

**CENTRAL BANK OF LESOTHO**

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## **I. Key Economic Events in Lesotho during the Third Quarter**

### **Two Commercial Banks Merge Operations**

In recent years, mergers and acquisitions have affected industries and organisations in many countries. The financial sector in Lesotho has not been immune in this regard. On 15 July 2006, Standard Bank Limited and Lesotho Bank (1999) Limited merged their operations giving birth to a new bank called Standard Lesotho Bank. The purpose of the merger was to ensure a more efficient business model that would better meet customer needs. In towns where the two banks operated branches separately, one of them was closed. Such towns as Botha-Bothe, Hlotse, Mafeteng and Mohale's Hoek were affected by this merger.

Advantages of this process by and large, include improvement of the financial situation of the resultant company and gaining of a better market position. Furthermore, bank mergers would enjoy economies of scale and scope. The synergies could enable the merger to reduce costs, extend the range of products and services, diversify risk, transfer skill and know-how, and expand customer services. Consequently, productivity could be enhanced and in turn, drive economic growth. Nevertheless, there are some disadvantages that accompany merging processes. The branch network could be narrowed and this could reduce the outreach of financial services in the country. This will also lower the branch-customer ratio and lengthen queuing time at service points. The merging of the two banks has increased the concentration level in the market. As some branches are closed some employees are laid-off and this worsens unemployment in the country.

### **The Launch of Lesotho Wire System**

The Central Bank of Lesotho (CBL) has embarked upon modernisation of the country's payment and settlement system as a way of strengthening the financial infrastructure and maintaining financial stability. On 25 August 2006, CBL launched the Real Time Gross Settlement (RTGS) system known as "Lesotho Wire system". RTGS is a centralised system in which inter-bank payments instructions are settled in real time throughout the business day. Transfers are settled individually without the netting of debits against credits as is the case with the traditional net settlement system. Banks initiate payment by verifying certain aspects of the payment instruction and determine the processing path to be followed through the inter-bank funds transfer processes.

Participants in the system are the financial institutions and the CBL. The CBL acts as both the system provider and a participant on behalf of the Government of Lesotho. The benefits of the system include, among others, safe, speedy, affordable, accessible and efficient funds transfer mechanisms. In addition, the system has a potential to encourage the development of the inter-bank money market in the economy. Furthermore, it would minimise various risks associated with payment and clearing systems, and for this reason, improves credit rating of the country. And finally, fraudulent payments would be minimised through proper design of payment instruments' security features, as well as system procedures.

### **Discovery of Lesotho Promise**

The Letseng diamond mine, discovered a diamond which weighed 603 carat on August 22, 2006. The stone was notable for its colour coupled with its size. Its colour has been graded 'D', the most exceptional colour a diamond can be. The uncut diamond, which has been named 'the Lesotho Promise', is the largest quality diamond found and ranked as the 15<sup>th</sup> largest diamond ever found in the world. The Letseng diamond mine made history for the second time. The previous largest diamond found in Lesotho was in 1967 with a weight of 601 carat.

The stone was sold for US\$12.36 million. A large portion of Lesotho diamonds is destined to Belgium in the Euro-zone. During the quarter under review, diamond export earnings increased by 86.9 per cent and thus improved Lesotho's external position.

### **Launch of the Private Capital Flows (PCF) Survey 2006**

The CBL in collaboration with the Bureau of Statistics and Lesotho National Development Corporation, launched a PCF survey on September 18 2006. This sensitization campaign was followed with a sensitization for Chief Executives and Managing Directors of privately-owned companies operating in Lesotho. The survey is expected to collect information on financial flows between Lesotho and the rest of the world. This is the first initiative covering the financial year 2005, and it is expected to be conducted on an annual basis.

The survey aims to improve data coverage of the Balance of Payments Statement and the country's international investment position. Further, the results of the survey are intended to enhance macroeconomic analysis.

## **II. International Economic Developments and their Implications for the Lesotho Economy**

### ***United States (US)***

Economic growth in the US measured by changes in real Gross Domestic Product (GDP) continued to weaken during the quarter. Growth in real GDP slowed down to 1.6 per cent on a quarterly basis compared with 2.6 per cent in the previous quarter. The slowdown was mainly driven by the decline in the housing market. Sales of existing homes fell by 1.9 per cent in September. However, consumer spending remained strong.

Inflation in the US measured by changes in Consumer Price Index (CPI) rose by 2.1 per cent in September compared to 4.3 per cent recorded at the end of June 2006. The observed easing of inflation in the US is mainly driven by the decline in the energy prices. The moderation in inflation led the Federal Reserve Open Market Committee to keep the benchmark rate unchanged at 5.25 per cent in September 2006.

On the labour market, unemployment in the US was recorded at 4.6 per cent in September compared with 4.7 per cent at the end of June 2006. The developments in the labour market indicate that companies are continuing to employ workers despite the outlook of economic slowdown.

Economic developments in the US have a number of implications for the Lesotho economy. The eminent economic slowdown in the US, if sustained, may negatively offset the expected recovery of the manufacturing sub-sector following the slowdown in 2005. However, the increasing employment and strong consumer spending may offset the impact. The current high interest rates may raise Lesotho's debt service because the external debt portfolio is denominated in foreign currencies.

### ***Euro-zone<sup>1</sup>***

Economic indicators indicate that economic activity in the Euro-zone remained strong during the quarter. The Purchasing Managers Index (PMI) for manufacturing showed that confidence in the Euro-zone was recorded at 56.6 in September. At this level, the index is above the critical level of 50 which indicates expansion. Retail sales, as a proxy for

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<sup>1</sup> Euro-zone: Austria, Belgium, Germany, Greece, Finland, France, Ireland, Italy, Luxembourg, Netherlands, Portugal and Spain.

economic growth increased by 1.4 per cent in September compared with a rise of 1.5 per cent observed in June 2006. Furthermore, on an annual basis, industrial production rose by 5.4 per cent in August from 3.2 per cent in July, 2006.

Inflation in the Euro-zone measured by changes in CPI rose 1.7 per cent at the end of the third quarter compared with 2.5 per cent at the end of the previous quarter. At this level, inflation is below the European Central Bank (ECB) targeted limit of 2 per cent. The deceleration was mainly driven by the fall in the energy prices. However, core inflation which excludes energy, food and tobacco prices is still on the increase.

During the third quarter of 2006, the ECB raised its benchmark rate by 25 basis points to 3.00 per cent. The increase was driven by the continuing risks to price stability despite the decline in the price of oil.

Unemployment continued to be high in the Euro-zone during the quarter. Unemployment rate rose from 7.8 per cent at the end of June to 7.9 per cent at the end of August 2006.

The Euro-zone is a potential market for a number of products from Lesotho. Currently, Lesotho exports diamonds to the EU. Thus a stable economic outlook has positive implications for Lesotho.

### ***South Africa (SA)***

There are indications that economic activity in South Africa may be negatively affected by higher interest rates, energy prices and food prices. Consumer confidence index during the quarter, declined to 17 compared with 20 in the previous quarter. The decline was mainly driven by interest rate hikes. However, at this level the consumer confidence is still regarded high. Manufacturing production seasonally adjusted increased by 4.7 per cent compared with 6.3 per cent recorded during the second quarter of 2006. Mining production also increased by 0.8 per cent from the previous quarter.

The Consumer Price Index excluding interest payments on mortgage bonds (CPI-X) in SA rose 5.1 per cent in September compared with 4.8 per cent in June. Inflation in September was driven by food and transport categories. At this level, CPI-X is still within the South African Reserve Bank (SARB) target range of 3 per cent to 6 per cent.

The deteriorating inflation outlook led the South African Reserve Bank Monetary Policy Committee (MPC) to increase its key interest rate twice



during the quarter. The repo rate rose by a total of 100 basis points to 8.00 per cent at the end of September.

On this background, prices in Lesotho may be expected to continue to increase in the coming months. Furthermore, the interest rate hikes may lead Lesotho rates to follow suit due to the monetary integration between the two economies.

### ***Commodity prices***

#### **Gold**

The average price of gold fell by 1.1 per cent, from \$628.2 per ounce in the previous quarter to \$621.3 per ounce during the quarter under review. It closed the quarter at a minimum and maximum of \$573.7 and \$664.2 per ounce, respectively. The weakness of the dollar price of gold was due to the strengthening of the US dollar which rendered gold more expensive to holders of other currencies. However, the fall in the price of gold was limited by increased demand from India, the world's largest gold consumer. In rand terms, the price of gold rose by 1.7 per cent, from R4 391.70 per ounce in the previous quarter to R4 464.70 in the quarter under review, due to the depreciation of the rand.

The dollar price of gold is the leading indicator on the prospects of the mining industry in South Africa. The depreciation of the rand continued to offset the negative impact of the fall in the dollar price of gold.

#### **Oil**

The price of crude oil continued to increase during the quarter under review. On average, the price of oil increased by 1.9 per cent, from \$64.79 per barrel in the previous quarter to \$66.07 per barrel during the quarter under review. The international oil price increased as a result of high oil consumption in China and India. Furthermore, continuous uncertainty in the Middle East coupled with violence in Nigeria continued to put upward pressure on the international oil prices. In rand terms, the average oil price increased by 4.8 per cent during the quarter. It increased from R452.97 per barrel in the previous quarter to R474.78 per barrel in the third quarter of 2006.

Although the price of crude oil seems to be increasing in rand term, there are indications that the price in dollar terms is on a declining trend. The increase in the international oil prices could affect the Lesotho economy

negatively. It could result in an upward revision of fuel prices. This could exert upward pressure on the inflation. High oil prices could also increase the cost of production which may adversely affect profit and therefore employment levels.

### **III. Overview of Macroeconomic Developments in Lesotho**

#### *Economic Performance*

In the third quarter of 2006, most indicators reflected good performance of the economy. The number of building permits approved, (measure of building and construction activity) increased by 54.0 per cent and 14.3 per cent on quarterly and annual basis, respectively. The number of imported motor vehicles, a measure of capital formation, also registered a seasonally adjusted 32.5 per cent increase on an annual basis following an 18.5 per cent growth in the previous quarter. Electricity and water consumption by the industrial sector, a measure of activity in the manufacturing sub-sector, reflected an improvement on both quarterly and year-on-year basis. However, data on demand and supply of cereals points to lower production domestically and hence poor performance of the agricultural sub-sector<sup>2</sup>.

#### *Inflation*

Inflation accelerated from 6.6 per cent in June to 6.8 per cent in the two months ending August 2006. The data for September is unavailable but it is expected that inflation will slow down, mainly driven by the drop in the crude oil price. It is however cautioned that the price of cereals is expected to continue exerting an upward pressure on the inflation rate.

#### *Employment*

Employment in the Lesotho National Development Corporation (LNDC) assisted companies increased by an estimated 2.3 per cent on a quarterly basis. This translates into a 16.6 per cent increase on an annual basis. The increase is a result of recovery of the export manufacturing sector, where the majority of firms managed to secure sales orders for a longer horizon.

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<sup>2</sup> This data is for the agricultural year 2006/2007 and not specifically for the quarter under review.

Employment in the Government sector has increased marginally by 0.6 per cent for the period ending September 2006. The major influence came from the increase in the employment of teachers and general civil servants. The increase in the employment of the number of teachers was expected as the Government reached the final year of the rollout of free primary education. It is also noted that if government decides to go on with basic education to cover for the initial ten years of education, the number of teachers hired would be expected to continue increasing. The migrant mineworkers' employment also increased by 2.1 per cent as marginal mines started to operate close to their optimal output. This was attributable to the improvement in the price of gold in the international markets.

### *Balance of Payments*

Lesotho's balance of payments position improved during the quarter under review. The overall balance increased from a seasonally adjusted surplus of M175.2 million in the second quarter to a surplus of M639.9 million in the third quarter. Transaction balance, which represents the overall balance excluding the effect of currency fluctuations, was also higher, in seasonally adjusted terms, than the previous quarter. It recorded a surplus of M371.0 million compared with M209.1 million in the previous quarter. The improvement in the BOP position during the review quarter was a reflection of an improvement in the current account. The current account recorded a surplus of 1.3 per cent of GDP in the review quarter, in contrast with a deficit of 1.6 per cent observed in the previous quarter. Gross reserves measured in months of import cover, increased from 6.2 months observed in the previous quarter to 7.1 months in the period under review. During the third quarter, the trade deficit declined as a result of growth in exports. Furthermore, the capital and financial account recorded an outflow of M32.4 million due to a rise in commercial banks' foreign assets.

### *Monetary Sector*

At the end of the review quarter, the broad measure of money supply (M2) registered a quarterly increase of 15.4 per cent following a rise of 5.3 per cent observed at the end of the previous quarter. The rise was mainly due to an increase in both the overall banking system's net foreign assets adjusted for valuation changes and domestic credit.

The prime lending rate rose from 12.0 per cent to 12.3 per cent in line with the increase in similar regional rates. The Lesotho 91-day treasury bill rate fell from last quarter's 6.90 per cent to 6.86 per cent in

September. During the same period, the counterpart SA rate rose from 6.83 per cent to 8.0 per cent in June and September, respectively. As a result, the margin between the two rates widened from 7 to 114 basis points.

#### *Fiscal position*

Government budgetary operations were estimated to have realised a surplus equivalent to 6.2 per cent of GDP. This was facilitated by Government efforts to contain recurrent expenditure at a minimum level during the review period, again improved collections of revenue.

Total public debt increased by 14.5 per cent during the period under review. This was a result of the increase in external debt disbursements along with depreciation of the local currency against the major currencies with which debt is contracted. As a ratio of GDP, the total debt stock was estimated to have increased to 50.8 per cent.

### **IV. Economic Indicators**

#### ***Demand and Supply of Cereals***

Despite good rainfall, domestic availability of cereals (production plus opening stock) stood at 172.9 thousand tonnes while cereal requirement for the marketing year is estimated at 414.8 thousand tonnes. Domestic maize supply is expected to fall short of demand by 167.7 thousand tonnes. This year's maize production is 8.3 thousand tonnes below the 2005/2006 production. Domestic production of sorghum is also estimated to decline from 22.8 thousand tonnes in 2005/2006 to 17.8 thousand tonnes in the year under review. Wheat production increased from 37.6 thousand tonnes in the previous year to 46.6 thousand tonnes in 2006/2007. Nonetheless the domestic consumption requirement remained quite high. The increase in wheat production is expected to be driven by good rainfall at the beginning of the year. Therefore, the overall domestic shortfall is estimated at 241.9 thousand tonnes which has to be covered by imports.

Furthermore, according to a report by Lesotho National Early Warning Unit (LNEWU) the commercial sector has planned to import 141.7 thousand tonnes of maize and 80.2 thousand tonnes of wheat while the donors have planned to import 21.7 thousand tonnes of maize making the total planned imports to stand at 243.6 thousand tonnes. The planned imports leave the country with a surplus of 1.7 thousand

tonnes. Generally, cereal production for the marketing year 2006/2007 is expected to be below the domestic requirement.

**Table 1: Demand and Supply of Cereals**

('000 tonnes)

	2004/2005			2005/2006			2006/2007		
	Maize	Sorghum	Wheat	Maize	Sorghum	Wheat	Maize	Sorghum	Wheat
Domestic Availability	105.9	14.8	31.9	117.0	22.8	37.6	108.7	17.8	46.6
Requirements	252.2	40.3	106.1	242.1	23.2	89.2	276.4	32.6	105.8
Balance	-172.7	-17.5	-68.6	-125.2	-0.4	-51.6	-167.7	-14.8	-59.4
Imports	142.9	8.1	84.8	141.1	0.0	78.7	163.4	0.0	80.2
Of which aid	21.9	8.1	5.8	0.0	0.0	0.0	21.7	0.0	0.0
Surplus/ Deficit (-)	-24.7	-17.5	10.5	-16.0	-27.1	21.7	-4.3	-14.8	20.8

Source: Lesotho National Early Warning Unit (LNEWU)

### ***Household and Business Sector Housing Statistics***

The number of building permits is used as a general indicator of activity in the construction sub-sector, due to the unavailability of quarterly building and construction statistics. The number of building permits, adjusted for seasonality changes, increased by 54.0 per cent in the third quarter of 2006, in contrast to a 27.0 per cent drop realised in the previous quarter. The quarterly increase was mostly driven by building permits for residential purposes *inter alia* the proposal by Lesotho Housing and Land Development Corporation (LHLDC) to build about 20 houses at Katilehong. Thus, the rise in the number of permits approved which signals amongst others demand for building materials, was reflective of the good performance in the construction sub-sector. On an

annual basis, the number of building permits increased by 14.3 per cent compared with 33.3 per cent. However, the number of building permits for commercial purposes continued on the downward trend.

**Table 2: Building Permits by Type of Building**  
(Value in Million Maloti)

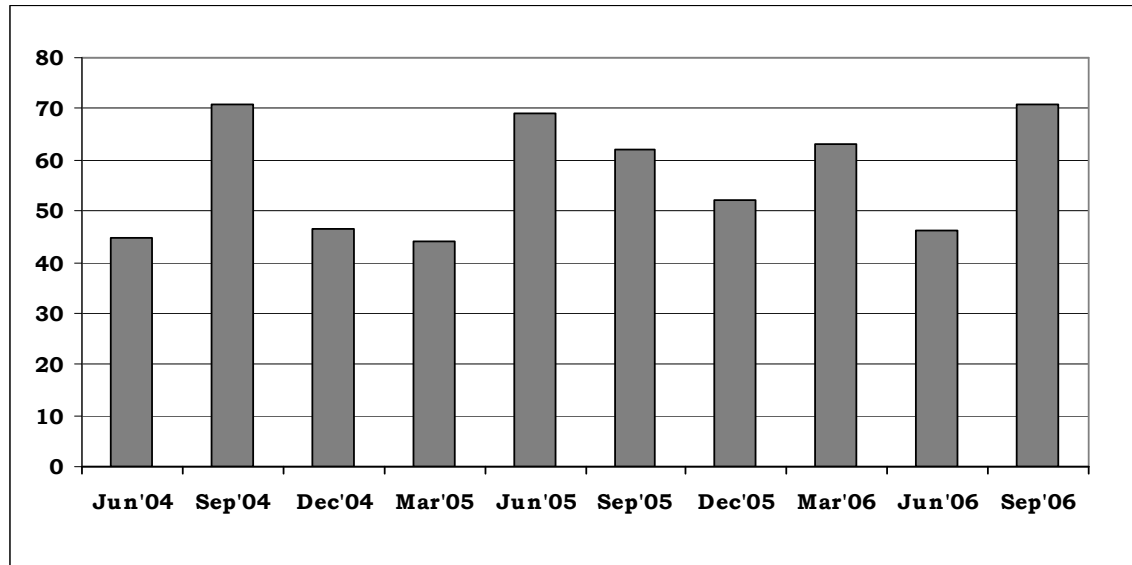
Type	Permits	2005			2006		
		QII	QIII	QIV	QI	QII	QIII
Residential	Value	8.27	11.93	9.05	18.05	23.53	28.40
	Number	49	61	40	54	45	71
Commercial	Value	1.14	0.00	14.59	0.88	1.13	0.00
	Number	5	0	7	3	2	0
Other	Value	22.87	1.38	1.12	70.31	0.33	1.32
	Number	18	3	2	5	1	2
<b>Total</b>	Value	32.28	13.31	24.76	89.24	24.99	29.72
	Number	72	64	49	62	48	73
	Number*	69	62	52	63	46	71

Source: Maseru City Council and Land Survey and Physical Planning

(1) Excludes data on buildings constructed without obtaining building permits. The table also excludes data on Mafeteng, Mokhotlong and Mohale's Hoek districts.

(2) Number\* denotes seasonally adjusted figures

**Figure 1: Number of Building Permits**  
(Million Maloti)



### ***Imported Motor Vehicles***

Data on imports of motor vehicles by both the private and Government sectors is used as an indicator of gross fixed capital formation. Imports of motor vehicles dropped in the third quarter of 2006. On a quarterly basis, the number of imported motor vehicles decreased by a seasonally adjusted 30.0 per cent in contrast with a 114.7 per cent rise observed in the previous quarter. Significant decreases were observed in cars, and vans. However, the decrease largely reflected the return to normality following the replacement of the Government fleet at the end of September. In the previous quarter, Government imported 251 motor vehicles compared with 48 cars imported in the review quarter. On an annual basis, the total number of imported motor vehicles increased by 32.5 per cent following 18.5 per cent growth in the previous quarter. In addition, the persistent increase in the number of imported trucks was indicative of the rise in investment. The improvement on an annual basis continued to be in accordance with a rise in credit extended to the private sector.

**Table 3: Motor Vehicle Imports**

(Value in Million Maloti)

		<b>Cars</b>	<b>Vans</b>	<b>Trucks</b>	<b>Buses</b>	<b>Trac-tors</b>	<b>M/ Cycles</b>	<b>Trail-ers</b>	<b>Total</b>	
<b>2004</b>	<b>III</b>	Value	17.40	16.34	2.62	4.02	0.21	0.00	0.56	41.15
		Number*								1011
		Number	323	244	6	45	7	0	15	640
	<b>IV</b>	Value	19.57	19.23	0.21	5.01	0.52	0.00	0.81	47.23
		Number*								700
		Number	346	205	5	45	12	0	12	625
<b>2005</b>	<b>I</b>	Value	15.79	25.19	1.57	2.77	0.70	0.01	0.48	46.51
		Number*								658
		Number	349	299	2	26	8	1	13	698
	<b>II</b>	Value	23.18	31.41	2.12	4.12	0.49	0.33	0.52	62.17
		Number*								809
		Number	385	364	5	26	5	7	9	801
<b>III</b>		Value	10.26	21.51	0.02	0.22	0.63	0.12	0.56	33.32
		Number*								348
		Number	165	180	2	15	12	8	10	392
	<b>IV</b>	Value	15.42	28.25	2.78	4.08	0.19	0.05	0.24	51.01
		Number*								505
		Number	210	208	5	13	6	1	8	451
<b>2006</b>	<b>I</b>	Value	15.42	28.25	2.78	4.08	0.19	0.05	0.24	51.01
		Number*								307
		Number	152	135	0	22	9	0	8	326
	<b>II</b>	Value	25.04	31.38	4.08	5.30	0.22	0.20	0.20	66.42
		Number*								659
		Number	336	223	13	31	5	7	9	624
<b>III</b>		Value	18.92	23.81	5.90	6.16	0.11	0.01	0.88	55.79
		Number*								461
		Number	259	187	24	23	3	2	11	509

Source: Imperial Fleet Services Lesotho and Customs Department  
(1) Number\* denotes seasonally adjusted figures

+ Includes imports of second hand cars



## **Electricity Consumption**

Consumption of electricity for general purposes, domestic and industrial purposes is indicative of the performance of the electricity sub-sector. Furthermore, consumption of electricity by the industrial sub-sector reflects the performance of the private business sector largely dominated by the manufacturing sub-sector (which continues to be the pillar of Lesotho's economy). At the end of September, overall electricity consumption increased by 6.2 per cent and 4.3 per cent in unit and value terms, respectively. All categories reflected an improvement. This increase signals good performance of the electricity sub-sector.

**Table 4: Electricity Consumption by LEC Customers**

<b>Quarter</b>		<b>General Purpose</b>	<b>Domestic</b>	<b>Commercial &amp; Industrial</b>	<b>Total</b>
<b>2006 II</b>	kwh	17.43	33.71	74.64	125.78
	Value	12.14	17.36	32.60	62.10
<b>III</b>	kwh	19.38	34.59	79.54	133.51
	Value	13.08	17.82	33.87	64.76

Source: Lesotho Electricity Authority

## **Water Consumption**

Water usage by the industrial sector also serves as one of the indicators of activity within the Lesotho manufacturing sub-sector. The dominant industries in the manufacturing sub-sector are the 'textile and clothing' and the 'food and beverages' industries, which are heavily reliant on water usage. In the third quarter of 2006, the units of water consumed by the 'wet' industries increased by a seasonally adjusted 4.2 per cent compared with a 4.4 per cent increase that was realised at the end of June 2006. On an annual basis, water consumption by the wet industries increased by 18.4 per cent.

Overall consumption of water rose by 1.7 per cent over the quarter compared with 12.7 per cent growth realised in the previous quarter. Water consumption was estimated to increase on account of the on-going Maseru Peri-Urban Water Supply Project which is aimed at supplying peri-urban areas around the city. Phase I of the project which is intended to supply the Eastern part of Maseru, is due for completion at the end of December 2006. Furthermore, Phase II of Project which is expected to commence in February 2007, will supply water to the Northern and Western parts of the city.

**Table 5: Water Consumption**

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

<b>Quarter</b>		<b>Domestic</b>	<b>Industrial</b>	<b>Other</b>	<b>Total</b>
<b>2004</b> <b>III</b>	Units	0.76	1.49	0.52	2.77
	Value	2.73	6.14	2.11	10.98
	Units*		1.42		2.70
<b>IV</b>	Units	0.95	1.44	0.54	2.93
	Value	3.66	5.88	2.24	11.78
	Units*		1.30		2.96
<b>2005</b> <b>I</b>	Units	0.95	1.20	0.53	2.68
	Value	3.69	4.97	2.20	10.86
	Units*		1.40		2.64
<b>II</b>	Units	0.79	1.36	0.61	2.76
	Value	3.07	6.05	2.59	11.71
	Units*		1.29		2.69
<b>III</b>	Units	0.80	1.38	0.57	2.75
	Value	3.07	6.14	2.53	11.74
	Units*		1.25		2.77
<b>IV</b>	Units	0.95	1.25	0.58	2.78
	Value	3.82	5.55	2.60	11.97
	Units*		1.13		2.80
<b>2006</b> <b>I</b>	Units	0.92	1.16	0.58	2.65
	Value	3.72	5.19	2.60	11.97
	Units*		1.36		2.60
<b>II</b>	Units	0.78	1.40	0.65	2.83
	Value	3.20	6.52	3.05	12.77
	Units*		1.42		2.93
<b>III</b>	Units	0.78	1.51	0.65	2.94
	Value	3.11	7.05	2.87	13.03
	Units*		1.48		2.98

Source: Water and Sewerage Authority

*(1) Units\* denotes seasonally adjusted figures*

## Telephone Statistics

The statistics on the number of calls destined to SA and other countries is used as an indicator of the performance of the telecommunications sub-sector. During the quarter under review, the number of calls, adjusted for seasonal changes, increased by 2.0 per cent in contrast with 2.1 per cent increase registered in the previous quarter. The rise was attributed to the overall pick-up in the number of calls destined to SA and other countries. The improvement indicates good performance in the telecommunications sub-sector.

**Table 6: Telephone Traffic Statistics**

		<b>SA Outgoing Calls</b>	<b>International Calls</b>	<b>Total Calls</b>
<b>2005</b>	<b>II</b>			
	No. of calls (millions)	3.43	0.11	3.54
	No. of calls*	3.73		3.83
	Total Duration	4.68	0.36	5.04
	Nominal Value	8.88	2.98	11.86
<b>III</b>	No. of calls (millions)	3.19	0.12	3.31
	No. of calls*	3.25		3.15
	Total Duration	4.53	0.35	4.88
	Nominal Value	8.60	2.88	11.84
<b>IV</b>	No. of calls (millions)	3.42	0.13	3.55
	No. of calls*	3.47		3.36
	Total Duration	4.82	0.41	5.23
	Nominal Value	10.12	3.41	13.53
<b>2006</b>	<b>I</b>			
	No. of calls (millions)	3.41	0.15	
	No. of calls*	3.25		3.19
	Total Duration	4.86	0.56	5.42
	Nominal Value	10.21	5.11	15.32
<b>II</b>	No. of calls (millions)	3.21	0.08	3.29
	No. of calls*	3.75		3.85
	Total Duration	3.02	0.36	3.38
	Nominal Value	6.66	3.89	10.55
<b>III</b>	No. of calls (millions)	3.81	0.28	4.09
	No. of calls*	3.91		3.93
	Total Duration	5.37	1.64	7.01
	Nominal Value	12.36	12.02	24.38

Source: Tele-Com Lesotho

(1) No. of calls\* refers to number of calls that have been adjusted for seasonality.

## V. Employment and Prices

### *Employment Developments*

The level of employment in the manufacturing sub sector of the economy is largely dependent on employment in the LNDC assisted companies. There was an observed increase in the level of employment within the manufacturing sub sector during the third quarter of 2006. Employment in these companies increased by an estimated 2.3 per cent on a quarterly basis, while on an annual basis it increased by 16.6 per cent. This was a movement from 45 140 to 46 189 in the period ending September. It is however cautioned that the June figure was adjusted for temporary employees during the period.

Most of the manufacturing firms, the majority of which are LNDC-assisted companies, have been operating at full capacity. This trend is expected to prevail for a long period given the projected positive general economic outlook. The domestic economy proved resilient during the quarter under review, given some negative international economic developments.

**Table 7: Employment Trends of LNDC Assisted Companies**

<b>Period</b>	<b>QI</b>	<b>QII</b>	<b>QIII</b>	<b>QIV</b>
<b>2006</b>	40459	45140*	46189	
<b>2005</b>	41985	40111	39597	43131
<b>2004</b>	52532	53525	52922	50607
<b>2003</b>	43525	46960	49862	51187
<b>2002</b>	36906	39255	42011	43773

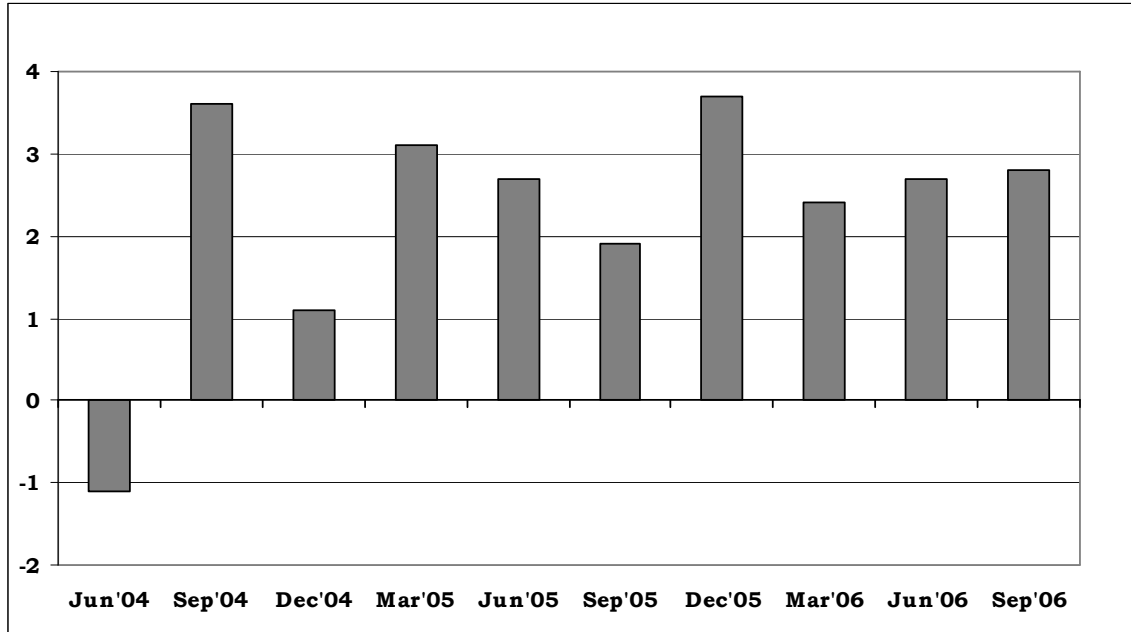
Source: LNDC

\*Revised figures

Government employment stood at 38 323 for the period ending September 2006, this is contrasted with 38 089 for the second quarter. This was an estimated increase of 0.6 per cent, and it was mainly

attributable to the increase in the number of teachers and a slight growth in the general civil servants. The increment in the number of teachers is expected to maintain an upward trend, if government education roll out is extended to cover basic education for the first ten years of schooling.

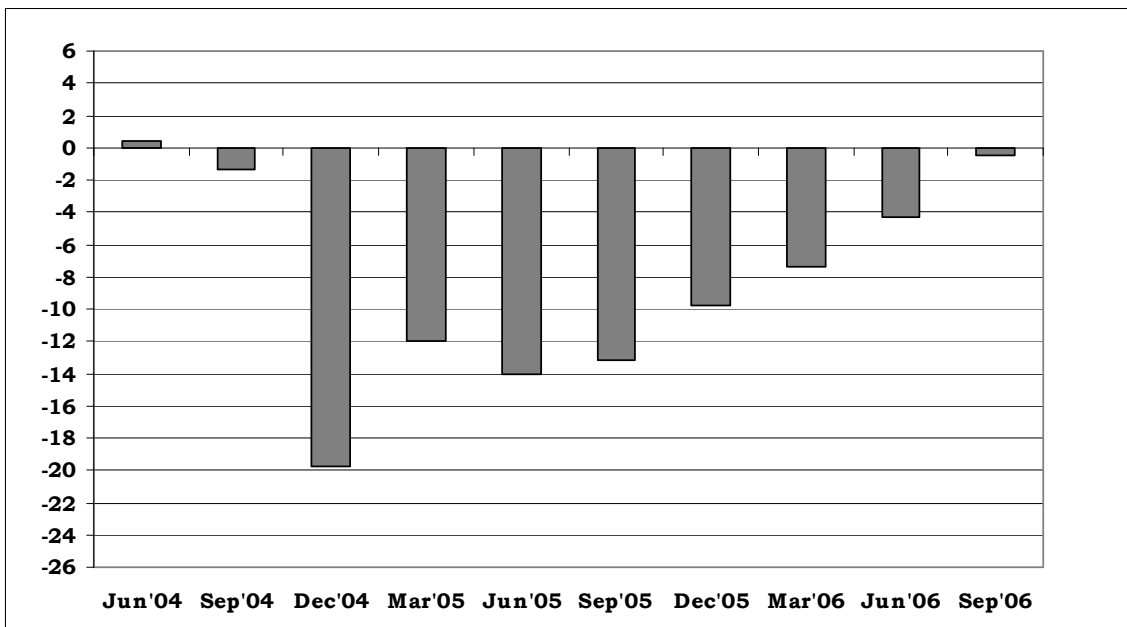
**Figure 2: Annual Percentage Change in Government Employment**



Source: Government of Lesotho

The number of mineworkers employed in the South African mines for the third quarter was estimated to have increased by 2.1 per cent. This was an increase from 50 640 to 51 724 workers. The increase has largely been a result of an increase in the price of gold, which managed to curb spiralling costs. It was further noted that though the sector registered an increase, this was a slower increase than the rate realised in the second quarter. Some of the marginal mines started to operate close to optimal output. The year-on-year movement indicated a decrease of 0.3 percent and this was a smaller decline compared with the first half of the year.

**Figure 3: Annual Percentage Change in Migrant Mineworkers Employment**



Source: Various mining recruitment agencies

### ***Price Developments***

The level of inflation as measured by changes in the CPI, accelerated from 6.6 per cent in June to 6.8 for the period ending August. The increase was mainly influenced by the category 'food and non alcoholic beverages' with its index increasing by 11.4 per cent in August, and within this category, maize meal increased by 5.4 percent. The category 'furniture, households' 'equipment and routine maintenance' decelerated from 4.7 per cent to 4.0 per cent in August. The last major contributor was 'clothing and footwear' which increased by 1.8 per cent in August 2006 relative to 2.9 per cent realised in June 2006.

Inflation is expected to decelerate in the third quarter<sup>3</sup>. This may be as a result of retarded growth in the South African producer price index which is usually transmitted into Lesotho inflation with an estimated lag of at least four months. It is further noted that even the Lesotho component of administered prices has relatively been stable. The major influence has been the fuel products component. It is nonetheless cautioned that the cereal sub-component of the food category has consistently been exerting an upward pressure, due to the low yield

<sup>3</sup> The inflation figure for the end of the quarter is not available.

realised in the previous harvest period. Inflation at the end of the year is projected at an average of 6.0 percent.

**Table 8: Inflation**

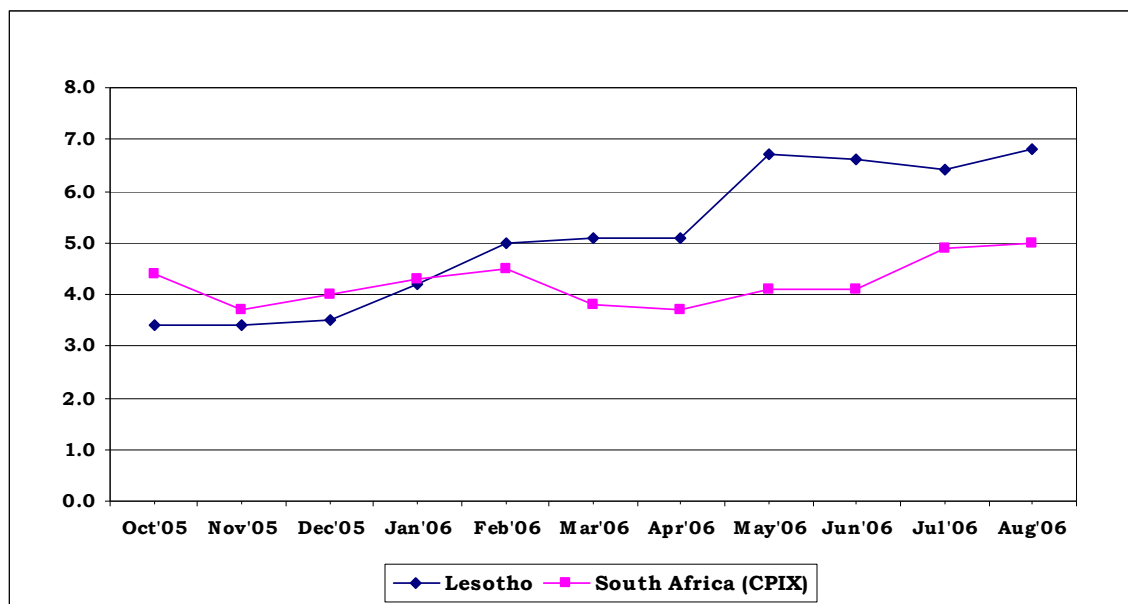
(Annualised Percentage Change)  
Base Period: 1997

	Weight	2006				
		Apr	May	Jun	Jul	Aug
All items	100.0	5.1	6.7	6.6	6.4	6.8
Food and non-alcoholic beverages	39.8	5.9	9.5	10.0	10.0	11.4
Alcoholic beverages & Tobacco	6.4	6.2	7.5	6.3	5.9	5.8
Clothing & footwear	15.6	3.7	3.4	2.9	2.5	1.8
Housing, electricity gas & other fuels	3.7	8.8	9.9	8.6	7.5	7.6
Furniture, households equipment & routine maintenance of house	17.0	4.5	4.8	4.7	4.6	4.0
Health	1.4	2.6	2.2	0.7	0.7	0.7
Transport	7.8	4.1	3.9	3.5	3.2	2.8
Communication	0.1	0.0	0.0	3.4	3.4	3.4
Leisure, entertainment & Culture	1.2	3.3	0.3	-0.4	1.2	1.2
Education	3.2	1.0	1.1	0.7	0.7	0.7
Restaurant & Hotels	0.4	5.5	8.3	7.8	7.0	7.0
Miscellaneous goods & services	3.2	1.9	2.1	2.8	2.8	3.3

Source: Bureau of Statistics, Lesotho



**Figure 4: Annual Inflation for Urban Households**  
(Per Cent)



Source: Bureau of Statistics and Statistics South Africa

## VI. Balance of Payments (BOP)

### Overview

Lesotho's external sector position improved during the third quarter. The overall balance recorded a seasonally adjusted surplus of M639.9 million compared with that of M175.2 million registered in the previous quarter. The increase in the overall balance was a result of developments in the current account coupled with the depreciation of the local currency. Transaction balance, which represents the overall balance excluding the effects of currency fluctuations, also recorded a seasonally adjusted surplus of M371.0 million during the review quarter compared with M209.1 million in the previous quarter. The improvement in the BOP position during the period resulted in an increase in gross official reserves, from 6.2 months of import cover in the second quarter to 7.1 months during the quarter under review.

The current account registered a surplus equivalent to 1.3 per cent of GDP. The surplus was driven largely by the receipt of SACU revenue during the quarter under review. SACU non-duty receipts rose by 0.4 per cent over the quarter. In addition, the trade deficit narrowed as a result of an improvement in the exports sub-sector. The capital and financial

account registered a net outflow of M34.2 million during the reporting quarter compared with M88.7 million recorded in the previous quarter. This net outflow resulted mainly from an increase in commercial banks foreign assets.

**Table 9: Summary of Balance of Payments**

(Million Maloti)

	2005		2006		
	QIII	QIV	QI*	QII*	QIII+
<b>I. CURRENT ACCOUNT</b>	-23.30	27.15	-15.98	-40.26	32.72
Goods, Services and Income	-536.50	-473.87	-598.25	-716.33	-647.02
(a) GOODS	-974.70	-833.56	-1093.44	-1204.52	-1185.30
Merchandise exports f.o.b.	992.00	1165.09	876.07	1049.43	1517.91
Merchandise imports f.o.b.	-1966.70	-1998.64	-1969.52	-2253.95	-2703.21
(b) SERVICES	-72.65	-52.44	-58.84	-75.46	-68.37
(c) INCOME	510.85	412.12	554.04	563.65	606.65
Labour	482.58	474.53	522.50	527.31	533.60
Other	28.27	-62.41	31.54	36.34	73.05
(d) CURRENT TRANSFERS	513.20	501.02	582.27	676.06	679.74
Government, net	496.66	474.17	552.42	646.21	649.88
SACU non-duty receipts	497.7	469.91	473.06	641.83	644.60
Other	-1.04	4.26	79.36	4.38	5.28
Other Sectors	16.54	26.85	29.85	29.85	29.86
<b>II. CAPITAL AND FINANCIAL ACCOUNT</b>	-49.52	221.82	288.52	88.74	-32.41
(e) CAPITAL ACCOUNT	34.50	8.20	4.90	7.00	20.00
(f) FINANCIAL ACCOUNT	-84.02	213.62	283.62	-81.74	-52.41
Special Financing – LHWP	49.24	61.35	43.35	31.26	31.26
<b>III. RESERVE ASSETS</b>	26.53	-86.90	-177.17	-441.12	-641.50
<b>IV. ERRORS AND OMISSIONS</b>	-13.92	-100.00	-84.12	411.31	377.47
<b>V. VALUATION ADJUSTMENT</b>	-62.06	-62.06	-11.26	-18.66	263.72

\* Revised estimates

+ Preliminary estimates

## ***Merchandise Trade***

### Exports

During the third quarter, merchandise exports, seasonally adjusted rose further by 38.5 per cent compared with the 20.1 per cent increase recorded in the previous quarter. On an annual basis, merchandise exports rose by 53.0 per cent. The strong growth observed during the last two quarters is indicative of the recovery of the Lesotho textiles sub-sector. Diamond exports are also contributing to the growth. Exports of diamonds grew by 86.9 per cent during the quarter. The Government of Lesotho has intensified efforts to turn around the sub-sector following the negative impact of 2005. The remarkable performance of exports bodes well with the developments in the domestic economy. Indicators such as water consumption in the industrial areas, telephone traffic statistics and employment in LNDC assisted companies showed some strong improvements. On the demand side, the economic slowdown in the US, if sustained, may negatively affect the observed recovery in the textile sub-sector.

### Imports

Merchandise imports, seasonally adjusted increased by 18.2 per cent compared with a revised 6.3 per cent registered during the previous quarter. On an annual basis, imports grew by 37.4 per cent. The growth in imports was consistent with the observed economic recovery in the country. In addition, the rate of implementation of government projects increased significantly during the quarter. Capital expenditure rose by 64.7 per cent in the review period compared with an increase of 1.6 per cent in the previous quarter.

**Table 10: Value of Exports by Section of the S.I.T.C.**

(Million Maloti)

COMMODITY	2005		2006		
	III	IV	I	II*	III+
0. Food & Live Animals	21.56	33.04	31.58	24.53	31.82
Cattle	1.83	1.79	1.28	0.13	0.25
Wheat Flour	6.64	8.33	10.62	13.18	15.57
Maize Meal	4.14	5.92	6.81	5.69	7.07
Other	8.95	17.00	12.87	5.53	8.93
1. Beverages & Tobacco	35.40	36.56	31.68	34.99	39.62
Beverages	35.36	36.39	31.68	34.99	39.62
2. Crude Materials	5.78	7.14	6.09	0.99	2.55
Wool	5.78	7.14	6.09	0.99	2.55
4. Chemicals	2.20	3.27	3.09	15.14	2.68
5. Manufactured Goods	105.36	194.63	103.84	161.63	321.45
6. Machinery & Transport Goods	92.21	113.91	84.39	79.05	143.80
7. Miscellaneous Manufactured Goods	723.73	772.50	612.74	730.25	969.78
8. Unclassified Goods	5.76	4.04	2.66	2.85	6.21
<b>TOTAL EXPORTS</b>	<b>992.00</b>	<b>1165.9</b>	<b>876.07</b>	<b>1049.43</b>	<b>1517.91</b>

Note: Totals may not tally due to rounding

\* Revised estimates

+ Preliminary estimates

#### Direction of Trade

During the review quarter, the US remained the largest recipient of Lesotho exports. The share of exports to the US was estimated at 55.3 per cent compared with 66.1 per cent registered in the previous quarter. The second largest share of Lesotho exports is destined to the SACU market. Exports to SACU rose from 17.5 per cent as a share of total exports in the second quarter to 24.7 per cent in the review quarter. The European market was the third largest recipient of Lesotho's exports, particularly diamonds to Belgium. Its share increased to 17.6 per cent during the quarter, following 13.6 per cent registered in the previous

quarter. The proportion of exports to Asia registered 0.1 per cent in the review quarter compared with 1.0 per cent observed in the previous quarter.

**Table 11: Direction of Trade - Exports and Re-Exports, f.o.b.**  
(Million Maloti)

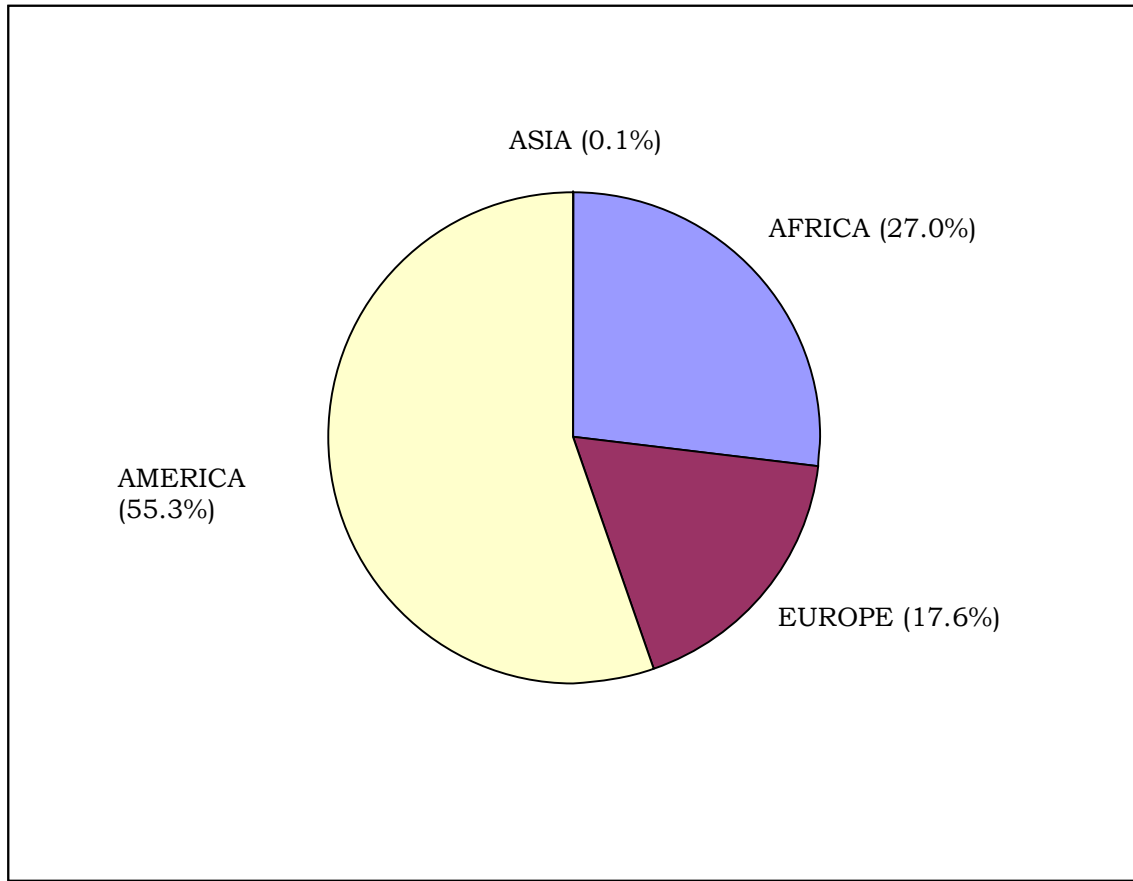
REGION	2005		2006					
	QIV AMOUNT	% SHARE	QI AMOUNT	% SHARE	QII* AMOUNT	% SHARE	QIII+ AMOUNT	% SHARE
World	1165.09	100	876.07	100	1049.4 3	100	1517.91	100
Africa	314.68	27.09	183.65	20.97	210.17	20.03	410.64	27.05
SACU	303.89	26.16	169.77	19.38	184.13	17.54	375.55	24.74
SADC	0.43	0.04	4.28	0.49	1.74	0.17	0.60	0.04
Other	10.36	0.89	9.60	1.10	24.3	2.32	34.49	2.27
Europe	172.64	14.82	80.89	9.23	142.78	13.61	266.73	17.57
EC	172.64	14.82	80.89	9.23	142.78	13.61	266.73	17.57
America	675.22	58.12	601.70	68.68	693.19	66.05	839.50	55.31
Asia	2.55	0.22	9.83	1.12	3.29	0.31	1.04	0.07

Note: Total may not tally due to rounding

\* Revised estimates

+ Preliminary estimates

**Figure 5: Direction of Trade Exports**  
(Quarter III)



### **Labour Income**

During the quarter under review, labour income, seasonally adjusted grew by 2.8 per cent compared with a decline of 1.7 per cent in the previous quarter. On an annual basis, labour income rose by 5.9 per cent. The performance of labour income was influenced by miners' remittances. Miners' remittances rose by 1.2 per cent during the quarter. The growth was due to the increase in the number of Basotho employed in the SA mining industry. As already mentioned, the number of Basotho employed in the SA mining industry rose by 2.1 per cent during the quarter. This was in line with the performance of the industry. Mining production in SA rose by 1.2 per cent in the three months to August.

## **Investment Income**

Net investment income further recorded a surplus of M73.1 million compared with M36.3 million in the previous quarter. Inflows of investment income continued to grow during the quarter. The inflows grew by 26.5 per cent compared with 8.6 per cent recorded in the previous quarter. The growth was due to increases in both CBL and commercial banks interest earnings. Interest earnings to CBL rose by 14.3 per cent, while those of the commercial banks grew by 68.2 per cent during the review period. A confluence of factors may explain the observed performance. Foreign assets of both CBL and commercial banks rose significantly during the quarter due to the general increase in the level of interest rates in both the developed countries and SA.

During the third quarter, outflows of investment income declined by 32.5 per cent compared with an increase of 3.9 per cent in the previous period. The decline was mainly driven by the fall in the interest paid on official loans by 64.6 per cent during the quarter. Interest paid by commercial banks also declined by 45.4 per cent. This was driven by the decline in commercial banks liabilities observed during the quarter.

## **Travel**

Net travel earnings rose to M17.4 million compared with M14.8 million during the previous quarter. This represented an increase of 17.6 per cent over the quarter. On an annual basis, travel receipts grew by 5.6 per cent during the quarter. Tourism spending rose by 0.1 per cent on quarterly basis. Tourism sub-sector in Lesotho is still in the embryonic stage but the on-going efforts by the Government seem to be bearing positive results.

Travel payments declined by 0.7 per cent during the quarter compared with the increase of 1.4 per cent in the previous quarter. The decline was attributed to the decline in government international subsistence allowances by 7.1 per cent during the review period.

## **Current Transfers**

During the review period, net current transfers, seasonally adjusted rose to M686.0 million from M675.0 million recorded in the previous quarter. On an annual basis, net current transfers grew by 32.5 per cent. The



performance of current transfers was mainly influenced by increased SACU non-duty receipts.

### ***Capital and Financial Account***

The capital and financial account declined from a net inflow of M88.7 million at the end of the second quarter to a net outflow of M32.4 million during the quarter under review. The observed net outflow resulted from the net outflow in the 'other investment' category. Other investment registered a net outflow of M183.6 million. This was mainly driven by the increase in commercial banks foreign assets coupled with the decline in their foreign liabilities. During the review period, commercial banks foreign assets rose by M182.6 million while their foreign liabilities fell by M56.8 million. The commercial banks foreign assets increased because of transfers abroad.

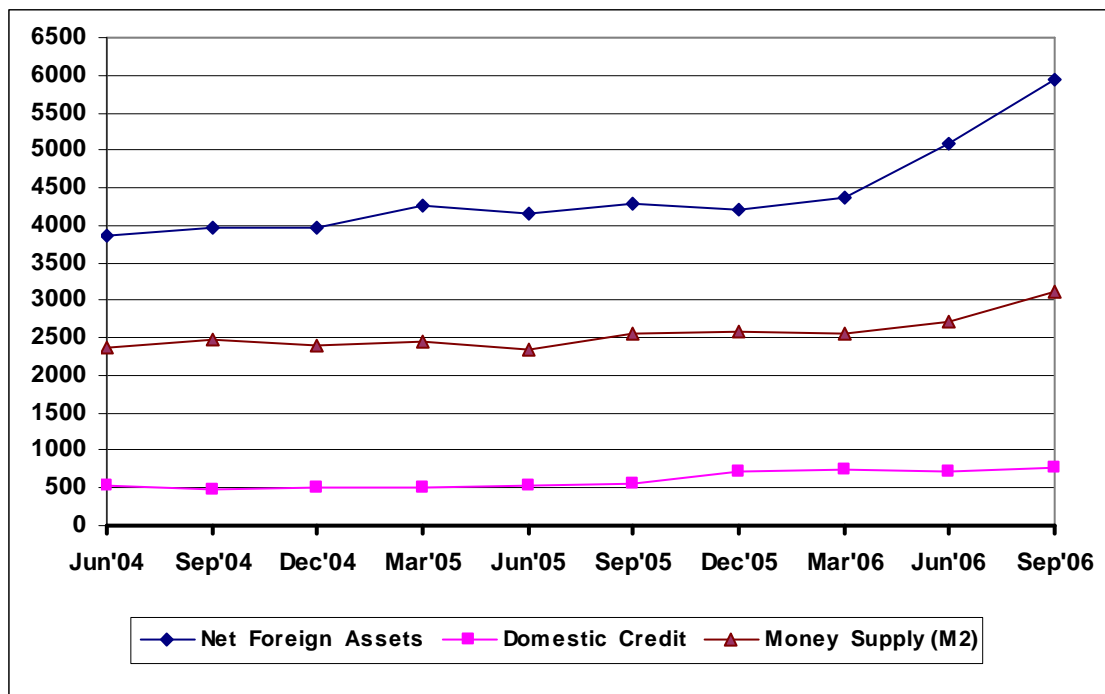
## **VIII. Money and Banking**

### **Money Supply**

#### **Determinants of Money Supply**

At the end of the review quarter, the broad measure of money supply (M2) increased further by 15.4 per cent on a quarterly basis, compared with an increase of 5.3 per cent observed at the end of June. This increase was at the back of a rise of 16.9 per cent in the overall banking system's net foreign assets, coupled with a rise of 6.8 per cent in domestic credit. On an annual basis, money supply rose by 22.7 per cent following a 16.7 per cent rise recorded at the end of June. The year on year rise in money supply was mainly attributable to the growth realised in both domestic credit and the overall banking sector's net foreign assets adjusted for revaluation changes.

**Figure 6: Overview of Recent Monetary Developments**



**Table 12: Determinants of Money Supply**

(Million Maloti; Changes)

Determinants	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
Net foreign assets	-81.2	154.2	-84.6	166.2	698.2	858.8
Domestic credit	9.7	32.1	159.7	26.6	-17.1	49.7
To statutory bodies	-8.3	-7.8	-13.3	-4.0	-11.4	-2.5
To private sector	18.0	39.9	173.0	30.6	-5.7	52.3
Other items, net	59.4	-37.2	29.5	215.9	543.8	491.3
Money Supply (M2)	-130.9	223.5	51.8	-23.1	137.0	417.5

## Components of Money Supply

Money supply comprises narrow money (M1) and quasi money. M1 increased by 18.2 per cent at the end of the review quarter, compared with a rise of 6.6 per cent recorded at the end of the previous quarter. The increase in M1, was mainly due to a 16.7 per cent rise in currency with public along with a 20.4 per cent increase in demand and call deposits. In addition, quasi money also rose by 7.9 per cent in September following a 2.0 per cent increase which was noted at the end of the quarter ended June. Quasi money rose due to a 30.5 per cent increase in time deposits which off-set a fall of 6.5 per cent in savings deposits. The observed increase in interest earning components of money namely, savings and time deposits, might indicate that the opportunity cost of holding money for transactional purposes is increasing due to the upward movement in interest rates.

**Table 13: Money Supply**

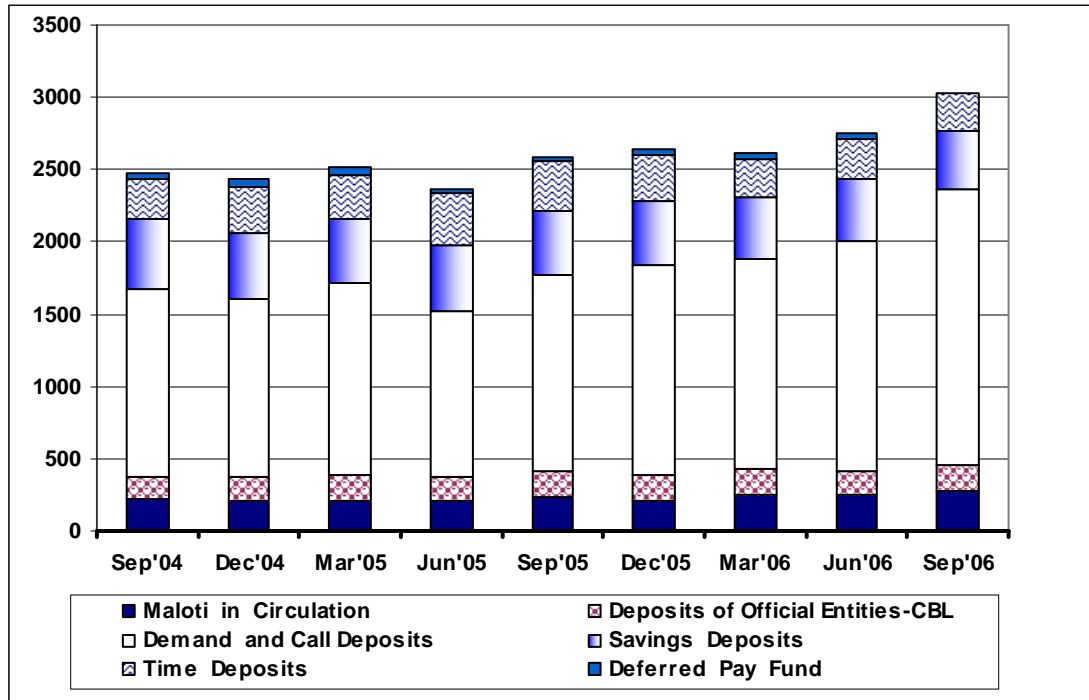
(Million Maloti; End of Period)

	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
Money Supply (M2)	2320.9	2544.4	2590.0	2566.9	2704.0	3121.5
Money (M1)	1514.2	1790.1	1760.8	1864.8	1987.6	2348.6
Maloti with public	202.5	232.0	212.8	247.4	242.6	283.1
Demand deposits <sup>(1)</sup>	1135.3	1347.4	1440.0	1440.0	1568.3	1888.1
Deposits of official Entities with CBL	176.4	176.7	176.7	177.4	176.7	177.4
Quasi-Money	806.7	788.3	760.5	702.2	716.4	772.8
Savings deposits	453.4	451.1	437.1	436.4	438.0	409.5
Time deposits	353.3	337.2	323.4	265.8	278.5	363.4

(1)- includes call deposits

NB: Totals may not tally due to rounding off

**Figure 7: Components of Money Supply**



### Commercial Banks' Deposits by Holder

A pool of deposits held with commercial banks comprises deposits held by the private sector and statutory bodies. Total deposits rose by 16.6 per cent, at the end of September compared with a 6.6 per cent increase recorded at the end of the quarter ended June. The table below shows that the rise was largely driven by a 28.9 per cent increase in private sector deposits which overshadowed a 16.7 per cent decline in deposits held by statutory bodies.

**Table 14: Commercial Banks Deposits by Holders**

(Million Maloti; End of Period)

	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
<b>TOTAL DEPOSITS</b>	1930.1	2123.7	2188.4	2130.2	2271.5	2649.4
<b>Private Sector</b>	1543.7	1667.1	1655.7	1598.7	1660.8	2140.6
Demand deposits	871.4	1014.8	1025.0	1001.3	1033.2	1469.5
Savings deposits	453.4	451.1	437.1	436.4	437.9	409.5
Time deposits	219.0	201.2	193.7	161.0	189.6	261.7
<b>Statutory Bodies</b>	349.7	415.9	494.0	531.5	610.7	508.8
<b>Deferred Pay Fund</b>	36.7	40.8	38.7	0.0	0.0	0.0

NB: Totals may not tally due to rounding off

**Liquidity of Commercial Banks**

One important function performed by commercial banks is the management of liquidity risk in the economy. The liquidity of commercial banks is measured by the ratio of their cash and near cash assets, including investment with maturities of less than twelve months at issue, to all their deposit liabilities. The ratio represents a chosen mix of cash and credit which enables the bank to honour customers' cash demand. The ratio declined from 72.2 per cent in June to 67.2 per cent at the end of September.

**Table 15: Components of Commercial Banks' Liquidity**

(Million Maloti; End of Period)

COMPONENT	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
Maloti Notes and Coins	58.3	57.1	85.2	64.7	69.6	43.3
Rand Notes and Coins	9.4	9.1	20.3	10.0	12.5	34.2
Balances due from Lesotho Banks	606.3	793.6	741.4	633.6	713.6	15.671
Balances due from Foreign Banks	974.5	1152.2	1051.9	938.1	1200.9	1382.5
Clearing Balances with CBL	12.2	63.2	70.7	24.8	29.7	15.9
RSA Short-term Securities	0.0	0.0	0.0	0.0	0.0	0.0
CBL Bills	0.0	0.0	0.0	0.0	0.0	0.0
Lesotho Government Securities	376.9	378.9	383.3	415.0	328.6	409.6

The credit deposit ratio measures the extent to which banks use deposit liabilities to finance economic activity. The ratio declined from 31.3 per cent registered in June to 28.7 per cent in September. This fall implied a faster increase in deposit liabilities which exceeded the rise in credit extended during the review quarter. Nevertheless, it is vital for this ratio to increase in order to enhance financial deepening in the economy, which in turn, would foster economic growth.

**Table 16: Consolidated Balance Sheet of Commercial Banks**

(Million Maloti; End of Period)

	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
Net foreign assets	1150.1	1310.3	1135.0	1139.0	1375.2	1614.6
Deposits with CBL	96.3	159.6	247.3	149.0	125.5	101.5
Credit:	963.2	995.5	1161.1	1217.4	1115.4	1247.8
o/w*: Statutory Bodies	54.5	46.7	33.4	29.4	17.9	15.4
Private Sector	455.5	493.7	666.1	696.9	691.9	745.0
Government:	453.2	455.2	461.6	491.1	404.5	487.4
o/w: Securities	452.5	454.5	461.6	490.6	404.3	487.4
Loans and Advances	0.6	0.7	0.5	0.5	0.2	0.0
<b>ASSETS/LIABILITIES</b>	2209.7	2465.5	2543.4	2505.4	2616.0	2963.9
Private sector deposits <sup>(2)</sup>	1930.1	2123.7	2188.4	2130.2	2271.5	2649.4
Government deposits	77.1	140.4	171.9	164.1	171.7	110.6
Capital, reserves & other, net	202.5	201.5	183.1	211.0	171.6	203.9

\* of which

(2)- includes statutory bodies' deposits.

***Demand for Money*****Domestic Credit**

At the end of September, domestic credit increased by 7.0 per cent, as opposed to a fall of 2.3 per cent observed at the end of the previous quarter. The rise mainly reflected an increase in credit extended to the private sector which off-set a fall in the portion granted to statutory bodies. Furthermore, domestic credit was observed to have risen by 39.4 per cent on an annual basis compared with an increase of 38.4 per cent recorded at the end of June.

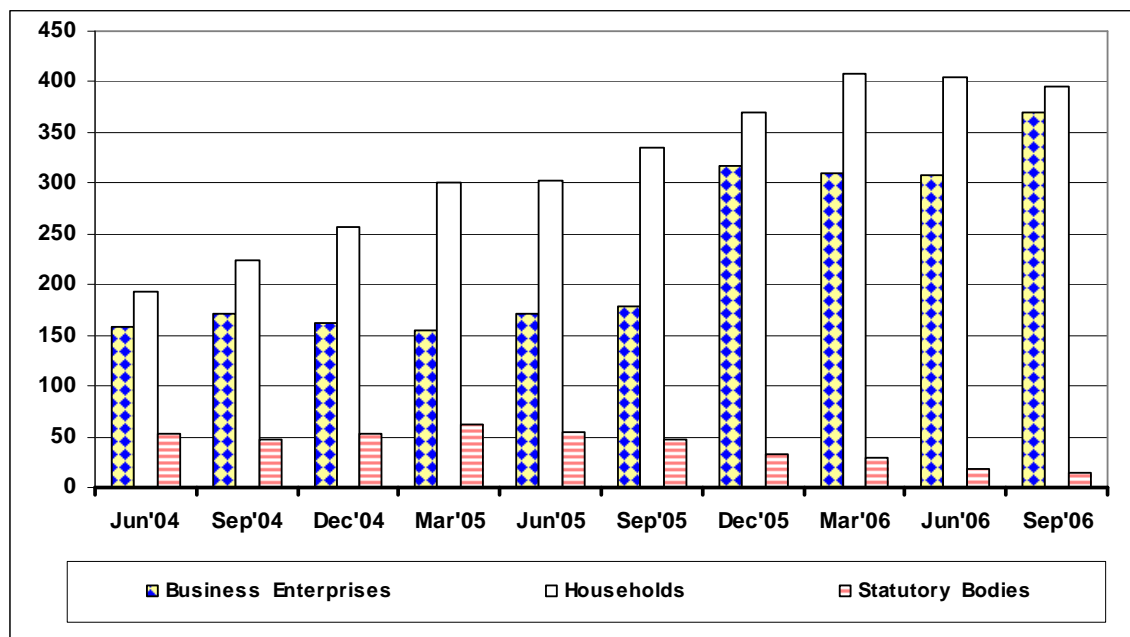
**Table 17: Domestic Credit**

(Million Maloti; End of Period)

	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
<b><u>DOMESTIC CREDIT</u></b>	528.8	560.9	719.3	747.1	731.1	782.0
Credit to private sector	474.3	514.3	685.9	717.7	713.2	766.6
Business enterprises	171.1	179.1	316.6	310.5	307.8	370.7
Households	303.2	335.1	369.3	407.3	405.4	395.9
Credit to statutory bodies	54.5	46.7	33.4	29.4	17.9	15.4

**Figure 8: Distribution of Credit by Holder**

(Million Maloti: End of Period)





## Credit to Private Sector

Credit to the private sector increased by 7.5 per cent during the quarter ending September, contrasted with a decline of 1.0 per cent registered in June. The rise was driven by a 20.4 per cent increase in credit extended to business enterprises which off-set the decline in credit granted to households. The performance of credit extended to the private sector reflected a like increase in economic activity driven by this sector during the review quarter.

Furthermore, private sector credit remained strong during the period under review on an annual basis. It increased by 39.4 per cent following a 38.2 per cent increase reported at the end of the quarter ended in June. Although credit to households declined during the September quarter, its share in total private sector credit remained large at 51.6 per cent. The larger share of credit granted to households indicated that much of the deposits that were mobilised by the banking system were used to finance more of consumption expenditure than productive investment.

## **Credit to Statutory Bodies**

The volume of credit extended to statutory bodies was expected to decline due to the on-going privatisation process in the medium to long-term. As expected, it declined by 14.2 per cent in September, compared with a fall of 39.0 per cent observed in June. Moreover, credit to this sub sector declined by 67.1 per cent on an annual basis, a fall which was similar to the shrinkage registered at the end of June.

## **Sectoral Distribution of Credit to Business Enterprises and Statutory Bodies**

The analysis of sectoral distribution of credit is carried out in order to measure the degree to which finance penetrated the economy to support various economic activities. The analysis helps to gauge the extent of financial deepening in the economy. Total credit distributed to all business-oriented sectors of the economy, including official entities, but excluding non-performing loans, increased by 22.6 per cent in September converse to a decrease of 4.1 per cent reported in June. The rise in total credit during the quarter under review was mainly due to an upward trend in credit extended to the manufacturing, distributive services and other development sub sectors.

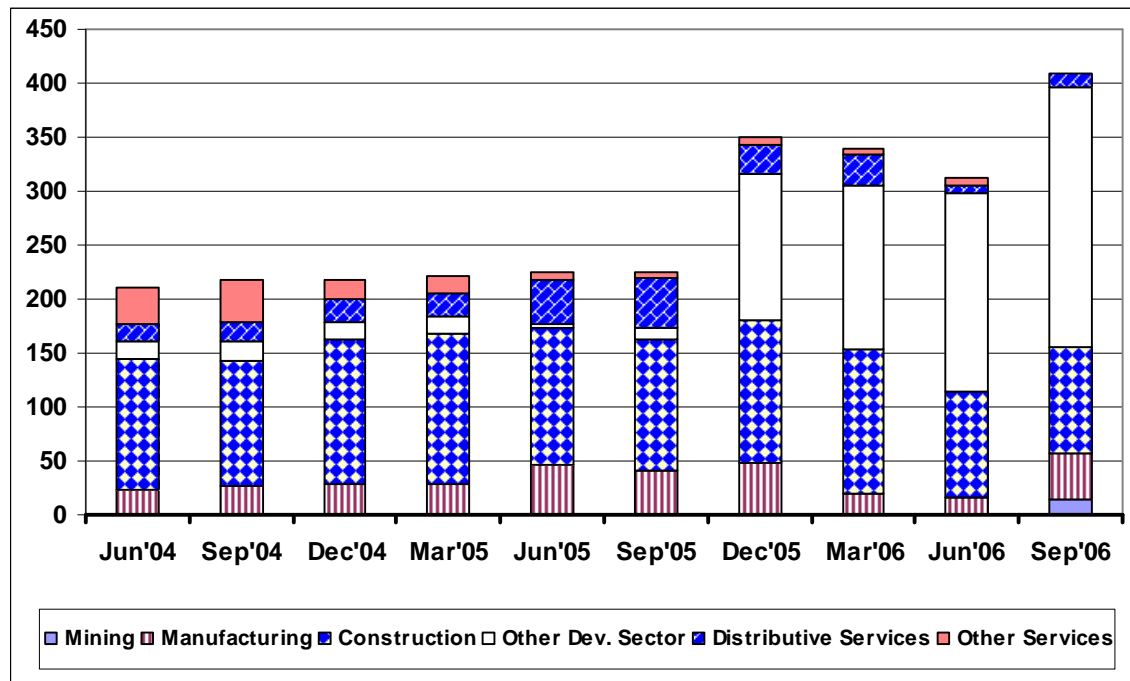
Credit allocated to other development sectors (made up of wholesale agriculture, hunting, storage, electricity, transport and communication) increased by 31.1 per cent in September following a rise of 38.2 per cent in June. The manufacturing sub sector saw an increase of 182.1 per cent in credit while the distributive services sub sector realised an increase of 79.4 per cent in credit receipts during the quarter ended September.

**Table 18: Sectoral Distribution of Credit to Enterprises**

(Million Maloti; End of period)

SECTOR	2005				2006	
	Jun	Sep	Dec	Mar	Jun	Sep
Mining	0.0	0.0	0.0	0.0	13.5	3.0
Manufacturing	46.0	41.3	47.8	20.4	15.6	44.0
Construction	126.8	121.0	132.6	133.3	99.1	97.8
Other development sectors	4.9	10.7	135.2	151.5	184.2	241.5
Distributive services	42.2	46.5	27.5	16.1	6.7	12.0
Other services	6.0	6.1	6.9	18.4	6.6	0.9
All sectors	225.9	225.7	350.0	339.6	325.8	399.3

**Figure 9: Sectoral Distribution of Credit to Business Enterprises**  
(Million Maloti: End of Period)



### Net Claims on Government

The banking system's net claims on Government continued to decline by 8.7 per cent during the quarter ended September, following a slump of 25.0 per cent noted at the end of June. The decrease was mainly driven by a build-up in government deposits with the Central Bank during the review quarter, reflecting a good fiscal position. As a result, net claims on Government by the Central Bank fell by 16.9 per cent (see the table below). It overtook a fall of 61.9 per cent in commercial banks' net claims on Government during the same period.

**Table 19: Banking System's Net Claims on Government**

(Million Maloti; End of Period)

Holder	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
<b>Commercial banks</b>	376.1	314.9	289.8	327.0	232.7	376.8
Claims on Government	453.2	455.2	461.6	491.1	404.5	487.4
<i>o/w MP T Bills</i> <sup>(3)</sup>	374.8	386.2	359.9	420.7	334.5	417.6
Less Government deposits	77.1	140.4	171.9	164.1	171.7	110.6
<b>Central Bank of Lesotho</b>	-1193.3	-1179.8	-1199.9	-1354.2	-1516.7	-1773.
Claims on Government <sup>(4)</sup>	237.6	226.3	222.2	237.7	257.0	282.1
Less Government deposits	1430.9	1406.2	1422.0	1591.9	1773.7	2055.0
<i>o/w those in blocked acct.</i>	478.72	484.2	519.6	487.7	490.7	493.7
<b>TOTAL NET CLAIMS</b>	-817.2	-865.0	-910.1	-1027.2	-1284.0	-1396.2

(3) – 'o/w' means of which and 'MP T Bills' means monetary policy treasury bills

(4) – IMF loans on-lent to the GOL

**Net Foreign Assets**

The net foreign assets (NFA) of the overall banking system rose by 16.9 per cent in September compared with a 16.0 per cent rise recorded in June. The surge mainly reflected a rise in both the NFA of the Central Bank and commercial banks. The commercial banks' net foreign assets increased by 17.4 per cent reflecting their transfers abroad for alternative investment options. Moreover, the Central Bank's net foreign assets grew as a result of the recapitalization of increased bond coupon payments and revaluation gains observed during the review period.

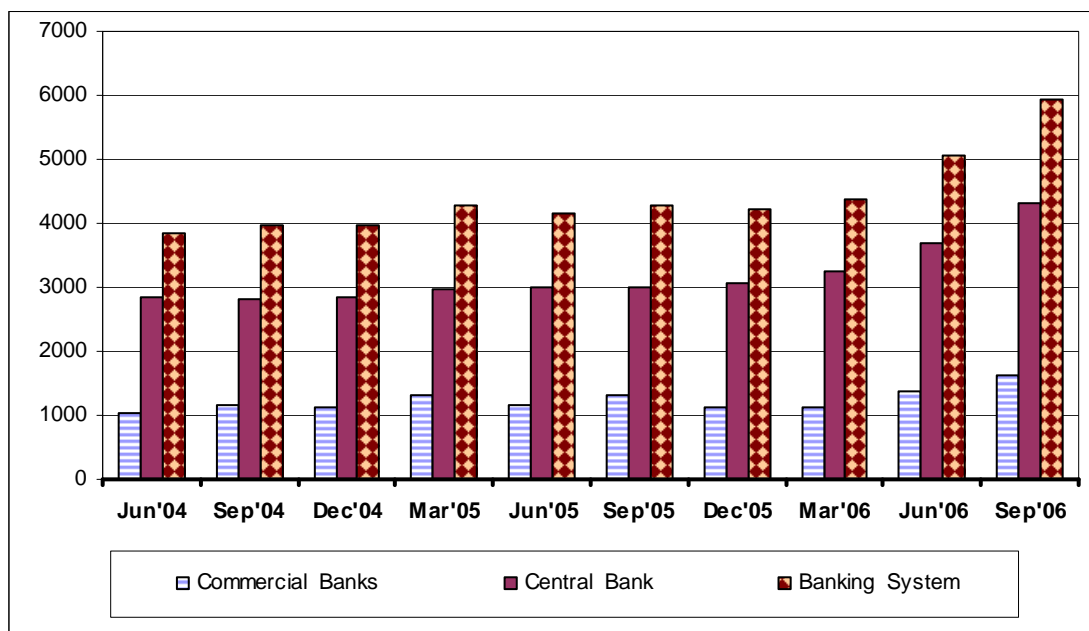
**Table 20: Banking System's Foreign Assets and Liabilities**

(Million Maloti; End of Period)

Holder	2005				2006	
	Jun	Sep	Dec	Mar	Jun	Sep
<b>A. Commercial Banks</b>	1150.2	1310.3	1135.0	1139.0	1375.2	1614.6
Foreign Assets	1274.3	1388.6	1241.8	1248.1	1500.5	1683.1
Foreign Liabilities	-124.1	-78.3	-106.9	-109.1	-125.4	-68.6
<b>B. Central Bank of Lesotho</b>	3000.9	2985.5	3076.2	3238.4	3700.5	4319.9
Foreign Assets	3566.0	3539.3	3625.6	3803.3	4244.4	4885.9
Foreign Liabilities	-565.1	-553.8	-549.3	-564.9	-543.9	-566.0
<b>NET TOTAL</b>	4151.0	4295.8	4211.2	4377.4	5075.7	5934.4

**Figure 10: Net Foreign Assets**

(Million Maloti; End of Period)



## **VIII. Money and Capital Markets**

### **Money Market Developments**

A total of five treasury bill auctions were conducted during the quarter under review. They comprised three 91-day and two 182-day treasury bill auctions. The former were offered for monetary policy purposes while the latter were targeted at encouraging investment by the general public. The total stock of securities for the quarter under review amounted to M544.7 million. This value represented a slight fall from M545.8 million which was offered during the quarter ended in June.

During the quarter ended September, the holders of securities composed of commercial banks, Non-Bank Financial Institutions (NBFI's), and other institutions. The banking sector continued to dominate the market by holding more securities than the NBFIs. The share of the banking sector rose from 61.3 per cent of the total in June to 77.7 per cent in September. At the same time the share of the NBFIs declined from 28.5 per cent in June to 12.1 per cent in September. The general public held 10.2 per cent share in September compared with 9.3 per cent recorded in June.

**Table 21: Holdings of Treasury Bills** <sup>(5)</sup>

(Million Maloti)

Holders Type	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
<b>Total</b>	<b>489.5</b>	<b>534.7</b>	<b>530.2</b>	<b>530.2</b>	<b>545.8</b>	<b>544.7</b>
<b>Banking System</b>	374.8	386.2	359.9	425.8	339.6	423.2
Central Bank	0.0	0.0	0.0	5.1	5.1	4.9
Commercial Banks	374.8	386.2	359.9	420.7	334.5	418.3
<b>Non-Bank Sector</b>	114.7	148.6	170.3	104.4	206.2	121.5
NBFIs	77.3	89.8	108.3	49.6	155.3	66.0
Others	37.4	58.8	62.0	54.8	50.9	55.5
<b>Memorandum Item</b>						
Average Yield per cent	7.25	7.21	7.27	7.10	7.04	7.16

(5) – Figures at face value

**Money Market and Short-term Interest Rates**

Although the margin between the Lesotho 91-day treasury bill rate and its SA counterpart is still within the guideline range, it is continuing to widen (see Table 22). The Lesotho 91-day treasury bill rate declined from 6.90 per cent in June to 6.86 per cent in September contrary to its SA counterpart which rose from 6.83 per cent to 8.00 per cent in June and September, respectively. The Lesotho rate was lower than the South African rate by 114 basis points in September, while it was higher by seven basis points in June.

The prime lending rate in the country increased from 12.0 per cent in June, to 12.33 per cent in September, in line with regional trends. The average deposit rates also followed the upward trend. As a result, the spread between lending and deposit rates narrowed from 7.55 per cent to 6.33 per cent. Nevertheless, at the end of September, the real interest rate on one-year deposits (adjusted for inflation) was still negative at 0.8 per cent. This simply meant that the return on deposits was still not sufficient to preserve depositors' purchasing power.

**Table 22: Major Money Market Interest Rates**

(Per cent; End of Period)

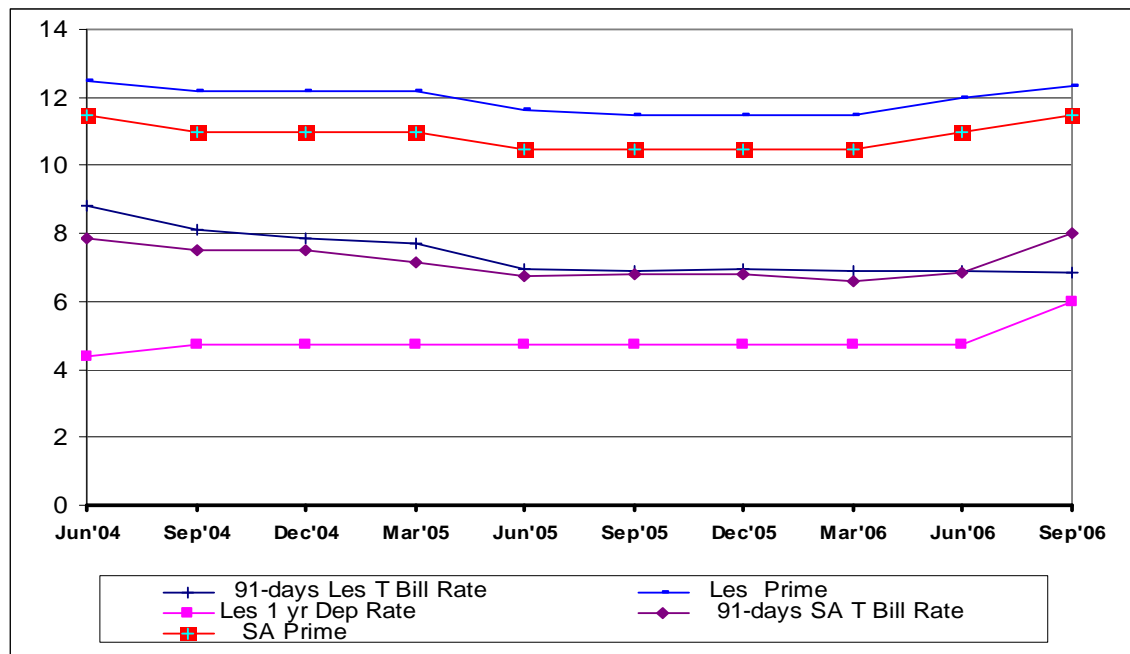
Interest Rates by Type	2005			2006		
	Jun	Sep	Dec	Mar	Jun	Sep
Central Bank T Bill Rate – 91 Days	6.93	6.89	6.95	6.90	6.90	6.86
Lombard Rate	13.00	13.00	13.00	10.40	10.40	10.36
Commercial Banks <sup>(6)</sup>						
Call	2.83	2.83	2.83	2.83	3.50	4.10
Time:						
31 days	3.50	3.50	3.50	3.50	3.50	3.50
88 days	4.25	4.25	4.25	4.25	4.25	5.5
6 months	4.50	4.50	4.50	4.50	4.50	5.8
1 year	4.75	4.75	4.75	4.75	4.75	6.0
Savings	2.00	2.00	2.00	2.00	2.00	2.96
Prime	11.50	11.50	11.50	11.50	12.00	12.33
South Africa*						
Repo	7.00	7.00	7.00	7.00	7.00	8.00
T Bill Rate – 91 Days	6.76	6.79	6.80	6.59	6.83	8.00
Marginal Lending Rate	12.00	12.00	12.00	12.00	12.50	13.00
Prime	10.50	10.50	10.50	10.50	11.00	11.5

\* Figures for South Africa were obtained from the SARB

(6) - Average rates by commercial banks



**Figure 3: Short-Term Interest Rates**  
(Per Cent Per Annum)



### Foreign Exchange Rates

The loti continued to show some weakness during the third quarter of 2006. On average, the loti depreciated by 10.6 per cent against the US dollar. The depreciation of the local currency was driven mainly by the strength of the US dollar and other major currencies. The US dollar continued to remain strong despite the growing concern of the US economic slowdown. Measured against other currencies, the loti depreciated 12.9, 11.8, and 12.6 per cent against the SDR, euro and pound sterling, respectively.

The depreciation of the local currency has some implications for the economy of Lesotho. On the one hand, the weakness of loti could mitigate the pressure on the trade balance by encouraging exports and limiting imports. The depreciation improves the price competitiveness of the country's exports in the international markets. On the other hand, the depreciation poses a threat to the level of inflation in the country.

**Table 23: Selected Exchange Rates**

(Loti per Foreign Currency units: Quarterly Averages)

Currency	2005				2006	
	Jun	Sep	Dec	Mar	Jun	Sep
SDR	9.584	9.512	9.398	8.871	9.537	10.601
EURO	8.077	7.937	7.772	7.403	8.127	9.118
USD	6.425	6.510	6.538	6.157	6.473	7.185
POUND STERLING	11.909	11.611	11.427	10.789	11.814	13.414

**IX. Government Finance****Summary of Budget Outturn**

Government budgetary operations were estimated to have resulted in a surplus equivalent to 6.2 per cent of GDP. This was facilitated by Government efforts to contain recurrent expenditure at a minimum level, coupled with improved collections of revenue during the review period.

Overall Government expenditure and net lending registered a 6.1 per cent growth. As a percentage of total expenditure, capital expenditure, on the one hand, rose to 19.2 per cent compared with 11.9 per cent recorded in the previous quarter. Recurrent expenditure, on the other hand, dropped to 80.8 per cent. This development reflected the general improvements in the implementation of development projects during the reporting period.

**Revenue**

During the period under review, Government revenue including grants grew by 2.0 per cent. This was mainly attributed to a rise in Non-customs revenue, which increased by 2.8 per cent. As a percentage of GDP, total revenue and grants grew by a 100 basis points to 52.3 per cent, during the period under review.

Tax revenue grew marginally by 1.0 per cent from the previous period. This was largely on account of the increase in non-customs tax revenue, as earlier mentioned. The increase benefited from the 7.5 per cent growth in income tax revenue following a hike in personal income tax. Conversely, taxes on goods and services dropped by 5.3 per cent, during the period under review. This was mainly attributed to the fall in collections from value added tax (VAT) and the oil levy. The fall in VAT collections mainly reflected the level of economic activities during the review quarter.

SACU receipts are dependent on the level of intra SACU trade, excise duties, and domestic economic developments. SACU receipts constituted 63.2 per cent of total tax receipts during the review period. Income tax and VAT constituted 20.6 per cent and 15.1 per cent respectively, of tax revenue.

Non-tax revenue improved by 2.6 per cent during the period under review. This was influenced by receipts of water royalties which strengthened by 22.0 per cent. This period also showed some improvements in implementation of Government development projects. This was supported by the increase in disbursements of development grants, which more than doubled during the third quarter of 2006.

**Table 24: Government Budgetary Operations**

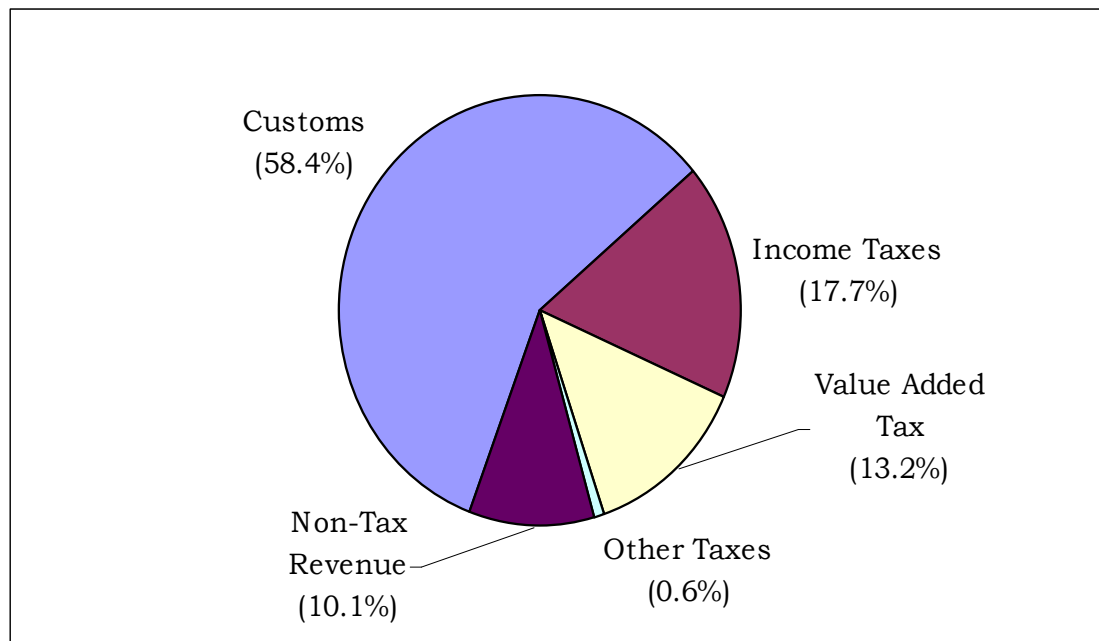
(Million Maloti)

	2005/06			2006/07	
	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun Revised	Jul-Sept * Preliminary
<b>Total Revenue and Grants</b>	<b>1174.6</b>	<b>1139.2</b>	<b>1222.5</b>	<b>1352.7</b>	<b>1380.1</b>
<b>Total Revenue</b>	1140.1	1130.9	1217.7	1344.3	1360.1
<i>Tax Revenue</i>	1024.8	1025.5	1049.9	1209.9	1222.2
Customs	603.3	603.3	603.3	772.3	772.3
Non-customs	421.4	422.1	446.6	437.6	449.9
Income Taxes	227.6	229.6	240.1	234.0	251.6
Taxes on goods & services	172.7	188.0	194.7	194.6	184.3
Other Taxes	21.1	4.6	11.8	9.0	14.0
<i>Non-Tax Revenue</i>	115.3	105.5	167.7	134.3	137.9
Of which: Water royalties	66.5	63.6	62.0	58.1	70.9
<b>Grants</b>	<b>34.5</b>	<b>8.2</b>	<b>4.9</b>	<b>8.4</b>	<b>20.0</b>
<b>Total Expenditure &amp; Net Lending</b>	<b>1015.4</b>	<b>1137.5</b>	<b>1077.3</b>	<b>1128.4</b>	<b>1217.2</b>
<b>Recurrent Expenditure</b>	835.9	951.8	941.7	987.3	967.2
Personnel Emoluments	313.1	318.7	321.4	340.6	341.9
Interest Payments	40.2	131.5	23.3	26.6	22.7
Foreign	22.5	120.4	10.7	16.3	10.0
Domestic	17.7	11.1	12.6	10.3	12.7
Other Expenditure	482.6	501.7	596.9	620.1	602.6
<b>Capital Expenditure</b>	179.6	189.0	138.9	141.2	252.4
<b>Net Lending</b>	0.0	-3.4	-3.3	0.0	-2.5
<b>Surplus/deficit before grants</b>	124.6	-6.5	140.4	215.8	142.9
<b>Surplus/deficit after grants</b>	159.2	1.7	145.2	224.2	162.9
<b>Financing</b>	-159.2	-1.7	-145.2	-224.2	-162.9
Foreign	-143.0	-33.9	-22.8	-67.3	33.6
Loan drawings	38.6	28.1	9.6	15.8	72.5
Amortization	-181.6	-62.0	-32.4	-83.1	-38.9
Domestic	-16.2	32.2	-122.4	-156.9	-196.5
Bank Financing	-47.8	-45.1	-117.1	-256.8	-112.2
Non – Bank	31.6	77.3	-5.3	99.8	-84.3

Source: Ministry of Finance and Development Planning (MoFDP)

\*CBL Preliminary Estimates

**Figure 12: Sources of Government Revenue**



### *Expenditure*

Total expenditure and net lending were estimated to have increased by 6.1 per cent during the review period. The increase was largely on account of the rise in gross fixed capital formation. As a percentage of GDP, total expenditure stood at 46.2 per cent.

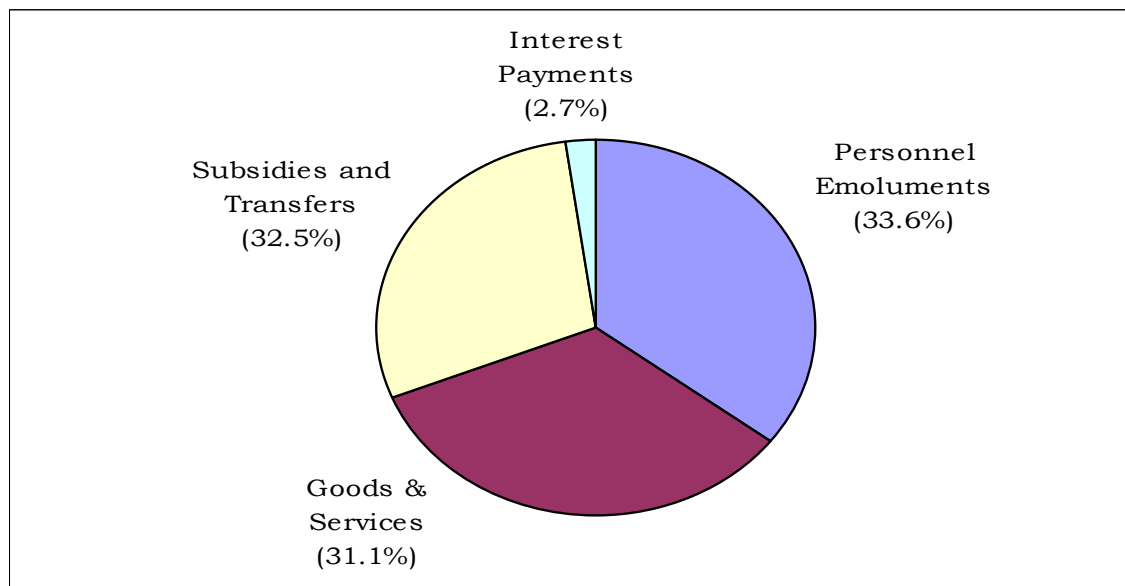
Recurrent expenditure dropped by 2.0 per cent during the third quarter of 2006. The decrease mainly reflected the 8.8 per cent fall in expenditure on purchases of goods and services. Personnel emoluments expenditure almost maintained the same level as in the previous period, while interest payments dropped by 14.8 per cent.

The fall in recurrent expenditure was moderated by the opposite movement in subsidies and transfers. The level of subsidies and transfers extended during the review period increased by 5.4 per cent. This was mainly driven by transfers to government agencies, plus payments of scholarships at tertiary level.

Implementation of development projects showed some improvement during the period under review. Expenditure on gross fixed capital formation was estimated to have soared by 64.7 per cent on a quarterly basis. This was attributed to, among others, the construction of roads

that network the lowlands with the eastern highlands, construction of primary schools to meet the demand of free primary education, improvement of water supply reticulation, and health sector reforms. This development was accompanied by an equivalent increase in public external indebtedness. Nonetheless, Government continued to be a dominant financier of development projects. About 58.6 per cent of this expenditure category was financed from own resources, while loans and grants financed 32.7 per cent and 8.7 per cent, respectively.

**Figure 4: Recurrent Expenditure by Type & Percentage Share**



### **Financing**

As earlier indicated, government budgetary operations during the review period were estimated to have resulted in a surplus equivalent to 6.2 per cent of GDP. The surplus enabled Government to reduce domestic indebtedness to the non-banking sector, and accumulate deposits with the banking sector. This has also facilitated the build-up in net international reserves, and hence, import cover, as discussed under balance of payments.

## **Public Debt**

### Overview

Total public debt climbed 14.5 per cent during the period under review. The growth was a result of the increase in external debt following improvement in implementation of development projects, along with the depreciation of the local currency against the major currencies with which debt is contracted. As a ratio of GDP, total debt stock was estimated to have increased to 50.8 per cent. External debt continued to account for the larger share of total debt stock during the review period. It registered approximately 87.8 per cent of total Government debt, while domestic debt accounted for the remaining 12.2 per cent.

### External debt

The level of external debt escalated by 17.1 per cent during the third quarter. The hike was mainly at the back of an improvement in loan disbursements destined to finance development projects. As a result, both concessional and non-concessional debt increased by 16.6 per cent and 22.5 per cent respectively. The hike was also accelerated by the depreciation of the local currency against major currencies. External debt maintained 87.8 per cent of total public debt stock. About 83.8 per cent of external debt was concessional. This was in line with Government policy to borrow on concessional terms in order to moderate the country's future debt burden.

The concessional nature of public debt stock continued to enable the country to retain a favourable position during the review period. Contrasted with the decrease observed in the previous period, the ratio of foreign debt to GDP jumped by 650 basis points to 44.6 per cent. At this level, the debt to GDP ratio was below the 60 per cent sustainability threshold for Highly Indebted Poor Countries (HIPC). As a ratio of exports of goods and services, debt service was recorded at 1.7 per cent, compared with the 15.0 per cent threshold. This position mainly benefited from the long maturity structure and concessionality of the overall external debt stock.

**Table 25: Outstanding Government Debt**

(Million Maloti)

	2005			2006		
	QII	QIII	QIV	QI	QII	QIII
<b>A. EXTERNAL DEBT</b>	<b>4379.4</b>	<b>4105.6</b>	<b>4011.6</b>	<b>3932.6</b>	<b>4013.9</b>	<b>4699.9</b>
<b>Bilateral Loans</b>	<b>422.0</b>	<b>408.6</b>	<b>396.9</b>	<b>408.5</b>	<b>383.2</b>	<b>385.4</b>
Concessional	381.6	375.9	369.9	386.2	381.5	322.3
Non-concessional	40.4	32.7	27.1	22.3	1.7	63.0
Multilateral Loans	3581.6	3484.6	3399.1	3334.4	3443.8	4129.2
Concessional	3125.0	3037.4	2985.9	2939.3	2992.4	3612.8
Non-concessional	456.6	447.2	413.2	395.1	451.4	516.3
Financial Institutions	306.7	147.9	141.5	117.2	113.1	113.6
Concessional	2.7	2.6	2.6	2.4	2.4	2.4
Non-concessional	304.0	145.4	138.9	114.8	110.7	111.1
Suppliers' Credit	69.1	64.4	74.1	72.5	73.8	71.8
<b>B. DOMESTIC DEBT</b>	<b>604.2</b>	<b>649.3</b>	<b>644.9</b>	<b>644.9</b>	<b>661.0</b>	<b>654.5</b>
Banks	489.5	500.9	474.6	540.4	454.7	533.0
Long-term	114.7	114.7	114.7	114.7	114.7	114.7
Short-term	374.8	386.2	359.9	425.7	340.0	418.3
Of which: treasury bills	374.8	386.2	359.9	425.7	339.6	418.3
Non-bank	114.7	148.5	170.3	104.4	206.3	121.5
Short-term (TBs)	114.7	148.5	170.3	104.4	206.3	121.5
<b>TOTAL (A + B)</b>	<b>4983.6</b>	<b>4754.9</b>	<b>4656.5</b>	<b>4577.5</b>	<b>4674.9</b>	<b>5354.4</b>

**N.B:** External debt figures are from MoFDP

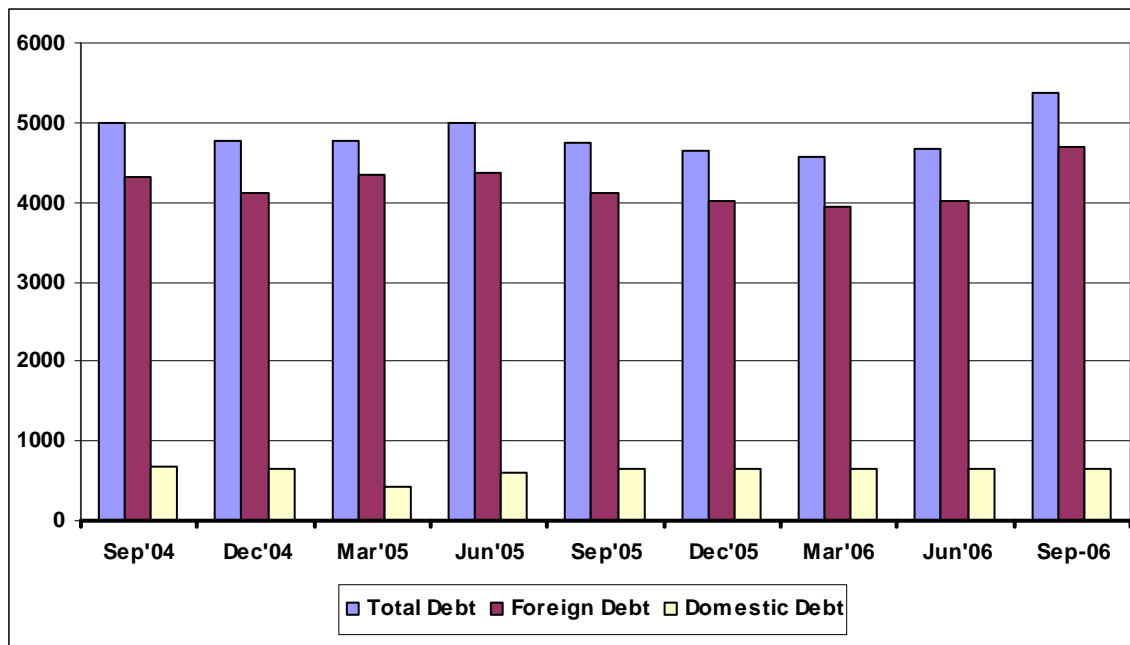
## Domestic Debt

Domestic debt marginally dropped by 1.0 per cent during the period under review. The fall was largely due to the decrease in holding of short term debt by the non-banking sector. Short term debt declined by 1.2 per cent, while long term debt maintained the level recorded in the previous



quarter. The long term component is made entirely of the ten year bond<sup>4</sup> that matures in 2009. As a percentage of GDP, domestic debt slightly dropped to 6.2 per cent during the period under review and it constituted 12.2 per cent of total public debt. Short-term debt continued to consist entirely of treasury bills, which were issued for monetary policy operations.

**Figure 5: Outstanding Public Debt**  
(Million Maloti: End of Period)



<sup>4</sup>This bond had been issued to finance the restructuring of the old Lesotho Bank in 1999.