradation and Halt Biodiversity Loss			
TARGET 15.1: By 2020, ensure the conservation, restoration and sustainable use of terrestrial and inland freshwater ecosystems and their services, in particular forests, wetlands, mountains and drylands, in line with obligations under international agreements			
15.1.1: Forest area as a proportion of total	1.63% (2015)	AO, Global Forest Resource Assessment, 2005, 2010 and 2015	SDG
SDG 16: Promote Peaceful and Inclusive Societies for Sustainable Development, Provide Access to Justice for All and Build Effective, Accountable and Inclusive Institutions At All Levels			
TARGET16.1: Significantly reduce all forms of violence and related death rates everywhere			
16.1.1D: Number of murder cases reported per 100,000 population	47 cases per 100,000 population (2015)	BOS Crime Statistics Report and National and Sub-National Population Projections (2010)	Domesticated
SDG 17: Strengthen the Means of Implementation and Revitalize the Global Partnership for Sustainable Development			
TARGET 17.1: Strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection			

17.1.1: Total government revenue as a proportion of GDP, by source	Tax revenues	Fiscal year 2015/16-Tax revenues-24.9% of GDP Taxes on income, profits, and capital gains-13.8% of GDP Income tax-6.4% of GDP		SDG

ANNEX A.12: LESOTHO-2019 COUNTRY FIDUCIARY RISK ASSESSMENT

1 Introduction

The primary purpose of the Country Fiduciary Risk Assessment (FRA) is to assess the inherent fiduciary risk associated with the use of national Public Financial Management (PFM) Systems. The FRA establishes whether the Bank can place reliance on the core PFM systems for the implementation of the Bank's aid initiatives, as well as indicate scope for capacity development where weaknesses are identified, in line with the Bank's commitment to operationalize the objectives of the Paris Declaration. In assessing the fiduciary risk, the team used recent diagnostic reviews of the Kingdom of Lesotho, including but not limited to the Public Expenditure Financial Accountability (PEFA) 2017, the 2016 Country Policy and Institutional Assessment (CPIA), the 2018 Country Portfolio Performance Assessment (PPA), and the Worldwide Governance Indicators (WGI) as updated. The Team also had discussions with the Kingdom of Lesotho Ministries, Departments, and Agencies (MDAs); as well as Development Partners. This is in line with the Bank's guidance on the fiduciary risk assessment framework for policy-based operations.

2 Overall Fiduciary Risk

The overall fiduciary risk for the Kingdom of Lesotho is assessed as High. The review identified the key areas of fiduciary risk as follows:

(i) Outdated PFM legislation,
(ii) Low budget credibility and predictability;
(iii) Weak controls on personnel and payroll records,
(iv) Low capacity and high staff turnover (in key institutions),
(v) Inadequate systems to safeguard assets from fraud, waste and abuse,
(vi) Weak cash management systems,
(vii) Weak controls over non-payroll expenditures,
(viii) Inadequate controls to ensure competition and value for money in procurement.

Regarding the enabling environment, despite Lesotho having held regular democratic elections since 1993, the country has experienced political instability due to weak State and governance institutions. The impact of these weaknesses has been exacerbated by the continuous splintering of coalition government arrangements, coupled with politicization of security establishments.

In an effort to address some of the PFM risks, the Kingdom of Lesotho with the support of the AfDB (under PFM Reform Project), has undertaken the following actions with a view to instigating Public Financial Management Reform:

(i) Enactment and implementation of a revised PFMA Act: a Bill was submitted to Parliamentary Council who recommended for repeal of old ACT and enactment of a new PFMA Act. This is work in progress;
(ii) Enactment and introduction of the Public Debt and Aid Management law (PDAM): the applicable Bill was approved by cabinet in 2018;
(iii) Debt Policy submitted to the Honorable Minister of Finance for approval and onward presentation to the Cabinet. The draft Public Debt and Aid Management Bill is ready and awaiting clearance of the Debt Policy before resubmission to Office of the Parliamentary Counsel;
(iv) Establishment of an Internal Audit Department compliant with COSO and IIA standards: IT Audit manual is being compiled while an assessment of Professional Internal Audit Program has been done. A number of internal auditors successfully completed the Internal Audit Technicians program while a further group have completed the Professional Internal Auditors training program;

(v) Budget process: being redesigned to ensure that it provides information to enable policy makers to make informed decisions. In addition, a budget strategy paper is being developed;

(vi) Cash Management: a functional Cash Management Unit (CMU) has been established. Staffing of the unit is in progress ahead of operationalization;

(vii) Access to consolidated information on Government cash balances: An inventory of all GOL controlled bank accounts is underway and plans in place to ensure monthly and quarterly cash availability reports;

(viii) The procurement Legal and Regulatory Framework is being revised and updated to underpin Improvement in Procurement Practices in the Public Administration, with measures to make Public Procurement activities fully transparent;

(ix) Capacity building of the Public Accounts Committee (PAC) being conducted by the Office of Auditor General (OAG) to improve audit reports scrutiny.

Summary of Overall Risk

Risk Pillars	Risk rating
Governance	High
Budget	High
Treasury	High
Accounting, Recording and Reporting	High
Internal Control	High
External Scrutiny and Audit	High
Procurement	Substantial
OVERALL RATING	High

3 Governance

3.1 Political stability and reform remains a priority in Lesotho. Lesotho has a complex electoral system, in which 80 members of the 120-seat National Assembly (the lower house of parliament) are elected on a constituency basis and the remaining 40 by proportional representation, the Senate (the upper house) consists of 33 non-elected members, 11 of whom are nominated by the king on the advice of the prime minister, plus the 22 principal chiefs of Lesotho. Although Lesotho has held regular democratic elections since 1993, the country has experienced political instability due to weak State and governance institutions; continuous splintering of coalition government arrangements and politicisation of security establishments. In June 2012, Lesotho established its first coalition government which collapsed, after only two years in power. The culmination of events subsequently led the country to holding three general elections[6] within a period of five years (between 2012 and 2017), all resulting in coalition governments. The next election is due in 2022, but the fragile and instable coalition governments remains a potential threat to the country's political stability, and economic development trajectory.

3.2 The current coalition government was formed with four political parties, comprising of the All Basotho Convention (ABC) with 48 seats, the Alliance of Democrats (AD) with 10 seats, the Basotho National Party (BNP) with 5 seats, and the Reformed Congress of Lesotho (RCL) with 1 seat. However, there has been ongoing infighting within the current Prime Minister Thomas Thabane's party, the All Basotho Convention (ABC), since a disputed elective conference in February 2019. At that conference, all positions in the party's National Executive Committee, except the presidency were contested amidst

[6] Lesotho has held elections in 2012, 2015 and 2017 – and on all three occasions, the sitting prime minister had lost a motion of no confidence and chosen to go to elections instead of stepping down.

intense factional battles that threatened to split the party. Though Mr. Thabane was elected unopposed as the Party Leader, but a faction that supports him doesn't want the winner of the deputy leader position, Professor Nqosa Mahao. The two factions have been through several court battles in the High Court and the appeal court, and they hold separate rallies that have led to further divisions among ordinary members on the ground. In this regard, the possibility of sweeping changes in the leadership of the largest political party in government, which is currently beset with factional battles, is a major concern for the ongoing national reforms process which hinges on a stable government.

3.3 Governance indicators shows that Lesotho needs to strengthen transparency and accountability in the use of public funds. Lesotho's rank in the MO Ibrahim Index of African Governance declined from 15^{th} in 2015 (a score of 57.8) to 16^{th} in 2018 (a score of 57.1) reflecting a marginal deterioration in overall governance. Thus governance and accountability issues remain a concern and possible contributor to fragility. Some of the governance challenges a. According Transparency International, Lesotho scored 41 points out of 100 on the 2018 Corruption Perception Index (CPI). The CPI in Lesotho averaged 38.79 points from 2005 until 2018, reaching an all time high of 49 points in 2013 and a record low of 32 points in 2006. The Bank's Country Policy and Institutional Assessment (CPIA) rates the country very low at 3.8 during the period 2014-2018.

3.4 Lesotho ranks 130 out of 140 countries ranked in the 2018 edition of the Global Competitiveness Report published by the World Economic Forum reflecting the country's poor competitiveness. Competitiveness rank in Lesotho averaged 121.17 from 2007 until 2018, reaching an all time high of 137 in 2013 and a record low of 101 in 2007. The main weaknesses identified include limited financial market development, market size, technological readiness, and infrastructure. According to the World Bank's Doing Business Report 2019, Lesotho ranks 106 out of 190 countries. It is behind South Africa (82), Botswana (86) and Zambia (87). It is evident that an uncompetitive business environment is one of the most binding constraints on private sector development. This arises from inadequate infrastructure, corruption, cumbersome business procedures, poor customs administration, lack of access to finance, high energy costs, lack of equitable and effective regulation and enforcement, and skill gaps, among others.

3.5 Despite a challenging political landscape, the country has embarked on political governance reform, and launched a National Dialogue in June 2018, supported by SADC and UN. The governance reforms aims at promoting consensus-building and a more conducive environment for reform including the review of the Constitution, the Security Sector Reforms, Judiciary, Media, and public administration reform with emphasis on depoliticisation of the civil service management. The implementation of these reforms are critical in ensuring that successive governments maintain policy continuity and sustain the economic reform agenda in order to preserve the country's focus towards its long-term strategic goals and implementation of the National Strategic Development Plan II (NDP II, 2018/19-2022/23).

4. Performance of the PFM systems and Risk Ratings

Table 2 – PFM Risk Determination

Elements	**Average Development Capacity Rating** (based on 2017 PEFA Indicators)	**Average Development Capacity Rating** (based on [7]UPDATES 2019	**Trajectory**	**Current Risk Assessment**
1. Budget				
1.1 The Budget sub-system capacity is adequate to plan (formulate) budgets for the programs and projects	0.75	0.75	-	High
1.2 The Budget sub-system capacity is adequate to execute budgetary control of programs or projects	0.75	0.75	-	High
2. Treasury				
2.1 The Treasury sub-system capacity is adequate to manage the inflow of resources and disbursements of aid funds.	0.75	0.75	-	High
2.2 The Single Treasury Account is an appropriate and reliable way to administer aid funds	0.75	0.75	-	High
3. Accounting Recording and Reporting				
3.1 The Financial Accounting sub-system is sound and capacity is adequate to record programme and/or project transactions and account for their progress and financial status.	1.5	1.5	-	Substantial
3.2 Financial Management information systems have flexibility to accommodate specific reporting requirements of programmes and projects and have procedures in place to ensure timeliness and quality of information produced.	1.5	1.5	-	Substantial
3.3 The Financial Accounting sub-system has an integrated Fixed Assets module for the proper recording and control of assets purchased with programme / project funds.	0.75	0.75	-	High
3.4 The Accounting sub-system maintains up to date records of the country's borrowings.	0.75	0.75	-	High
3.5 The Accounting systems are secure against deliberate manipulation of data and/or accidental loss of or corruption of data.	0.75	0.75	-	High
4. Internal Control				
4.1 The Internal Control sub-system capacity is adequate to control the financial operations of programs and projects.	0.75	0.75	-	High
4.2 Competition, value for money and controls in procurement are adequate	-	-	-	

[7] CSP dialogue 2019 outcomes

4.3 The Internal Audit function capacity is adequate	1.5	1.5	-	Substantial
5. External Scrutiny and Audit				
5.1 The SAI has the level of “independence” needed to enable it to effectively fulfill its functions.	0.75	1.5	↗	Substantial
5.2 The SAI has the capacity to meet its audit mandate	0.75	0.75	-	High
Risk assessment (see para 6 below): Below 0.75 = High Risk, Between 0.76-1.50 = Substantial Risk Between 1.51-2.50 = Moderate Risk Above 2.51=Low Risk				

4.1 Budget

Fiduciary Risk Rating	High

4.1.1 Review of Performance

i. Credibility of the Budget

Budgeting is guided by the Public Financial Management Accountability (PFMA) Act of 2011. The latest PEFA rated budget reliability a D, the lowest score possible, on account of large and persistent variations between estimates and actual, both for revenue, and for expenditure in more the majority of the years reviewed. Credibility of the budget has been negatively impacted by lack of reliable information and knowledge of the stock of arrears, which continue to put a strain on current budgets, since the arrears are normally paid out before the current obligations. This is exacerbated by a tendency by line ministries to generate some purchases outside of the system, coupled with the weak sanctions by the authorities for the non-compliance, which thus continues to feed the arrears. Instances of mis-procurement have also been recorded, which however result in unbudgeted liability for the government. Low budget credibility could therefore be a function of both low budgeting capacity, and inadequate budgetary control whereby government fails to contain actual expenditure within approved levels, made worse by delays in the generation of reliable outturn reports.

ii. Comprehensiveness and transparency of the budget

The reviewed Budgets were presented in accordance with economic, administrative and sub-functional classifications which are consistent with GFS 2001, but not COFOG standards. However, it should be acknowledged that in addition to a revision of the chart of accounts, the government has set out to attain compliance with the cash basis GFS and COFOG, followed by full implementation of cash-basis IPSAS. The comprehensiveness and transparency rating is therefore expected to improve once full COFOG and GFS compliance is attained. Current comprehensiveness is also negatively affected by incomplete data on donor support, especially contributions from China and USAID, which is not always reflected in the budgets. Information on non-tax revenues is scanty, incomplete, and unreliable, resulting in budgets whose basis can be questionable. This is made worse by the regular exclusion of information on large numbers of State Owned Enterprises (SOEs), Autonomous Agencies, District Councils and other Extra-Budgetary Units (EBUs). Lastly, ministries present summarized output/performance plans, complete with indicators but it is unclear if the plans are derived from the approved strategies, nor demonstrate clear links to the budget, as no budget data is attached. In terms of transparency, access to fiscal information remains limited on account of outdated GoL websites, and limited financial information where paper reports on government performance are circulated.

iii. Policy-based budgeting

The MoF's Macroeconomic Policy and Management Department (MPMD) was established in the early 2000s, with the aim of building technical capacity and developing forecasting tools. Since then, the unit has grown and is now well established with requisite skilled staff. The MPMD mainly uses an IMF-type Financial Programming model to produce its three-year medium-term macro-fiscal forecasts, which feed into the budget strategy paper. The underlying assumptions giving rise to the forecasts are never disclosed. Further, the macro-fiscal forecasts made by the MoF are hampered by a lack of timely and accurate macroeconomic data and weak coordination across departments and agencies. In addition, there is significant delays in releasing actual statistical figures by the Bureau of Statistics, meaning that most data used are forecast figures. This has serious and negative implications on data quality. Thus, according to the development partners, including the IMF, there is a need to improve the reliability of macro-fiscal forecasts and the medium-term fiscal framework (MTFF), possibly through:

• Improving coordination and information exchange;
• Strengthening the macro-fiscal forecasting model by correcting historical inconsistencies within the existing database;
• Preparing macro-fiscal forecasts at the beginning of the fiscal year and updating these before the budget strategy paper is approved, and;
• Developing analytical capacity to assess the impact of fiscal risks on public finances so that these can be incorporated into the forecasting and fiscal policymaking process.

Last, while a National Development Plan (NDP) exists, there appears to be only a very weak between this and the annual budgets- meaning that the NDP does not really guide the allocation of resources in the budget. The annual budget presents estimates of expenditure for the budget year and the two following fiscal years allocated by administrative and economic classification. As indicated, the economic classification is according to GFS 2001 but COFOG is not applied. Nevertheless, evidence from previous year's budget compared to current year's figures clearly point to a very weak MTEF. It is said that the process merely exists but is not functional. It appears as though at the beginning of each fiscal year, budget formulation and preparation starts afresh without any recourse to previous year's forecast. In year, while clear rules exist for any budget adjustments, the rules unfortunately allow for extensive administrative reallocations and expansion of the budget is accepted with ex post approval.

iv. Predictability and control in budget execution

The Lesotho Revenue Authority (LRA), is in place and has responsibility for collecting the bulk of domestic revenue (in excess of 90%), and provides necessary tax information to taxpayers. The information is easily accessible on the LRA website as well as at the LRA offices. LRA uses structured and systematic procedures for ensuring tax compliance. LRA uses two sets of software for tax management:

- ASYCUDA for Customs; and
- Oracle-based Enterprise Taxation and Policy Management (ETPM) for VAT and Income Tax.

The two platforms are linked only on the payment segment; meaning any information and/or update on ASYCUDA cannot be automatically viewed by ETPM and vice versa. In addition, neither of the software is linked to the IFMIS. Even though Tax Identification Numbers (TINs) are automatically generated, it remains a challenge to uniquely detect multiple registrations of taxpayers especially with the absence of a single national identification system - the current practice involves the use of either a driver's license or passport. Another challenge is the inability of LRA to detect tax evasion from company directors/shareholders with multiple companies.

Domestic revenues account for approximately 45% of total revenue, with Southern African Customs Union (SACU) revenues accounting for another 45%. Of late, this has been unstable, volatile, and on a sustained downward spiral, negatively impacting predictability.

The balance is made up of non-tax revenue, which is even less organized: no non-tax revenue unit exists within MoF to coordinate and monitor the non-tax revenues. There is thus no reliable data on unreported non-tax revenue (it is believed that at least half of non-tax revenue remains unreported). Whereas the Office of the Accountant General could generate a monthly non-tax revenue report from the Integrated Financial Management information System (IFMIS) for timely monitoring, a quarterly in-year budget outturn report is produced instead.

Currently, there is no mechanism for complete and comprehensive revenue accounts reconciliation within the revenue administration framework, both for tax and non-tax revenue. The only reconciliation that takes place within LRA is between collections and remittances as well as the usual bank reconciliations. 'Complete Revenue Accounts Reconciliation' refers to the process of comparing total revenue (tax and non-tax) assessed in a given period to actual revenue collected, then arrears which arise as a result of the difference between revenue assessed and revenue collected, and finally comparing actual revenue collections to total revenue transferred to Ministry of Finance Treasury. Complete revenue account reconciliation assures effective revenue accountability, but is not currently exercised.

On the expenditure side, there are no reliable figures on the stock of expenditure arrears from central government. Most line ministries procure goods and services without an IFMIS generated and approved purchase order, leading to unrecorded and unapproved commitments. Officials from the Office of the Accountant General confirmed that the stock of expenditure arrears outside IFMIS are significant but could not determine the exact figure. Further, expenditure arrears from state-owned enterprises pose fiscal risk to central government, as amounts due by the likes of the Lesotho Electricity Company can be significant. Arrears tend to have the effect of crowding out the current budgeted expenditures.

4.1.2 Current Risks– The main risks currently associated with the sub system relate to:

(a) The indeterminate stock of expenditure arrears,
(b) Incomplete information on donor contributions;
(c) Inaccurate and unreliable macro-economic data;
(d) Volatility of SACU revenues,
(e) Absence of reliable data on unreported non-tax revenues.

4.1.3 Mitigation

The Government has prioritized the elimination and curtailment of accumulation of arrears. There are mechanisms (including tax related bills such as income Tax Bill and VAT Bill) put in place aimed at achieving efficiency in domestic revenue mobilization to finance government programmes while limiting the dependence on external financing. Other reforms that are underway and will improve the performance in the budget area include:

- Fiscal and budget bulletin has been introduced and is published on quarterly basis;
- Citizen’s budget has also been introduced and first issue has already been published;
- Programme performance based budgeting (PPBB) framework has also been rolled out to all MDAs. A comprehensive performance framework is expected to be defined and introduced to complete and consolidate the reform;
- Development of draft national planning and budget regulations completed;
- Development of budget guidebook (i.e guidelines and procedures) is almost completed

4.1.4 Overall Ratings

Overall risk rating for the budgeting sub system was **High** at May 2019.

4.2 Treasury

Fiduciary Risk Rating	High

4.2.1 Review of Performance

The sub system is also governed by the PFMA Act together with the supporting Treasury regulations. There is no operational Treasury Single Account (TSA) within the central government banking framework as yet. The GoL has five main treasury bank accounts, namely:

(i) Main Revenue Account;
(ii) Recurrent Expenditure Account;
(iii) Trust Account;
(iv) Main Consolidated Fund Account; and
(v) Capital Account.

Additionally, the Treasury system includes about 20 ministry own revenue collection accounts (which are regularly swept into the Main Consolidated Fund Account), 9 sub-accountancy revenue accounts (also swept weekly) and about 18 sub-accountancy bank accounts for payments and trusts. Furthermore, there are more than 250 government bank accounts outside the treasury system, maintained and operated by line ministries with authority from the Treasury. These bank accounts include donor financed project accounts as well as own revenue (internally generated fund) accounts, of which Treasury has no information with regards to the balances thereto. Also lacking is the electronic banking platform needed to provide an interface between the banks and IFMIS that will facilitate real-time daily, weekly or monthly reconciliations as required by good practice. Treasury only obtains hard copies of bank statements for reconciliation purposes, and consolidation of treasury managed bank balances is only done monthly. The remaining 250 odd bank accounts remain outside this consolidation system, quantum unknown. Daily cash consolidations enable efficient and effective cash management, but this is currently lacking. Overall therefore, treasury management functions are weak.
Treasury Regulations 2014, require line ministries to prepare and submit annual cash flow forecasts to MoF for consolidation by the Cash Management Unit. In practice, this is never adhered to.
The PFMA Act on its part requires line ministries to prepare annual procurement plans, once budget appropriations are approved by parliament. The procurement plans would be used as input to annual cash flow plans, in order to facilitate the setting of expenditure commitment ceilings. The current practice however is not effectively coordinated as a result of the non-existence of annual cash flow plans. Instead, the MoF issues quarterly expenditure commitment ceilings to line ministries, while actual cash is released on a monthly basis. The cash planning system is therefore not functioning as envisaged, nor in line with good practice!

4.2.2 Current Risk

(a)Lack of a functional Single Treasury Account
(b)Delays in access to funds
(c)Unrealistic budget

4.2.3 Mitigation

Cash planning & forecasting tools have been developed which will enable line ministries have realistic warrant requests per quarter. The structure of the Treasury Single Account has been agreed, and an upgraded version of IFMIS has been launched w.e.f April 2019. The upgraded IFMIS has capability to perform daily bank reconciliations automatically.

4.2.4 Overall Risk Rating

The overall rating for the treasury sub system at May 2019 was **High.**

4.3 Accounting and Reporting

Fiduciary Risk Rating	High

4.3.1 Review of Performance

The sub system is guided by the PFMA Act 2011. Since 2008, financial accounting and reporting has been run on an IFMIS, running on EPICOR software. The system provides an adequate audit trail, with sufficient passwords control to regulate unauthorized access. This should ordinarily guarantee financial data integrity, however, because prior years' are not closed within IFMIS, this allows for retrospective data entry and possible manipulation. In-year budget execution reports are compatible with the original budget classifications and allow for easy statistical analysis. Another plus is that progress has been made towards making annual financial reports compliant with IPSAS (Cash Basis). But numerous challenges still remain:

- Some line ministries generate transactions outside the IFMIS, severely impacting the completeness of the records;
- Bank account reconciliations are generally behind (for the numerous government owned bank accounts), rendering cash account information unreliable;
- There is a large prevalence of suspense and advance accounts, most uncleared for several years – again putting a damper on the quality of data and information generated by the system;
- Donor project accounting is generally conducted outside of the IFMIS, with the concomitant banking independent of treasury;
- While the availability of information in IFMIS is on a real-time basis and should ordinarily promote budget monitoring, the reality is that there are significant delays of sometimes more than 4 months in producing quarterly in-year budget execution reports. This makes budget monitoring weak, and is of significance as procurement cannot proceed without available commitment (which can only be made after the reports are generated);
- The Government does not maintain a consolidated register of all fixed assets in its custody (although some line ministries do maintain a register of fixed assets funded by donors);
- Regarding financial assets, MoF maintains some record of government equity holdings in SOEs, however the information only shows the name of the company and the percentage share. Information on number of shares, cost and date of investments is not available;
- Although a legal and regulatory framework providing for fixed asset disposal procedures exists, the consolidated annual financial statements only provide partial information on proceeds of fixed assets disposed;
- On debt, The MoF does not prepare a medium-term debt sustainability strategy to guide central government borrowing decisions, although both domestic and foreign debt including guarantees are properly recorded in the CS-DRMS system, and reconciled at

least quarterly with information obtained from creditor statements. PPPs on the other hand are neither recorded nor reported. In addition, with regards to reconciling the CS-DRMS records to IFMIS, internal reconciliation challenges arising as a result of manual debt data entry onto IFMIS remain.

4.3.2 Current Risks

These pertain to the multiplicity of bulleted items above, ranging from incomplete records, delayed reconciliations, prevalence of suspense accounts, absence of a consolidated asset register, and inadequate debt information reconciliation to the IFMIS.

4.3.3 Mitigation

New and improved legislation and regulations to plug known gaps are being developed. This includes the revisions to the treasury regulations supporting the PFMA Act, the new Public Debt and Aid Management Bill, coupled with the rollout of an upgraded version of IFMIS with which bank to IFMIS bank reconciliations would now be possible to speed up the bank reconciliation process among other key activities. The upgraded IFMIS version has an asset management module that will aide in the maintenance of assets data, which will be augmented by annual physical count of assets where possible.

4.3.4 Overall rating

The overall risk rating for the accounting and reporting sub system at May 2019 remains **High**.

4.4 Internal Controls

Fiduciary Risk Rating	High

4.4.1 Review of Performance

Both the PFMA Act of 2012 and the Treasury Regulations, 2014 directly address internal controls and allocate specific duties and responsibilities to accounting officers in ministries. Appropriate segregation of duties is prescribed throughout the expenditure process and responsibilities are clearly laid down. There is also clear segregation of responsibilities when it comes to recording of financial data, reconciliations and internal audit. However, with regards to non-salary expenditure, compliance remains a major concern due to high vacancy levels, lack of skills and capacity.

The procurement process provides for a commitment to be raised and offset against available funds (budgets) on the IFMS system once an order is generated. Any procurement outside of the process is regarded as irregular and service providers will not ordinarily be paid. There are instances however where commitments are raised outside IFMIS, and the suppliers are still paid - for example, payments for infrastructure projects where the projects span over multiple financial years. Thus despite IFMIS functionality disallowing all commitments that are in excess of approved limits within the IFMIS, there is clear disregard and staff have found workarounds, as cases of ministries over-spending their budgets are common.

Payroll is acknowledged as a significant component of government expenditure. In terms of accuracy of the payroll data, there is no automatic integration or reconciliations between personnel records and the payroll system, leaving the accuracy of key payroll data unverified. With regards to changes made to personnel records, incidents of retrospective adjustments happen so frequently the matter has been flagged as an area of concern. There are thus no controls to validate payroll data, nor have any payroll audits been undertaken.

With respect to Internal Audit, The regulatory framework within which the function operates also includes:

- the PFMA Act;
- the Treasury Regulations 2014; and
- the International Standards for the Professional Practice of Internal Auditing, 2012 (this is partly adopted by Lesotho)

The Internal Audit Unit functions on a "shared-service" basis reporting to the Accountant General, both functionally and administratively. Since the Accountant General is in many ways the main "auditee", this reporting arrangement is clearly not optimal. In terms of practices, there is insufficient evidence that internal audit activities are prioritizing risks as prescribed in the PFMA Act and in accordance with Internal Auditing standards. While individual auditors are deployed in the various ministries, this is mainly an operational arrangement and does not necessary result in adequate audit coverage in terms of the high risk areas including payroll, fixed assets, non-tax revenue, procurement, cash management, ICT, among others. Further, no audit has been carried out on information technology system(s) used in government in the recent past to test the general and application control strengths. Last, there is no evidence that there is an adequate Quality Assurance System for internal audit in process and the Internal Audit Unit has not conducted any self-assessment or arranged for an external assessment as prescribed in IIA standards. The Office of the Auditor General (OAG) has concluded in its audit strategy that it places no reliance on Internal Audit due to lack of coverage, limited compliance to standards, incomplete working paper files and lack of comprehensive internal audit reports. On the recipients' side, even though periodic internal audit reports are prepared and issued to management, there is neither execution action nor responses to audit queries.

4.4.2 Current Risks

Main risks relate to low levels of compliance with set procedures. These have been attributed to any of the high vacancy rates, low skills levels, and low capacity. Unverified payroll data, coupled with the absence of any internal check and audit on the government ICT systems mean that errors could be carried undetected.

4.4.3 Mitigation Measures

Ongoing PFM reforms supported by the donors are helping to upgrade the GoL's payroll processes, and internal audit, which will be key to reforming practices and procedures relating to Internal Control. Specific reforms that may have an impact on payroll management processes include:

- The Department of Home Affairs is issuing each citizen with an identity number to be captured onto payroll and updating personnel files;
- The roll out of the Government Human Resource Information Management System (HRIMS);
- The execution of the Public Service Biometric and Payroll Census;
- The Public Financial Management Reform Project;
- The Public Service Modernization Project (PSMP).

4.4.4 Overall Rating

The above mitigations notwithstanding, the assessed overall rating of risk relating to internal controls was high, at May 2019.

4.5 External Scrutiny and Audit

Fiduciary Risk Rating	High

4.5.1 Review of Performance

The Audit Act 2016 together with the PFMA Act govern the sub system. The Auditor General (AG) is appointed by the King with advice from the Prime Minister in terms of the Constitution Article 142. The Constitution guarantees the AG's tenure in office until retirement age. Regarding budget, the OAG is funded through the national budget process, which frequently results in budget constraints for the office. Staff recruitment however is in the process of being transferred from the legal framework provided for public services, to an autonomous arrangement for the OAG. This may help address the historical problem of high staff turnover in the OAG by providing improved salary scales that can then attract staff with the necessary skills and experience. This, together with the new audit regulations, is unfortunately still work in progress whose impact is yet to be determined.

In terms of coverage, the OAG audits the entire consolidated fund and the majority of line ministries, utilizing some international standards. The main challenge has been on timeliness of completion of the process, with delays in excess of 10 months common. Timely audit and recommendations obviously help the system correct itself quicker and prevent recurrence of errors, while delayed audit mean that potentially harmful practices take longer to detect. However, when presented, affected ministries do provide responses to findings and participate in the parliamentary hearings when scheduled. The effectiveness of the process is diminished by the extended delays between performance of the work, late audits, and even more delayed parliamentary hearings (sometimes done two or three years late). It is therefore not uncommon to find the same audit recommendation repeated over several years because of the length of time it takes for the initial recommendation to be finally communicated to the auditees to enable them to make the requisite changes.

In terms of capacity, the OAG is generally constrained, more so for the specialist audit areas such as “Value for Money”, IT, and “Performance” audit. In practice therefore, for donor financed projects, the OAG outsources the audits to private audit firms, but provides quality assurance of sorts by reviewing the outcomes and including the OAG’s cover letter on each outsourced audit.

4.5.2 Current Risks

The main risks relate to low audit staff capacity, as well as delayed finalization of the process, which results in delayed correction of identified anomalies.

4.5.3 Mitigation

Implementation of the provisions of the Audit Act 2016 is still in process. This is expected to address especially the staffing issues, which is at the centre of the challenges noted (both capacity and delayed finalization of audits). In addition, some capacity development of the parliamentary public accounts committee is underway, which should also contribute to more robust debate of the audit reports, and earlier completion of the parliamentary review process.

4.5.4 Overall rating

The risk rating at May 2019 remains high, as the impact of most of the approved changes is yet to be felt.

5 Review of Performance: Procurement

Fiduciary Risk Rating	Substantial

5.1 Introduction: In addition to the diagnostics reports reviewed as indicated in the paragraph on introduction of this CFRA other documents were reviewed in order to update the status of the reform measures undertaken since the last CFRA 2013 within the country public procurement system. These comprised; MARS 2011, Public Procurement (Amendment) Regulations March 2018, Report on Procurement Compliance & Performance, April 2019 by Banks financed Institutional Support for Enhancement of Public Financial Management Project (ISEP) and proposed Procurement Bill.

5.2 General Environment

5.2.1 PPAD is a division of the Ministry of Finance and is therefore not a fully independent oversight body in discharging its functions within the Ministry of Finance. The lack of a Procurement Act means that the legal framework is incomplete even though the Regulations do provide policy direction. The Manual provides for a clear understanding of the required ethics for public officers and anti-corruption measures. The Government Code of Good Practice in Procurement sets out the core values and behavior for all members of the government's supply chain, government organizations and suppliers. It is a code of conduct for all members of the supply chain which encourages all participants to work together openly and co-operatively. The Regulations do not provide penalties and remedial actions when breaches occur during the conduct of public procurement. Generally, there is the lack of skilled procurement personnel which is an impediment to procurement efficiency. In light of the decentralization of procurement, the Regulations require that trained and qualified personnel in the Procurement Units do procurement processing. There is no information to indicate that the Units are appropriately staffed for this task. Any lack of capacity at central and district level may result in under performance and could expose the system to abuse.

5.2.2 **<u>Risks</u>**: According to the Compliance & Performance Report April 2019, the compliance on procurement systems was measured on five factors of procurement unit, procurement staff, procurement controls, records and reports; the results are shown in Figure 3.1. The compliance level for procurement staffing was highest at 50% while records and reporting was lowest at 13%. The overall procurement systems compliance level was low at 37%. Considerable efforts are required to improve all aspects of procurement systems, especially on procurement planning, records and reporting. Furthermore, there are no SBDs to analyze in order to determine if there are deviations that would lead to discretionary or unprofessional processes that would lead to poor procurement performance. An inherent risk, which is part of the broader issue of procurement-related corruption, may be due to failure on the part of public officials to comply with the Procurement Regulations. In addition, the deviations identified in the Public Procurement Regulations and lack of SBDs would often lead to misuse of the system. Discretionary and subjective award of contracts caused by use non-price criteria and use of "Cost Matching Scheme" procedure pose a big risk to value for money and corruption.

5.2.3 **<u>Internal Controls</u>**: The PPAD has a mandate to monitor public procurement proceedings regularly and to deal with any identified irregularities. The Procurement Units (PU) are supposed to be staffed with qualified staff to ensure sound procurement processing. The Regulations provide for establishment of evaluation committees and Bid Panel for approving proposed contract awards. The Regulations also allow the PPAD to establish an "Independent Appeals Panel" to review its decision and provide an opinion. Furthermore, procurement activities are subjected to regular internal and external auditing. The internal control mechanisms are essentially in place but there is no assessment report to indicate how efficiently the PPAD, the PUs' and auditors carry out their respective functions.

5.2.4 Fraud and Corruption, Complaints Review and Appeals Mechanisms:

According to the publication by the Directorate on Corruption and Economic Offences "Strategic Plan 2018/2019". From the report, it is to be noted that the directorate received about 1718 reports from July 2004 to July 2013. Out of this total, 50% were of the alleged cases attended are for misappropriation of fund or embezzlement, while 15% were fraud, 9% and 8% tender manipulation and bribery respectively and only 4% were corruption related cases. But in any case, relatively high quantum of procurement-related corruption cannot miss in Lesotho, given the loose procurement system and internal controls. This is corroborated by 2018 Transparency International perception index where Lesotho ranked 78 having been at 74 the previous year out of 178 countries. This index shows that Lesotho does not fall among the most corrupt countries.

5.2.5 The manual provides in detail rules and guidelines on how public officers should deal with corruption but there is no evidence that these elaborate guidelines are followed. The Regulations describe the Complaints Review and Appeals Mechanisms. Any act performed by a procuring entity in implementing procurement processes covered by the regulations is subject to administrative appeal through a complaint or a hierarchical recourse. The administrative appeal is optional and, if used, it should be submitted Head of the Procuring Unit and if not satisfied to the PPAD, followed by procurement tribunal. Failure to reach a satisfactory decision, the bidder may refer the complaint to the courts of law. A period of 15 days is provided between the time of informing the successful bidder and the time of signing the contract to allow an aggrieved bidder launch a complaint prior to the signing of the contract. The administrative appeal has a suspension effect in the procurement process, especially the acceptance of bidder qualification, negotiation, and contract award and contract signature. Court processes can often be too lengthy and may delay procurement processing to the detriment of public operations. The mechanism is not independent because it is all in the hands of public servants, the implementers of public procurement processes. In order to avoid delays in dealing with complaints and appeals, and make the mechanism independent, the normal and more acceptable arrangement is to establish an Independent Procurement Review Panel constituted of all members from private sector.

5.2.6 **Overall risk assessment**: The *inherent risk* of failure to achieve value for money and efficiency arise from procurement mismanagement, a loose procurement system, absence of SBDs, and low procurement capacity and professionalism in Procurement Units. For Lesotho to be able to implement a procurement system with minimal risks, it would require a new public procurement law, a strong oversight agency, and professionally staffed procurement units. *The procedural risk* is that the GOL may not be willing (due to political and cultural considerations) to enact a new public procurement law and there is no guarantee that the deviations identified in this report will be addressed in a timely manner**. The overall risk rating is substantial**

5.3 Legal, Regulatory and Policy Framework

5.3.1 As cited in the introduction above, the procurement legal and regulatory framework consists of the Public Procurement Regulations of 2007 and a Procurement Manual. There is no public procurement law but information from GOL indicates that one is already been developed but has not yet been adopted by Parliament, so it cannot be used for this assessment. There SBDs have been drafted but will further revisions once the bill becomes a law. Basically his means that the procurement system has major gaps as both the legal framework level (Act) and at the operational level (SBDs) are absent. The Procurement Manual includes standard operating procedures or standing instructions as well as guidance notes that guide the conduct of public procurement.

5.3.2 To date, the Regulations establish the functions of the Procurement Policy and Advice Division (PPAD) in the Ministry of Finance and the Procurement Units (PU) in the procuring entities. PPAD is responsible for the development of a public procurement system and enforcing compliance in order to achieve accountability, efficiency and transparency in the conduct of public procurement. Its main function is to provide assistance and support to the decentralized procurement units and to ensure compliance with the public procurement system in Lesotho. The Regulations provide for establishment of evaluation committees for evaluating bids/proposals, and Bid Panels for approving proposed contract awards. The Regulations allow the PPAD to establish an "Independent Appeals Panel" to review its decision and provide an opinion. The Panel comprises three experts, two selected by the complainant and the concerned Procurement Unit, and one selected by the first two. The operational procedure of the Appeals Panel is described in the Manual, which allows the proceedings to have little formality and open to the public. The Panel is only advisory, so it is not in reality "independent".

5.3.3 The Public Procurement Manual provides standard operating procedures on national approach to public procurement. The Manual provides for (i) general ethical matters, best practice in public procurement and the strategic value of procurement in developing the national private sector; (ii) standard terms and conditions of contract, procurement strategies, information on whole life costing, procedure for dispute resolution, the concept of managing risk, the need to uphold standards, and guidance in the various stages of the procurement cycle, including asset disposal, and (iii) guidance on the bid process, general issues such as intellectual property, donor funding and private public partnerships. The Manual contains many **annexes** on procurement templates and formats for documents required in the conduct of public procurement.

5.3.4 The Manual does describes provisions, guidelines and structure to be followed when preparing bidding documents for the procurement of goods, works and services. It also provides a list of the documents that comprise the bidding document and thresholds for use of various procurement methods as defined in Schedule 1 of the Regulations. The Regulations provide for three types of procurement methods: (i) *Competitive Methods* (Open International Bidding, Open Domestic Bidding, Restricted International Bidding and Restricted Domestic Bidding), (ii) *Shopping*, and (iii) Direct Methods

5.3.5 The Regulations set out Open Bidding as the default method of procurement with the other methods being referred to as exceptional. According to the Regulations, when the value of the procurement exceeds the threshold, only genuine emergencies and the lack of competition within the market will be regarded as acceptable justification for waiver by PPAD. The risk rating is considered substantial due the reasons highlighted below;

The main constraints are as follows:

The Kingdom of Lesotho has made good strides to enact a national procurement policy, prepared a draft procurement law, regulations, procurement manual, standard tender documents, and while several staff have undergone long term procurement professional qualifications. However, the procurement law is yet to be promulgated, thus curtailing the rest of the efforts in procurement reforms. The PFM Action Plan indicates that public procurement is in early stages of development and GOL acknowledged that there are significant issues relating to the regulatory framework, processes, structure, capacity and public disclosure of information.

(i) The Public Procurement Advisory Division currently performs functions that are to be taken over by the proposed Public Procurement Authority (PPA) in the draft bill; there is need to build the number and capacity of the staff to prepare them for their new roles and functions to ensure effective and timely transition.

(ii) In September 2018, the Ministry of Finance issued a circular to all procuring entities to implement the new job descriptions and specifications, which provide for procurement qualification and experience in the performance of procurement functions. This notification should be followed up with regular review of the procurement units at entities to ensure all entities comply.

(iii) Whereas several procurement officers had undergone the long-term procurement-training program, the review confirms the need to build practical skills among the procurement staff to effectively implement the procurement legislation and use the standard tender documents.

(vi) The PPAD seldom did procurement reviews and investigations due to the considerable efforts spent in processing retrospective approvals, lack of an annual work program, and a budget to conduct such reviews. Support will be required to ensure the PPAD is resourced both in personnel and finances to carry out its core mandate, even after the promulgation of the new procurement law.

(vii) A procurement information management system was lacking; whereas a format for preparing reports by entities was developed, there would be need to have a simplified excel version that could be uploaded in an online database to capture contract registers from procuring entities.

(viii) As reported in the procurement compliance and performance review reveals that the average time taken to resolve procurement disputes by suppliers to entities, through PPAD and procurement tribunal was significantly long at 301 days. Moreover, cases took an average of 248 days awaiting the decision of the Procurement Tribunal. There is need to legislate the maximum time the tribunal take to decide cases and build its capacity to do so.

(ix) A review of the main reasons of complaints to procuring entities showed that in most cases, the procurement unit failed to set the criteria correctly, leading to arbitrary award of contracts to undeserving cases. The root cause of this problem was traced to lack of standard tender documents, which will be resolved once the revised documents are implemented in procuring entities.

(x) Furthermore, the following are areas to be considered within the reform agenda of public procurement system;

- No conditions to allow for Parastatals to participate in the bidding process and award of contracts,
- "Bracketing" procedure is used which eliminates all bids above 15% of the estimated cost of the contract.
- No requirement for fraud and corruption clauses to be included in the bidding documents.
- There is no independent complaints and appeals review mechanism.
- "Cost Matching Scheme" procedure undermines the principle of value for money and fairness.
- No Provision for debarment of erring suppliers, contractors and consultants.
- "Two envelope" bid opening procedure is permitted routinely.
- Bid evaluation should not include criteria other than those with price considerations.
- Granting of Margin of Domestic Preference (10%) is allowed under NCB
- There is no provision for price adjustment.

5.4 Institutional Framework and Management Capacity

5.4.1 The PPAD is a division within the Ministry of Finance responsible for the development of the public procurement system. This is done by securing legality, accountability, efficiency, transparency and value for money in implementation of public procurement and by stimulating a competition with equality of treatment among bidders, while taking due regard of the GoL policy in respect of local preference schemes. Amongst the other functions are; Develop public procurement legislation and initiate proposals for the adoption of further acts and best practice; 2. Provide advice and support to the MoF on all aspects of procurement legislation, policy and implementation; 3. Monitor compliance with procurement policies and Procurement Regulations; 4. Provide the Principal Secretary of the Ministry with an annual report for the detailing performance of the public procurement system with recommendations; The Director of the PPAD reports to the Principal Secretary of the MoF. As noted in the compliance and performance report, the advice, instructions and directives from the PPAD have largely been ignored by MDAs since it was department under the MoF; the MDAs being legally established were reluctant to take instructions from a department of another procuring entity. In the proposed Procurement Bill, the Public Procurement Authority (PPA) will have a nationwide procurement oversight authority to regulate the practice of public procurement. The PPA however will not be involved in operational work of MDAs in the conduct of procurements, contract award decisions or resolving of disputes.

5.4.2 The Procurement Units are required under Regulation 52(4) to prepare and submit a procurement report for a given year and submit to the Principal Secretary. The information is then reported to the Minister of Finance in the first quarter of the following year. The PPAD will prepare a consolidated report that will be tabled in the Cabinet; after approval, the report is published in the mass media and the procurement webpage. In practice, MDAs are not motivated in complying with this regulation due to the absence of any consequence for noncompliance. The review revealed that the MDAs had little incentive to submit reports due to several factors. First, a manual procurement reporting format had been prepared but there was no electronic procurement reporting template that standardizes the required information from MDAs. Second, the responsibility for prepare the electronic reporting template was with the PPAD, who should now prepare this format to be issued to MDAs. Third, the entities perceived preparation of reports take time; hence, the procurement website should provide for easy upload online of reports using, for example, in Ms Excel forms.

5.4.3 Under the ISEP a number of activities have been undertaken to address some of the challenges in the institutional Framework and Management Capacity including; to improve spending efficiency and transparency of procurement; On improved spending efficiency and transparency in procurement, a revised output is a modern public procurement system operationalized, procedural manuals and guidelines, standard bidding documents developed and published; the draft procurement procedure manual and SBDs were developed in 2015 but will need revision once the procurement law is enacted. The senior managers at the PPAD have indicated that the Procurement Policy had been approved in April 2018 while the new Procurement Law and procurement Regulations are expected to be promulgated by year 2020. As a result of these efforts, an improved PEFA indicators PI-19 (PI-24) on use of competitive procurement methods increased from a rating of D in 2012 to C in 2016 and an improved execution rate of capital budget from 75.2% in 2012 to 80% in 2016. The PI-19 (PI-24) indicator on competition, value for money and controls in procurement measures (i) evidence on the use of open competition for award of contracts; (ii) extent of justification for use of less competitive procurement methods; (iii) existence and operation of a procurement complaints mechanism and (iv) existence of an independent administrative procurement complaints system are some of the notable improvements. But despite these efforts capacity remains a challenge within the MDAs and at the national level, PPAD. The risk rating under this pillar is still substantial due to the following constraints.

1) The regulatory, monitoring and oversight functions of PPAD conflicts with the power to issue 'no-objection' to the award of contracts. Indeed, the PPAD is involved in procurement transactions because in accordance with the retroactive approvals. It is to be noted that prior to March 2018, Regulation 8 provided for exceptional procurement procedure, which may be used when there is concern as to the degree of competition that could be secured or there is genuine emergency which is not brought about by the Procurement Unit or the clients.

2) To use single sourcing, the PPAD will review the request before approval by the Minister of Finance. After March 2018, the Regulation was repealed; the new Regulation 8 provided for Single Sourcing Method with conditions for use. In the revised procedure, the recommended contract is approved by Tender Panel. A copy of the contract and approval of Tender Panel shall be submitted to the PPAD soon after signing of the contract. Under the new Regulation 42A, the Minister of Finance may in exceptional circumstances, grant an authority to pay a supplier retrospectively provided the procurement was done in good faith.

3) There is no clear strategy for professionalization with coordination between PPAD and other stakeholders (public sector, private sector, professional institutes like universities, etc.) on procurement including weak contract management, which cannot meet the required demands.

4) Though the procurement planning is a requirement in the Regulations, most of the MDAs do feel it is not mandatory and it is not being used by the Procuring Units (PUs) during the budget formulation process.

5.4.1 Procurement Operations and Market Practices

5.5.1 There is lack of operationalization of the systems due to noncompliance with preparation of annual procurement plan, absence of publication of contract awards, delays in contract execution and in payment of invoices and poor record keeping. Under the law, it is mandatory to ensure availability of funding prior to the start of a procurement process. However, in practice the funding is often not available due to resource constraints.

5.5.2 One of the functions of the PPAD is to provide the Principal Secretary of the MoF with an annual report detailing the performance of the public procurement system with recommendations for improvement on identified weaknesses. Likewise, the proposed PPA will be required to prepare an annual report on the overall functioning of the public procurement system as well as a profile of procurement activities and submit to the Minister of Finance to table before Parliament. The Procurement Units are required under Regulation 52(4) to prepare and submit a procurement report for a given year and submit to the Principal Secretary. The information is then reported to the Minister of Finance in the first quarter of the following year. The PPAD will prepare a consolidated report that will be tabled in the Cabinet; after approval, the report is published in the mass media and the procurement webpage. In practice, MDAs are not motivated in complying with this regulation due to the absence of any consequence for noncompliance.

5.5.3 The Procurement Regulations do not have deterrent measures to punish those that fail to prepare and submit the statutory reports, leading to a lax compliance system. However, the proposed Procurement Bill proposes offences and penalties for failure to comply with the rules. Fifth, any new system is bound to face resistance; hence, the PPAD should communicate to MDAs Chief Accounting Officers and procurement practitioners on the need to internalize change in the current operations to align to the proposed procurement legislation.

5.5.4 The local private sector is not well organized and is facing constraints in accessing the public procurement market. For instance, the construction market is dominated by a few national contractors while in the area of consultancy services, few local firms are able to compete with the international players. In general, the access of the local industry to public procurement opportunities is hampered by: (i) difficulty to access to credit because of high interest rates; (ii) lack of understanding of tender documents and bidding procedures; and (iii) limited dialogue and partnership between the private and the public sector.

5.5.5 The current trend is for enterprises is to partner in order to reach the required the capability & capacity to compete for public contracts. However, the local industry faces stiff competition from international firms that have much more technical and financial advantage. In order to be more competitive, local firms are increasingly trying to make partnership with international firms through joint venture and subcontracting. In general, the business environment in Lesotho is moderately conducive to the private sector. The risk rating for this is moderate.

5.6 Accountability, Integrity and Transparency of the Public Procurement

5.6.1 The Integrity and Transparency of the public procurement system has been reviewed and in accordance with PEFA 2017 report, in the public sector, the function is primarily focused on assuring the adequacy and effectiveness of internal controls. However, there is insufficient evidence the at internal audit activities are prioritizing risks as prescribed in the PFMAA with IA standards, instead internal services are rendered on a shared basis with the IA Director reporting to the Accountant General, MOF. Though individual auditors are deployed in ministries, this is mainly an operational arrangement and does not result in adequate audit coverage in terms of the risk areas including procurement. There is neither legal nor regulatory requirements for conducting performance audits, which should provide recommendations, executive actions. Where actions are taken they are limited and at times with delays.

5.6.2 The external audit for PPAD is limited to administrative audit and not procurement audit undertaken by the PPAD on the Procuring Units, as part of the annual report for detailing performance of public procurement system with recommendations. Furthermore, the PPAD is responsible for setting up an Appeals Panel to deal with complaints and appeals from suppliers' ad companies, and PPAD shall provide the Secretariat service to the Appeals Panel. From this perspective, the Complaint Mechanism seems not independent of the Minister of Finance involvement, as the composition of the panel have to be accepted to the Minister thus compromising the independent nature of the panel. Details of what amounts to conflict of interest and how it should be dealt with by members of evaluation committees and bid panels are dealt with in the Regulations and in the Manual. However, the Regulations do not provide definitions of corrupt practices although these are mentioned as grounds for the exclusion of bidders. Detailed information on corruption, its impact and how to fight it can be found in Chapter 3 of the Manual. Furthermore, a Code of Conduct for procurement staff has been established; it is a requirement that each member of staff signs it.

5.6.3 In addition, as reported, Corruption that is critical in public procurement because of the huge quantities of commodities often being transacted and the volume of money involved in the procurement process. This creates substantial opportunities for public officials with the propensity to be corrupt because of the high profitability attached to these large procurements. According to the director of the Directorate on Corruption and Economic Offences (DCEO), public procurement in Lesotho is the most vulnerable area to corruption and public procurement cases form 99% of corruption cases handled by the DCEO in 2016. The risk rated as High under this pillar.

Table: 3 - Country Procurement Risk Assessment Rating Using the MAPS

PILLAR I – LEGAL, REGULATORY AND POLICY FRAMEWORK			
Indicator 1 – Public procurement legislative and regulatory framework achieves the agreed standards and complies with applicable obligations			**RATING**
Sub-indicators 1(a) –Scope of application and coverage of the legislative and regulatory framework			2
Sub-indicator 1(b) – Procurement Methods			3
Sub-indicators 1(c) – Advertising rules and time limits			3
Sub-indicators 1(d) – Rules on participation			1
Sub-indicators 1(e) – Procurement documentation and specifications.			2
Sub-indicators 1(f) –Evaluation and award criteria			3
Sub-indicators 1(g) – Submission, receipt and opening of tenders			2
Sub-indicators 1(h) Right to challenge and appeal			2
Sub-indicator 1(i) – Contract management			2
Sub-indicator 1(j) – Electronic Procurement (e-procurement)			1
Indicator 2 – Existence of Implementing Regulations and Documentation			
Sub-indicator 2 (a) –Implementing regulation that provide defined processes and procedures included in higher-level legislation			2
Sub-indicator 2 (b) - Model procurement documents for goods works, and services			2
Sub-indicator 2 (c) – Standard Contract Conditions			2
PILLAR II – INSTITUTIONAL FRAMEWORK AND MANAGEMENT CAPACITY			
Indicator 5 – The country has an institution in charge of the normative /regulatory function			
Sub-indicator 5(d) – Avoiding conflict of interest	The normative/regulatory institution has a system in place to avoid conflicts of interest		1
PILLAR III – PUBLIC PROCUREMENT OPERATIONS & MARKET PRACTICES			
Indicator 9 - Public procurement practices achieve stated objectives			

Sub-indicator 9(a) - Planning			2
Sub-indicator 9(c) – Contract management			2
PILLAR IV – ACCOUNTABILITY, INTEGRITY AND TRANSPARENCY OF THE PUBLIC PROCUREMENT			
Indicator 12 – The country has effective control and audit system			
Sub-indicator 12(a) – Legal framework, organization and procedures of the control system			2
Indicator 13 – Procurement appeals mechanisms are effective and efficient			
Sub-indicator 13 (a) – Process for challenge and appeals			2
Sub-indicator 13(b) – Independence and capacity of the appeals body			2
Sub-indicator 13(c) – Decisions of the appeals body			1
Indicator – 14 Country has ethics and anti-corruption measures in place			
Sub-indicator 14(a) – Legal definition of prohibited practices, conflict of interest, and associated responsibilities, accountabilities and penalties			2
Provision on prohibited practices in procurement documents			1
OVERAL PROCUREMENT RATING			**42**

Legend: Rating is based on a 0-3 scale, according to the defined criteria indicated in the June 2006 OECD/DAC paper. A score of 3 indicates full achievement of the stated generally-accepted international practice for each sub-indicator. A score of 2 is given when the system exhibits less than full achievement and needs more improvements in the area being assessed, but still reflects substantive compliance with the standard.

COUNTRY PROCUREMENT RISK RATINGS - Current Assessment - Substantial

Overall Programme Risk:
☐ Low (between 71-78)
☐ Moderate(between 48-70)
☐ Substantial (1-47 points)

6 Fiduciary Risk Management Framework: Key to Risk Ratings

Low (L) Risk implies a situation where the structure of PFM broadly reflects good international practice and there is routine compliance with the majority of controls within the system.
Moderate (M) Risk implies a situation where the structure of the PFM system broadly reflects good international practice, although there may be some gaps or inefficiencies. There is basic compliance with controls within the system and although regular exceptions occur, these are not financially significant.
Substantial (S) Risk implies a situation where the structure of the PFM system falls short of good international practice in a number of areas and/or there are numerous and/or material weaknesses in compliance with many controls within the system.
High (H) Risk implies a situation where the structure of PFM system shows a significant divergence from good international practice and/or there is widespread lack of compliance with many of the controls within the system. Inefficiencies and leakage from the system may be financially significant.

7 Key fiduciary risk not addressed by the existing PFM reforms

PFM Reforms in Lesotho have been under one comprehensive umbrella in the form of a formal PFM Reform Secretariat for some time. As far back as 2013, and coming out of the 2012 PEFA, GoL developed and launched a comprehensive five-year PFM Reform Strategic Action Plan (PFMRAP) covering the period from 2013 to 2018 to ensure a focused and properly guided reform process. A criticism of that effort was that it targeted achieving the equivalent of 'A' scores in the next PEFA, without acknowledging peculiar country circumstances. Following the 2016 PEFA, a more realistic and pragmatic set of targets for the next reform period is being developed. The 2013 -18 Secretariat's lifespan came to an end, and a successor to this needs to be put in place to retain the momentum. However using the PEFA as a baseline does ensure comprehensive coverage **(no risks are therefore not being addressed**) and eliminates duplication of efforts.

8 Short-term safeguards to mitigate key fiduciary risks

There is a need to continuously assess the implementation of the reforms and prepare evolving strategies to address shortcomings as well as to accelerate the implementation of the ongoing reforms. As noted by the GoL themselves, each country is different hence the need to be realistic and pragmatic. For the ongoing reforms, the government and development partners should maximize efforts on the following areas to accelerate the implementation of the PFM reforms in the country:

- Formalize a robust platform for inclusive dialogue at all levels;
- Ensure adequate funding for the key elements of the agreed PFM reforms;
- Expand support to increase the reach and capacity of Internal Audit, given its critical role in improving the overall control environment;

- Expand support to the Procurement Authority (PPAD) to build its capacity for oversight of the public procurement process;
- Formalize the establishment of the Treasury Single Account to enhance control and adherence to approved budgets; and
- Continue Payroll related reforms to improve control on the wage bill.

For the upcoming CSP period, Bank financed investment projects will continue to be ring fenced and accounted for and audited outside the IFMIS due to the current inflexibility of IFMIS regarding the production of necessary Bank specific reports, while policy based operations can be implemented within IFMIS as no unique and separate reporting is expected nor required. The use of Borrower Procurement Systems will continue to be determined on a case by case basis.

8 Monitoring fiduciary risk

The Bank, in collaboration with Development Partners will support and cooperate with the Government of Lesotho in addressing fiduciary risks identified. In the Bank funded operations a component or subcomponent will be included with specific activities aimed at mitigating the fiduciary risks. The Bank will continue monitoring and funding the ongoing Institutional Support for enhancement of public financial management system.

9 Country Fiduciary Strategy

9.1 Financial Management

As already noted, during the upcoming CSP period, investment projects will continue to be accounted for outside of the IFMIS, pending a review of compatibility and capacity of the upgraded IFMIS to generate Bank specific financial reports. Bank specific audits will continue to be coordinated by the OAG, including scope for the OAG to conduct the audits without the need to outsource, depending on the OAG's own capacity and resources.

9.2 Procurement

9.2.1 In order to reach a common agreement on the utilization of Country public procurement System, it will be important, within the context of continued dialogue with Government, to engage in discussions and reach agreement on the identified deviations and the modalities for their resolution through; (i) enactment of the Procurement Law (ii) Revision of the Regulations and Manual to better align them with the law; (iii) Revision of the SBDs and any relevant toolkits to conform with the related law & Regulations.

9.2.2 Apart from the utilization of the Country Procurement System and new SBDs, successful management of the inherent risks will lead to reduction, and final elimination, of prior review by the Bank in favor of post review of Lesotho's procurement processing under Open Competitive Bidding (OCB) – National. In pursuit of this objective and apart from the implementation of some of the recommendations, the following supplementary mitigating measures should be envisaged during the appraisal ,negotiation and implementation of projects and programs financed by the Bank: (i) systematic assessment of the procurement capacity at the sector, project and that of the Executing Agency (EA); (ii) consideration by the Bank of setting-up the threshold for OCB (National) at the same level as that for prior review; (iii) initial prior review of a specified number of OCB contracts to ensure that the track record of the EA concerned is acceptable based on its procurement risk; (iv) ensure the post review of OCB contracts by the Bank; (v) intensify the frequency of supervision on Bank-funded projects and programs; and (vi) jointly with other Development Partners prepare a MAPS II Assessment to inform on how public procurement is managed and to make recommendations for further improvement.

ANNEX A.13: ECONOMIC LABORATORIES

A total of 78 firms across the 4 sectors have been identified for funding following the 1st stage of workshops to review business plans and the government expects that these firms will require about USD 71 million over an initial 3 year-period beginning in 2020.

	Agriculture	Manufacturing	Tourism and Creative Arts	Technology and Innovation
Salient Features	It is Lesotho's 4th largest sector, Contributes 5.3% to GDP Sectoral growth has been driven largely by the Livestock and Crops sub-sectors, which accounted for 50.5% and 31.2% respectively to agricultural GDP. Employs 48% of total number of the employed, the majority are subsistence farmers A net food and agricultural products importer. Food insecurity affects approximately 70% of the population who reside in rural areas. A net food importer with a food and agricultural trade deficit of USD342 million as of 2016. The 2018 Global Hunger Report had ranked Lesotho 78 out of 119 Half of the people in Lesotho were severely food insecure from 2015-2017 (FAO). High cost of agriculture (expensive inputs rom South Africa)	Contributes about 12% to GDP 2016. Highly dependent on the textiles, garment, leather and footwear sub-sector, provides 90% of total employment within the sector. Concentrated in the low technology segment, requiring low-skilled labour which in turn earns low wages. Concerns over job quality and limited career advancement opportunities for Basotho employees. However, the industry remains important for poverty reduction. Income generated by the industry benefits 13% of Lesotho's total population. US and South Africa are Lesotho's two largest export markets, accounting for more than 95% of the country's exports Textile exports under AGOA increased by 120% from 2000 to 2005. Exports to the US decreased from 94% to 61% of total textile and apparel exports between 2005 and 2016 due to intense competition with other low-cost producers. The textile industry is also under pressure to diversify its export market as AGOA expires in 2025.	Tourism-related activities, represented by hotels and restaurants, wholesale and retail trade sub-sectors account for about 13% of GDP. Between 2015-2017, arrivals into Lesotho have been increasing at 2.5% annually, while tourism receipts grew at 4.8% during the same period. Key Travel & Tourism economic indicators, 2017: International Tourist Arrivals: 320,000 people International Tourist Inbound Receipts: USD34.4 mil Average Receipts Per Arrival: USD107.60 Travel & Tourism Industry GDP: SD114.9 mil (5.8% of total) Travel & Tourism Industry Employment 34,402 jobs (5.1% of total) Lesotho ranks 128 out of 136 countries in the World Economic Forum (WEF) Travel & Tourism Competitiveness Index (TTCI), well behind its Southern Africa Customs Union (SACU) peers. This is attributed to limited economic activities catered for tourists to stimulate spending and increase retention in Lesotho around tourist attraction sites. Almost 90% of tourists are residents of South Africa, which also contributed to the low amount of average receipt per arrival for the country. Lesotho ranks 4th in average receipt per arrival, at USD20 spent per tourist arrival.	Contributes about 5% to GDP. With low internet penetration in Lesotho (about 32.5% of the population), the non-growth in this sector is most likely caused by the fact that Basotho talent and content developers look towards South Africa for work or to sell their work there.

Challenges	Expensive inputs mainly imported from South Africa. Limited irrigated land dissuades locals and foreigners from investing in the sector Most farmers are subsistence farmers who do not have the capacity nor technical knowledge to venture into commercial farming. Lack of access to finance for expanding farmers' projects Lack of collection & storage infrastructure Poor handling techniques Lack of access to markets results in suppressed commercialization of Lesotho's agricultural products Lack of standards authority and legislation in Lesotho that certifies local agricultural produce that fulfill international requirements. Certified processing & manufacturing facilities are also limited, preventing expansion of agro- processing businesses	**Finance:** Of the four banks in Lesotho, only one (Post Bank) is Lesotho-owned Private sector financing in Lesotho (18% of GDP) is much lower than the average for Sub-Saharan Africa, e.g. South Africa (68%) & Namibia (55%) Banks prefer to invest excess liquidity in South Africa, draining savings and capital from Lesotho The lack of quality investments is seen as the main cause of low private sector lending and high interest rates (14.5% for micro and macro credit) **Human Capital:** Low productivity and limited technical, marketing, & financial skills to match industry demand Foreign investments also face restrictions like minimum capital requirements (USD250,000), licensing requirements & the inability of foreigners to lease land & hold land titles. Dependency on the US market via the AGOA limits sector expansion and diversification In the WB's Ease of Doing Business Index 2019, Lesotho ranked 106 out of 190 countries, behind fellow SACU members South Africa & Botswana at 82nd and 86th respectively. Problematic factors include access to finance, bureaucratic processes and inadequate infrastructure, inability of local suppliers to meet the quality standards, volume and deadline requirements and routine and urgent maintenance issues	Poor infrastructure: No direct, long-haul connections are available, and regional connections are costly. Road network and quality are poor (rank 98) & ICT infrastructure is limited (rank 113). Lack of skilled labour**:** The Travel and Tourism Competitiveness Index (TTCI) ranks Lesotho 128th among 136 countries reflecting lack of specialized tourism training such as degree of customer orientation (rank 133) and barriers to hiring foreign labor (rank 108). Protection of rich cultural heritage from destruction is limited, especially the physical assets, which threatens their continued existence for future generations. The main causes of environmental degradation include ploughing on steep slopes and/or marginal lands by crop farmers (54% of croplands are exposed to sheet erosion), overgrazing of rangelands (an estimated 50% overstocking of livestock), cutting of trees for fuel & other uses, and unregulated encroachment.	The costs of voice calls and SMS in Lesotho is the 7th most expensive amongst SACU & SADC countries owing to lack of competition amongst service providers, relatively high interconnection rates and government levies that get passed on to consumers. Lesotho is still the 8th most expensive among SACU and SADC in this regard – again, for the same reasons cited above. Lesotho's Technological Readiness ranked at 125 in 2017, a drop from 123 in 2015 was mainly due to lower FDI, technology transfer and availability of the latest technology. Despite the saturation, the percentage of mobile subscribers per 100 people is only at 70.9%, placing Lesotho 9th amongst SADC countries and the lowest in the SACU region. While mobile phone ownership stands at 78.7%, only 35% of them are smartphone users, and the low take-up is attributed to high service prices due to the duopoly of the two telecommunications companies, & government levies (3.5% annual royalty to Lesotho Communications Authority & 1% for Universal Service Fund. Slow progress in developing a Digital Government (e-Government); few online application presence from government agencies including the Ministry of Communications Science and Technology who does not have a website.

Policy Response	The sector seeks to unlock M3,969 million in private investments, create 12,158 employment opportunities, & contribute M5,091million to the national GDP by 2022/23. Maximize existing preferential trade agreements, such as the African Growth and Opportunity Act (AGOA) and Everything But Arms Initiative which Lesotho has benefitted from. Red Meat Diversification Expand Dairy Production Boosting Poultry Production Diversifying cereal & Vegetable crop Production Boosting Fresh Fruit Production Boosting the trout industry Aquaculture expansion Preferred destination for local and international companies seeking to establish agricultural (particularly Cannabis), industrial & manufacturing operations in Southern Africa.	The Manufacturing sector aims to unlock M10.76 billion in private sector investments, create 13,787 jobs & contribute M2.21 billion to GDP by 2022/2023. Textile & garment expansion Knowledge-Based industries Develop the Aviation industry Water Bottling Diversified Products Waste Management Special Economic Zones	The Tourism and Creative industries sector aims to contribute m225 mil in GDP by 2022/23 by unlocking m3,068 mil in private investments, and creating an additional 1,133 direct employment. Developing High-end Luxury accommodation Diversifying accommodation Offerings with Boutique and Small, medium-sized developments unlocking Lesotho's Tourism Potential by Tourism Product diversification to enhance Tourist experiences. International Sports, recreational events & Festivals Creative Cultural experience Platform Marketing & Promoting Lesotho internationally as a Key Tourist destination Unlocking Community-Based Tourism Projects	The Technology & Innovation sector aims to unlock M2.13 billion in private sector investments, create 2,943 direct jobs and contribute M1.29 billion to the GDP by 2022/2023. Digitalize government Services digital address System Business expansion Production Tech Film academy Lesotho National Broadcasting Service (LNBS) smart partnership Telco expansion Business Process Outsourcing Special Projects to act as a catalyst for the Technology & Innovation sector: These are the National University of Lesotho (NUL) Innovation Hub, the NUL-Lesotho National Development Corporation (LNDC) Industrial Park, & the LNBS Broadcasting Centre. These hubs are essential to drive innovation in Lesotho