This budget brief is one of four briefs that explore the extent to which the national budget of the Kingdom of Lesotho addresses the needs of children under the age of 18. This brief analyses the size and composition of budget allocations for the fiscal year 2018/19, and offers insights into the efficiency, equity and adequacy of past expenditure at the national level. The main objectives of the brief are to:

- synthesize complex budget information so that it can be easily understood by all stakeholders
- highlight key messages which can inform policy and budgeting decision-making processes.
Key messages

- The Government of Lesotho’s expenditure on health and education remains well below international targets. This is despite the two sectors receiving the highest allocations. As Lesotho will be one of the first countries in Africa to close its demographic dividend window, there is great urgency to better prioritize and increase investments in children and youth.

- The government’s fiscal policy is expansionary, primarily financed by high and unsustainable public borrowing; the fiscal deficit is set to widen to 5.6 per cent in the current financial year (2018/19). Austerity measures to curb unnecessary expenditure, such as the bloated wage bill, should be implemented. Education and health spending should be ring-fenced.

- The government remains overly dependent on South African Customs Union (SACU) revenue, which has been declining markedly in recent times. This means that to ensure fiscal sustainability and greater predictability of the budget, the government should adjust expenditure appropriately, implement government saving measures, modernize tax revenue collection, improve public financial management and reduce red tape.

- Government spending in Lesotho is dominated by the recurrent budget, which accounts for about 70 per cent of the national budget. Most of this is spent on salaries and operational costs. High levels of recurrent spending not only crowd out social benefits, particularly for children, but also constrain investment spending. This reduces the overall efficiency and effectiveness of government operations.

- Budget credibility is weak and underspending – especially of the development budget – is all too common. Attention must thus turn towards minimizing political instability, fiduciary risk and cumbersome procurement processes. Accountability to donors should be improved to ensure more dependable grant and loan commitments.

- Lesotho’s budget system is one of the least transparent in the world. The government could foster an environment of greater accountability to taxpayers and other stakeholders by making more and better budget information available in the public domain. It could also introduce meaningful opportunities for civil society to contribute to the budget cycle. These measures could result in more donor funding and lower borrowing costs.
1. Macroeconomic and socioeconomic performance

1.1 Macroeconomic performance

Lesotho’s annual growth rate is expected to be 4.2 per cent¹ in the current fiscal year (2018/19), up from 2.3 per cent in 2017/18. Gross domestic profit (GDP) is expected to reach 37.3 billion maLoti (M) in 2018/19.² GDP has increased nominally by 5.9 per cent year on year, but only by 0.13 per cent in real terms (Figure 1). Lesotho’s real per capita GDP is forecast to grow very slightly from US$1,023.9 in 2017/18 to US$1,060.4 in 2018/19. Lesotho therefore continues to just meet the World Bank criteria for classification as a lower-middle income country (LMIC).

Table 1: Value of selected macro-fiscal indicators in Lesotho: 2018/19

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Value</th>
<th>Indicator</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nominal GDP (in million M)</td>
<td>37,259.7</td>
<td>Inflation rate (annual %)</td>
<td>6.2</td>
</tr>
<tr>
<td>Real GDP (in million M)</td>
<td>25,709.2</td>
<td>Remittances (in million US$)</td>
<td>270.9</td>
</tr>
<tr>
<td>GDP growth rate (%)</td>
<td>4.2</td>
<td>Expenditure as % of GDP</td>
<td>53.2</td>
</tr>
<tr>
<td>Real GDP per capita (US$)</td>
<td>1,023.9</td>
<td>Fiscal deficit as % of GDP</td>
<td>-4.2</td>
</tr>
</tbody>
</table>

Source: Government of the Kingdom of Lesotho (GoL) National Budget speech 2018/19 and Ministry of Finance Budget Book 2018/19; World Bank Development Indicators (sourced August 2018).

Inflation in Lesotho remains moderately high. Inflation is forecast to decline marginally to 6.2 per cent in 2018/19, from 6.6 per cent in 2017/18. Looking forward, the International Monetary Fund (IMF) predicts that this level of inflation will remain at 5–6 per cent for the rest of the decade³ (Figure 2). Inflation affects vulnerable children’s access to basic social services. High inflation seriously affects the capacity of poor households to buy basic food items. Poor households thus either reduce the frequency of food intake or adopt negative coping mechanisms, such as engaging children in work, taking them out of school or reducing spending on health care.⁴

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² GoL, National Budget speech, 2018/19.
³ IMF, International Monetary Fund 2017 Article IV Consultation estimates and projections, 2018.
Lesotho’s forecast growth rate in 2018/19 is higher than that of its neighbours Swaziland (eSwatini), South Africa and Namibia. (Only Botswana’s growth is forecast to be higher, at 6.6 per cent). However, GDP per capita in Lesotho is still around 39 per cent lower than these neighbouring countries. GDP per capita can be used to compare both the standard of living and productivity. Lesotho’s fiscal deficit as a percentage of GDP remains consistently high: 5.7 per cent in 2017/18 and 5.2 per cent in 2018/19. Lower per capita GDP and high levels of budget deficit suggest that there are persistent structural issues in the economy and these need to be addressed urgently.5

Table 2: Forecast regional macroeconomic performance: 2018/19

<table>
<thead>
<tr>
<th></th>
<th>Lesotho</th>
<th>Swaziland</th>
<th>South Africa</th>
<th>Namibia</th>
<th>Botswana</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth (%)</td>
<td>4.2</td>
<td>1.3</td>
<td>-2.2</td>
<td>-1.0</td>
<td>6.5</td>
</tr>
<tr>
<td>Inflation rate (%)</td>
<td>6.2</td>
<td>6.90</td>
<td>5.3</td>
<td>3.6</td>
<td>3.4</td>
</tr>
<tr>
<td>GDP per capita (US$)</td>
<td>1,060</td>
<td>2,770</td>
<td>7,504</td>
<td>4,415</td>
<td>6,924</td>
</tr>
</tbody>
</table>

Source: GoL National Budget speeches 2018/19; Swaziland National Budget speeches 2018/19, 2018; IMF World Economic Outlook 2018; and <https://tradingeconomics.com/>.

1.2 Socioeconomic overview

Poverty and inequality in Lesotho continue to be structural problems. Lesotho is one of the poorest countries in sub-Saharan Africa, with over 1 million people living in poverty. This is half the population. Of this number, about 34 per cent are extremely poor, living below the national food poverty line of M138 per adult per month (about US$10) (Table 3). With a Gini coefficient of 0.53, income disparity in Lesotho is one of the highest in the world. Poverty is further exacerbated by: a very high prevalence of HIV (25 per cent among adults); high overall unemployment (33 per cent) and 32 per cent unemployment among youth; and food insecurity caused by the effects of climate change, including droughts and floods.6
Children classified as being aged between 0 and 17 years are the main victims of poverty and inequality. Of the nine dimensions of child well-being, about 65 per cent of all children in Lesotho are deprived simultaneously in three or more dimensions. Deprivation varies according to age groups and dimensions: for example, between 84 per cent and 88 per cent of all children are deprived of housing; 17 per cent are deprived of primary education and 62 per cent of secondary education; between 29 per cent and 32 per cent are deprived of water; 64 per cent of children aged between 0 and 23 months and between 51 per cent aged between 2 and 17 years are deprived of sanitation. The rate of overall deprivation is high among boys (66.5 per cent), and in rural areas (72 per cent). The extent of deprivation also varies between districts (Figure 3).

Rates of maternal and infant mortality in Lesotho are exceptionally high. The maternal mortality rate is 1,024 per 100,000 live births; infant mortality is 59 per 1,000 live births; and mortality among under-five year-olds is 88.1 per 1,000 live births. Ten per cent of children under the age of 5 are underweight and 33 per cent have stunted growth (Table 3).

Population growth in Lesotho is low. The total population of the country is 2.01 million, with a ratio of 49 per cent males to 51 per cent females. The population growth rate is only 0.9 per cent. The total fertility rate per woman is 3.3 children. This has declined over time and is now below the necessary population replacement threshold of 3.4. If not addressed, this could adversely affect the population growth rate.

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**Table 3: Socioeconomic indicators in Lesotho**

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total population</td>
<td>2,007,201</td>
</tr>
<tr>
<td>Population &lt;18 years</td>
<td>765,614</td>
</tr>
<tr>
<td>Children as a percentage of population</td>
<td>38.1</td>
</tr>
<tr>
<td>Demographic growth</td>
<td>0.68</td>
</tr>
<tr>
<td>Percentage of stunted children &lt;5 years</td>
<td>33</td>
</tr>
<tr>
<td>Life expectancy (years)</td>
<td>56</td>
</tr>
<tr>
<td>Infant mortality rate per 1,000 live births</td>
<td>59</td>
</tr>
<tr>
<td>Maternal mortality rate per 100,000 births</td>
<td>1,024</td>
</tr>
<tr>
<td>Adult literacy rate (% aged 15 and above, 2010)</td>
<td>89.6</td>
</tr>
<tr>
<td>Primary school net attendance rate (NAR) (%)</td>
<td>93.6</td>
</tr>
</tbody>
</table>

**Table 3 Notes:**

2. Lesotho Demographic Health Survey, 2014.
5. Q1 2014/15 Continuous Multipurpose Survey.

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**Sources:**

It is also an appropriate time for Lesotho to achieve improved economic growth by exploiting the advantages of the current demographic dividend. The working-age population in Lesotho is 62 per cent of the total. This suggests that the country is in a demographic transition, pointing to the current opportunity for the country to benefit from a demographic dividend. If the demographic dividend is not realized through adequate investment in youth, the country may not be able to come out of the prevailing negative cycle of poverty and inequality, and the inevitable increase in crime, violence, and more general social and political instability.

1.3 National policy

The National Vision 2020 outlines the government’s development strategy, which is implemented through the five-year Strategic Development Plan. The national vision states that Lesotho shall be a stable democracy, a united and prosperous nation at peace with itself and neighbours, with a healthy and well-developed human resource base, strong economy and technological base. To realize this vision, the National Strategic Development Plan for 2019–2023 prioritizes four key areas:

- enhancing inclusive and sustainable economic growth and private sector-led job creation
- strengthening human capital through improved health, nutrition, education, social protection and workplace skills
- building enabling infrastructure
- strengthening governance and accountability.

Takeaways

- Real growth is expected to increase from 2.3 percent in 2017/18 to 4.2 percent in the current fiscal year (2018/19).
- Inflation in 2018/19 is moderately high, at 6.2 percent, though down from 6.6 percent in 2017/18.
- Unemployment in 2018/19 is very high at 33 percent, with 32 percent of youth unemployed.
- Children, youth and women are disproportionately affected by poverty and poor access to basic social services.
- Lesotho has a low fertility rate, which could adversely affect population growth if not addressed.
- Lesotho can realize improved economic growth and social stability by taking advantage of the current demographic dividend.
2. Government spending

2.1 Spending trends

The nominal budget for 2018/19 is expected to reach M19,830 million, which represents an increase of only 0.1 per cent compared to 2017/18. In real terms, however, actual spending is expected to decline by close to 6 per cent. Looking back over the past five years, nominal spending has increased by 23.3 per cent, but real spending has decreased by only 0.7 per cent.

Figure 4: Total nominal and real government expenditure, as a percentage of GDP: 2014/15 to 2018/19

![Graph showing expenditure and GDP percentages from 2014/15 to 2018/19.]

Source: World Bank Boost Database, 2017; GoL National Budget 2018/19, 2018; and author’s own calculations.

Figure 5: Trends in recurrent and capital expenditure, as a percentage of the national budget: 2014/15 to 2018/19

![Graph showing trends in recurrent and capital expenditure from 2014/15 to 2018/19.]

Source: World Bank Boost Database, 2017; GoL National Budget 2018/19, 2018; and author’s own calculations.

Showing an average annual 53.6 per cent between 2014/15 and 2018/19, total expenditure as a share of GDP has been erratic over the period under review. Expenditure as a share of GDP for the approved budget for 2018/19 is set to remain at around 53.2 per cent (Figure 4), a 3 per cent decrease from the 56.3 per cent in 2017/18.

Recurrent expenditure in Lesotho continues to dominate overall spending. Significant increases in the wage bill over the last five years are particularly evident. While recurrent expenditure declined slightly, from 72.4 per cent of overall spending in 2017/18 to 70.2 per cent in 2018/19, the wage bill increased significantly over the whole period under review (Figure 5). The rise of total expenditure from 27.4 per cent in 2014/15 to 33.8 per cent in 2018/19 shows a year-on-year increase of 8 per cent. This is despite the ongoing commitments by the government to rein in the wage bill.

In contrast with the growing wage bill, development spending has remained relatively stagnant. This suggests that key development plans have been marginalized. Over the five years of the period under review, development spending constituted an average annual 29.6 per cent, never exceeding 29.8 per cent.

A breakdown of recurrent expenditure by administrative classification shows that it is dominated by compensation of employees and operating costs. In 2018/19, spending on compensation of employees accounts for 48.2 per cent of recurrent expenditure, followed by operating costs at 17.6 per cent, transfers at 15.2 per cent and travel costs at 4.7 per cent of the total recurrent expenditure budget (Figure 6).
2. GOVERNMENT SPENDING

2.2 Spending priorities

The Ministries of Education and Health receive the largest sectoral share of the national budget. In 2018/19, 13.2 per cent of the national budget is allocated to the Ministry of Education, followed by 12.7 per cent to the Ministry of Health (Figure 7). However, the budget allocations to these ministries still fall short of international benchmarks and targets: the Education for All Initiative recommends a 20 per cent allocation of the national budget to Education; and the Abuja Declaration recommends a 15 per cent allocation of the national budget to Health.

In 2018/19, just over one-third of the national budget is devoted to four key social sectors: health, education, water and social development. However, expenditure in the four sectors, as a share of total expenditure, has declined from 35.5 per cent in 2016/17 to 32.7 per cent in 2018/19 (Figure 8). As a percentage of GDP, the social sector share has increased only marginally, from 16.5 per cent in 2017/18 to 16.6 per cent in 2018/19. This trend is of great concern because of the pressing need to expand the reach of social services across all social sectors to reduce levels of deprivation, particularly among women and children.

Sectoral budget allocation as a percentage of the national budget to education, health, finance and social development has increased by an average of 0.6 per cent. In contrast, the allocation to the agriculture, police, defence, local government, development planning and water sectors has declined by an average of 0.3 per cent in 2018/19.

Takeaways

- The recurrent budget in 2018/19 has declined slightly as a share of total expenditure compared to 2017/18; however, it is still large and continues to be dominated by the wages bill and operational costs.

- Governments that operate such high levels of recurrent expenditure severely crowd out development spending. This has significantly negative implications for growth, poverty eradication and social development performance.

- The proportion of the allocation to the social sectors has decreased from 35.5 per cent in 2016/17 to 32.7 per cent in 2018/19. This undermines the provision of basic social services across the country.

- Health and education receive the largest shares of the national budget. However, at their current levels they remain below international targets, which are set in line with the Sustainable Development Goals (SDGs) and related targets.

- Total spending has declined in real terms. This is on the back of falling revenues and this has affected development spending in a number of priority areas, such as agriculture and water.
3. Budget credibility and budget execution

3.1 Budget credibility

**Budget credibility is defined as the variance between the approved and released budget.** Budget credibility in Lesotho is erratic; in particular, weak performance is noted for the capital budget. As a rule, recurrent expenditure performs much better than the capital budget (Figure 10); for example, 98.6 per cent of the approved budget for 2018/19 was released, compared to only 51.7 per cent of the capital budget. The development budget is severely undermined by poor procurement practices; the weak spending capacity of ministries, departments and agencies; and the lack of a credible system to capture donor reporting for on- and off-budget financial support.

![Figure 10: Budget credibility in Lesotho, as a percentage of the approved vs. released budget: 2014/15 to 2018/19](source: World Bank Boost Database, 2017; GoL National Budget 2018/19, 2018; and author’s own calculations.)

3.2 Budget execution

**Budget execution in Lesotho is weak.** The overall total budget execution rates between 2014/15 and 2017/18 have also been very erratic. They range from as low as 41 per cent in 2016/17 to 80 per cent in 2018/19. Budget execution rates for the recurrent budget also declined, from 95.8 per cent in 2014/15 to 44.5 per cent in 2016/17, and increasing to 92.2 per cent in 2017/18. The development budget, on the other hand, has been executed from a low of 32.9 per cent in 2016/17 to a high of 90.7 per cent in 2017/18 (Figure 11).

![Figure 11: Budget execution rates in Lesotho: 2014/15 to 2017/18](source: World Bank Boost Database, 2017; GoL National Budget 2018/19, 2018; and author’s own calculations.)

The fiscal crisis in 2016/17, brought about by political turmoil, resulted in large losses in the recuperated revenue flows that had been expected.
Takeaways

- Lesotho’s budget is generally characterized by weak budget credibility and budget execution.

- The recurrent budget lacks credibility largely because of unplanned in-year increases in civil servant salaries and other forms of patronage.

- The development budget is dominated by donor commitments and is severely under-funded by year-end. This is due to a complex mix of factors such as political uncertainty, high levels of fiduciary risk, poor donor reporting systems and delays because of cumbersome procurement processes on the part of both the government and donors. These factors significantly contribute to the poor execution rates for the capital budget.
4. Budget transparency

Lesotho’s budget system is one of the least transparent in the world. Lesotho scored zero on the 2017 Open Budget Survey.¹¹ The survey shows that Lesotho citizens do not have access to national budget information and opportunities to engage in the budget process. Oversight of budget implementation by the Lesotho Legislature and the Supreme Audit is weak. By making more and better budget information available in the public domain and introducing meaningful opportunities for civil society to contribute to the budget cycle, the government could foster an environment of greater accountability to taxpayers and other stakeholders. This would potentially result in more donor funding and lower borrowing costs.

5. Financing the national budget

5.1 Domestic revenue

Revenue collection as a percentage of GDP has decreased steadily since 2014/15. It declined from 58.5 per cent in 2014/15 to 42 per cent in 2016/17. It is projected to improve slightly to 43.2 per cent in 2017/18 and remain at this level in 2018/19 before it is expected to decline further to 40.5 per cent in 2019/2020. Revenue collection is projected to increase to 46.3 per cent in 2020/2021.

Weak revenue performance is primarily a result of declining South African Customs Union (SACU) revenue. For 2018/19, revenues are projected at M16,099.6 million or 43.2 per cent of the national output. SACU revenue is the third-largest component of overall revenues, after tax revenues and non-tax revenues.¹² However, revenue has fallen steadily from 28.2 per cent in 2014/15 to as low as 13.5 in 2016/17 and 14.9 per cent in 2018/19. The volatility is largely a result of the weaker South African economy. In monetary terms, SACU revenues for 2018/19 have declined by M616.1 million from their 2017/18 levels. This means that government would need nearly M1 billion in real terms to cover the same programmes covered in 2017/18. Tax revenue, on the other hand, is projected to improve slightly, from 19.5 per cent in 2017/18 to 22.0 per cent in 2018/19. According to the

¹¹ See <www.internationalbudget.org/open-budget-survey/>.
¹² Tax revenues are composed of income tax, property tax and taxes on goods and services.
5. Financing the National Budget

IMF, if the situation is not addressed promptly, there will be pressure on international reserves, and arrear payments due by government will increase.\(^{13}\)

The IMF suggested the following measures:

- Adjusting expenditure appropriately in line with key priorities
- Addressing the public sector wage bill, which is one of the largest in the world
- Implementing saving measures on government travel, foreign embassies and procurement
- Protecting the most vulnerable sectors of the population
- Modernizing tax policies and improving systems of revenue collection
- Improving public financial management to ensure the provision of reliable fiscal data and the efficient and effective use of public resources
- Reviewing licensing procedures and regulations to reduce red tape
- Modernizing the legal credit framework
- Reviewing the role of the government in the economy.

5.2 Financing the budget

While the recurrent budget is fully financed by the government, the development budget is financed primarily by the government with support from donors in the form of loans and grants. Government financing for the development budget has grown from 72.7 per cent in 2014/15 to 80 per cent in 2018/19, with an average of 69.3 per cent over the whole period under review. Loans have more than doubled in size from 5.4 per cent in 2014/15 to 22.2 per cent in 2016/17 and 10.3 per cent in 2018/19. Grants are set to decline significantly in 2018/19 to only 9.7 per cent of the development budget, from 23.3 per cent in 2016/17 (Figure 13). This may be the result of Lesotho’s LMIC status.

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\(^{13}\) IMF staff concludes visit to Lesotho, 15 September 2018.
5.3 National debt

Government debt is expected to increase sharply from 2018/19 onwards, to finance the growing budget deficit. In 2018/19, external debt increased to 33.3 per cent from 31.4 per cent in 2017/18. On the other hand, domestic debt is also projected to increase, from 4 per cent in 2017/18 to 5.5 per cent in 2018/19, and it is expected to continue to increase significantly. Likewise, gross debt is projected to increase to 38.8 per cent of GDP in 2018/19, from 35.4 per cent in 2017/18. The IMF considers this a moderate risk of distress: the debt ratio could be unsustainable over time if not monitored carefully. For instance, the stock of debt is set to increase to 45.3 per cent by 2020/21. For the current fiscal year (2018/19), interest rate payments are 1 per cent on domestic debt and 2.7 per cent on foreign debt.\textsuperscript{14}

![Figure 14: Share of debt in Lesotho, as a percentage of GDP: 2014/15 to 2018/19](image)

Source: IMF, Staff Report for the 2017 Article IV Consultation, 2018.

Takeaways

- Lesotho remains dependent on volatile and shrinking SACU revenues. If the situation is not addressed promptly, international reserves will be under pressure and result in the build-up of government arrear payments.
- Debt is high, but according to IMF assessments, there remains only a moderate risk of macroeconomic performance being destabilized. Nonetheless, the debt ratio needs to be monitored carefully to ensure its sustainability in the long term.
- Loans are replacing grants as a source of external finance, in line with the country’s LMIC status.

\textsuperscript{14} GoL, National Budget 2018/19, 2018.
## Annex 1: Budget calendar

<table>
<thead>
<tr>
<th>Month</th>
<th>Key activities and outputs</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>April</strong></td>
<td>• Public Sector Investment Committee quarterly meetings</td>
</tr>
<tr>
<td><strong>May</strong></td>
<td>• Budget Book published</td>
</tr>
</tbody>
</table>
| **June** | • Discussion and approval of physical and financial reports by Cabinet Budget Committee  
• Baseline Medium-Term Fiscal Framework prepared by Ministry of Finance and the Ministry of Development Planning |

### Strategic and analytical phase

| July | • Cabinet retreat (presentation of the key fiscal and budget policy, strategy and priorities) |
| August | • Budget Framework Paper circular and ceilings are issued by the Ministry of Finance  
• Line ministry Budget Framework Papers prepared |
| September | • Review of Budget Framework Paper requests  
• Ministry Budget Framework Paper hearings |
| October | • Updated Baseline Medium-Term Fiscal Framework prepared  
• Draft ceilings finalized  
• Budget ceilings approved by Cabinet |

### Budget finalization phase

| November | • Budget call circular and ceilings issued by Ministry of Finance to line ministries  
• Budget estimates prepared by all ministries |
| December | • Review of estimates request by Ministry of Finance and Ministry of Development Planning |
| January | • Ministry budget hearings |
| **February** | • Draft estimates compiled  
• Draft budget approved by Cabinet Budget Committee  
• Budget speech prepared  
• Budget Day  
• District consultations on the budget |
| **March** | • Appropriation bill approved by Parliament |

Source: UNICEF