Lesotho Economic Outlook 2023 - 2025
An Update

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Despite Heightened Construction Activity Subpar Performance Persists

Overview

The near-term economic growth forecast has been revised down reflecting declining activity in the manufacturing industry. The domestic economy is now projected to grow by 1.8 per cent in 2023 and average 2.4 per cent over 2024-2025. Construction activity and associated knock-on effects onto the service industry are expected to continue to shape growth in the medium-term. In addition, mining industry is expected to provide additional support to growth as it proves resilient against falling global diamond prices. However, weakness in manufacturing and agricultural industries is expected to weigh on growth. Inflation is now projected to average 6.2 per cent in 2023, reflecting still high food prices despite recent moderation. It is projected to gradually moderate to 5.4 per cent in 2024 and stabilize around 4.9 per cent in 2025.

The fiscal position is expected to improve in the medium-term, on account of higher SACU revenue and modest growth in domestic tax revenue. The fiscal position is projected to move from a marginal deficit in 2023 to surpluses in 2023-2024. The fiscal deficit will be finance by both domestic and foreign borrowing while the surpluses will lead to accumulation of government deposits with the banking sector.

The current account deficit has been revised downwards to 6.4 per cent (from 5.5 per cent) of GDP in 2023 but remain relatively unchanged at 6.3 per cent of GDP in 2024 and 7.7 per cent of GDP in 2025. Downward revision in 2023 reflects the weaker manufacturing exports. The expected high imports of goods and services related to the LHWP II project are expected to continue to drive the current account. Most of the current account deficit will be financed through capital transfers associated with the LHWP II.

Private sector credit is projected to rise by a revised 10.7 per cent in 2023 consistent with the growth in nominal GDP and slow down to an average growth of 4.9 per cent in 2024-2025. The upward revision of credit growth in 2023 is due increased uptake of credit by households, which is expected to continue to drive private sector credit growth. Despite the projected growth in key sectors in the medium-term, credit extended to businesses is projected to remain stagnant. The muted business credit is due to financing of the economy through non-banking sources.

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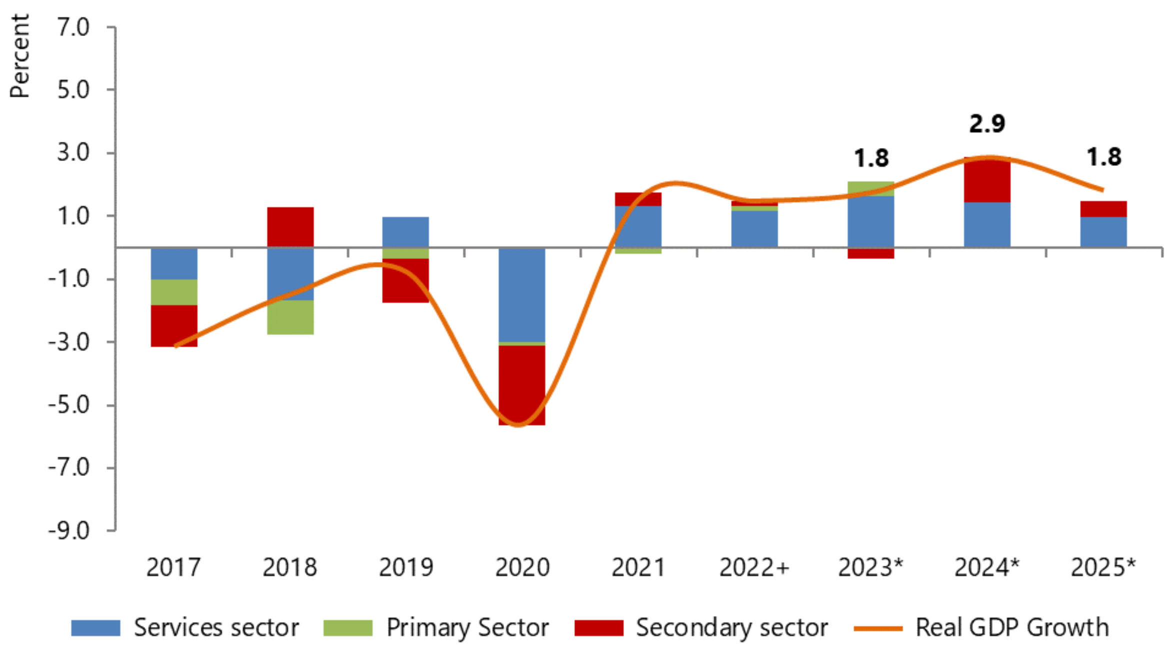
1. Real Sector Outlook

Lesotho's near-term growth has been downgraded as challenges in the manufacturing industry outweigh resilience in the mining industry. The high frequency indicators in the textile and clothing industry point to declining orders from the US market. The declining orders are due to a combination of high material and inputs costs and pre-existing structural factors that are rendering the industry less competitive. Meanwhile, the mining industry was somewhat resilient as some mines experienced increases in the price per carat in the first half of 2023; despite the generally decreasing prices in the global diamond market. Thus, Lesotho's GDP is now projected to grow by a revised 1.8 per cent (from 2.0 per cent in June) in 2023. In 2024, GDP growth is projected to pick up to 2.9 per cent and slow down to 1.8 per cent in 2025. Both 2024 and 2025 growth projections are revised up by 0.1 percentage points. The second phase of the Lesotho Highlands Water Project (LHWP II) and related knock-on effects continue to drive the projected growth trajectory.

GDP growth in 2023 is revised down by 0.2 percentage points...

Figure 1: Domestic Economic Outlook



*Source: CBL, + Estimates, * Projections*

Mining industry is expected to drive primary sector growth in the medium-term, while adverse weather effects continue to hinder agricultural production. The mining industry is projected to grow by an upwardly revised 11.5 per cent in 2023, and slow down to average 3.2 per cent in 2024-2025. The projected mining industry growth is supported by better-than-expected comeback by Liqhobong mine following an extended period on care and maintenance. Additional boost is expected to come from the relatively favourable diamond prices for some mines despite the downward trend in prices in the global diamond market. Within the agricultural sub-sector, crop production is projected to contract in both 2023 and 2024 before recovering in 2025. The projected declines in crop output are due to adverse weather effects, particularly the anticipated dry weather conditions throughout the 2023 planting season.

The secondary sector is projected to contract by 1.7 per cent in 2023 following a downward revision in the textile and clothing industry growth projection. The clothing and textile industry is now projected to contract by 7.4 per cent (previously -2.8 per cent) in 2023. The industry's growth downgrade reflects significantly lower-than-expected output in the first half of 2023. Lesotho's textile orders from the US continue to decline due to high material and input costs. The recent developments have exacerbated structural challenges facing the industry making it less competitive and leading to mass job losses. The textile and clothing exports to the US dropped by 59.2 per cent between January and July in 2023, relative to the same period in 2022. In 2024-2025, the secondary sector is projected to rebound by 5.0 per cent, driven by the strong growth in the construction industry. The LHWP II is expected to reach its peak in 2024-2025, boosting the construction industry output. Consequently, the construction industry is projected to grow by 17.0 per cent over 2024-2025.

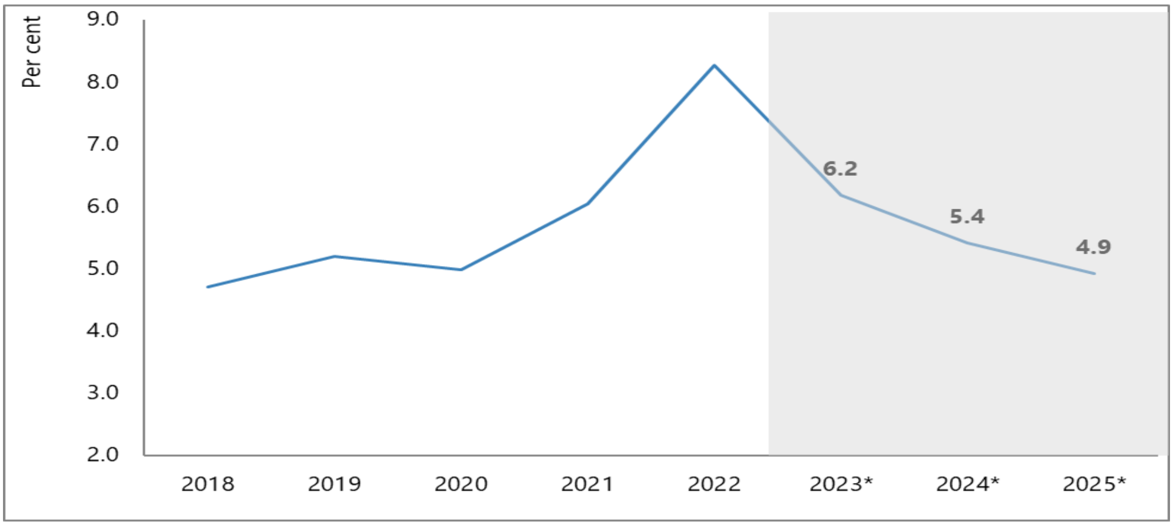
Lesotho's textile orders from the US continue to decline...

The services sector is projected to grow by a revised 2.4 per cent in 2023 and average an unchanged 1.5 per cent growth in 2024-2025. The sector's growth has been revised up by 0.4 percentage points in 2023 reflective of expected modest pick-up in consumer spending following higher household credit growth in the first half of 2023 and faster moderation in inflation. Overall, the sector is expected to be largely supported by the positive knock-on effects from the LHWP II activities over its implementation cycle. Additional boost is expected to come from improvement in real incomes in line with the projected inflation trajectory in the medium-term.

Domestic inflationary pressures have moderated faster than expected, with inflation outcomes reaching their lowest in three years in July 2023. Therefore, annual inflation rate is now projected to average 6.2 per cent in 2023 (0.5 percentage points lower) and gradually moderate to 5.4 per cent in 2024 and stabilize around 4.9 per cent in 2025. Falling imported food and energy prices are behind the faster moderation in inflation. Global food prices are moderating due to record-level production of grains. Despite the moderation, domestic food prices remain high. Moreover, dry weather conditions that are forecasted to coincide with the summer cropping season present upside risks to the inflation projections.

Despite recent moderation, domestic food prices remain high...

Figure 2: Inflation Outlook

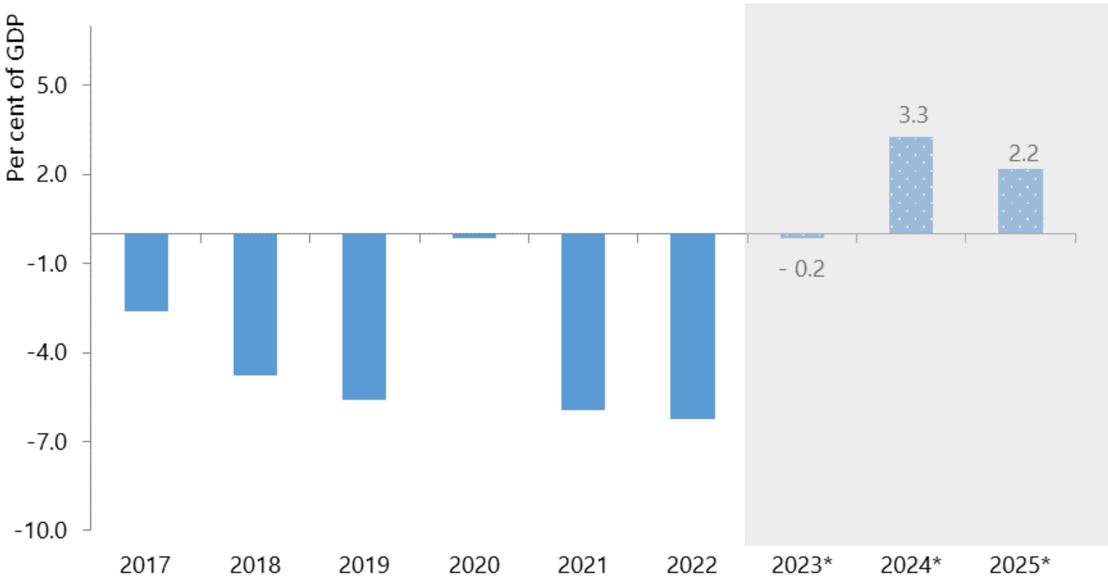


2. Public Sector Outlook

The fiscal position is relatively unchanged from June projections. The fiscal balance is projected to move from a marginal deficit in 2023 into the surplus territory in 2024-2025. In 2023, the fiscal balance is expected to record an unchanged deficit of 0.2 per cent of GDP as expenditures marginally outpace revenues. Fiscal position is expected to improve and register surpluses equivalent to 3.3 per cent and 2.2 per cent in 2024 and 2025, respectively. The expected improvement in the fiscal deficit reflects marked increases in revenue against modest increases in expenditure. Particularly, SACU revenue is projected to increase by 27.5 per cent in over 2023-2025 while tax revenue is projected to increase by 7.6 per cent over the same period. SACU revenues are expected to be boosted by higher trade flows. Meanwhile, expenditures are projected to increase by 8.6 per cent over 2023-2025, driven mainly by recurrent expenditures.

Fiscal position is expected to improve and register surpluses...

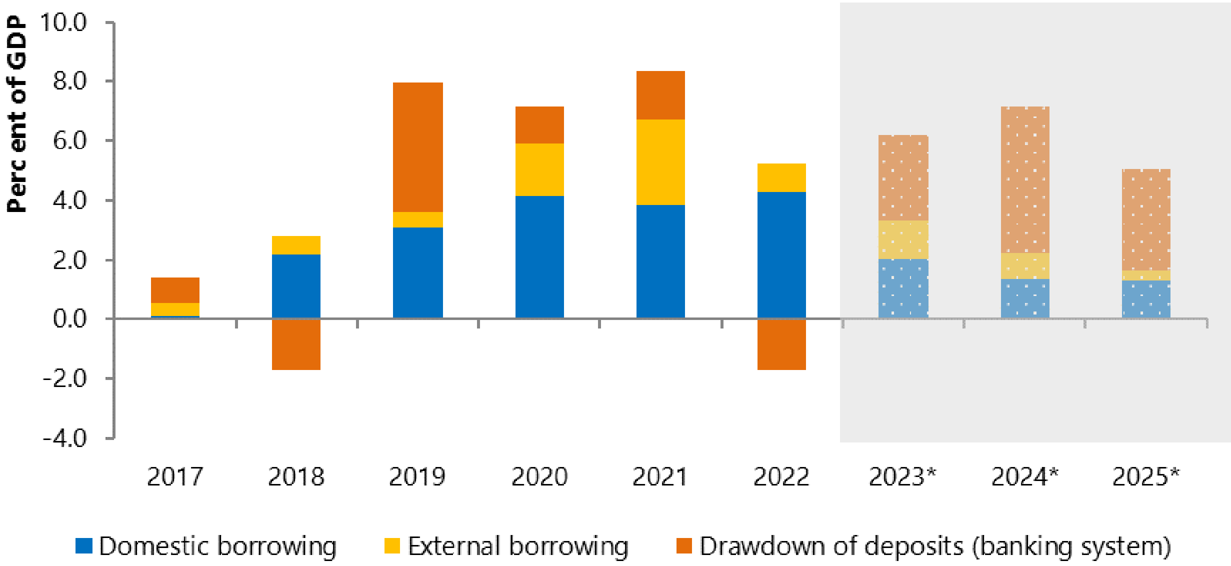
Figure 3: Fiscal Balance Outlook



*Source: CBL, + Estimates, * Projections*

The projected fiscal deficit in 2023 will be financed through domestic and foreign borrowing. Domestic borrowing will account for 1.6 per cent of GDP as government continues to issue securities to develop the domestic capital market over the medium-term. Foreign borrowing is expected to account for 0.9 per cent of GDP. Given the expected fiscal surpluses, government deposits with the banking sector are expected to rise by 3.7 per cent as percentage of GDP.

Figure 3A: Fiscal Financing



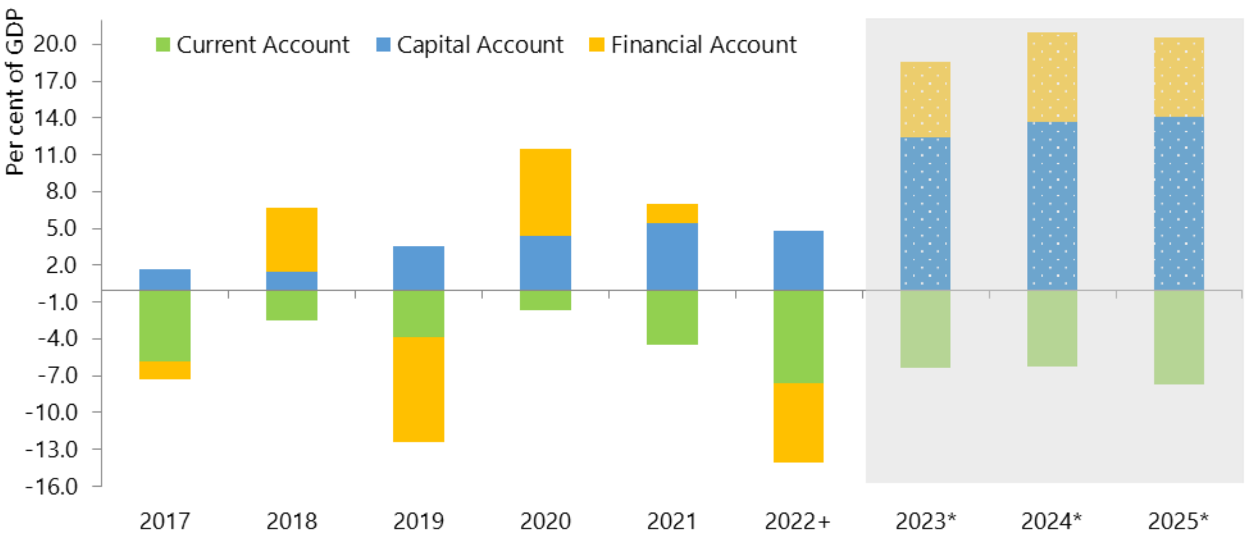
*Source: CBL, + Estimates, * Projections*

3. External Sector

The external sector projections show that the current account is expected to widen in the coming years. The forecasts indicate that in 2023 the current account deficit as a percentage of GDP will be at 6.4 per cent of and 6.3 per cent in 2024, before expanding to 7.7 per cent in 2025. The 2023 projections have been revised upwards by 0.9 percentage points relative to June 2023 LEO. The revision was mainly due to downward revisions in diamonds and textiles earnings by 7.9 and 3.6 percentage points, respectively. The mining industry has mostly seen recovery of low-value diamonds in the first half of the year. With regard to textiles exports, the challenges of decreased demand for Lesotho's imports and closure of several firms in the textiles and clothing industry are expected to negatively affect export earnings in the near-term. The external sector developments continue to show the need for the country to promote export-oriented industries as well as diversify the export base.

Diamond and textile export earnings revised down…

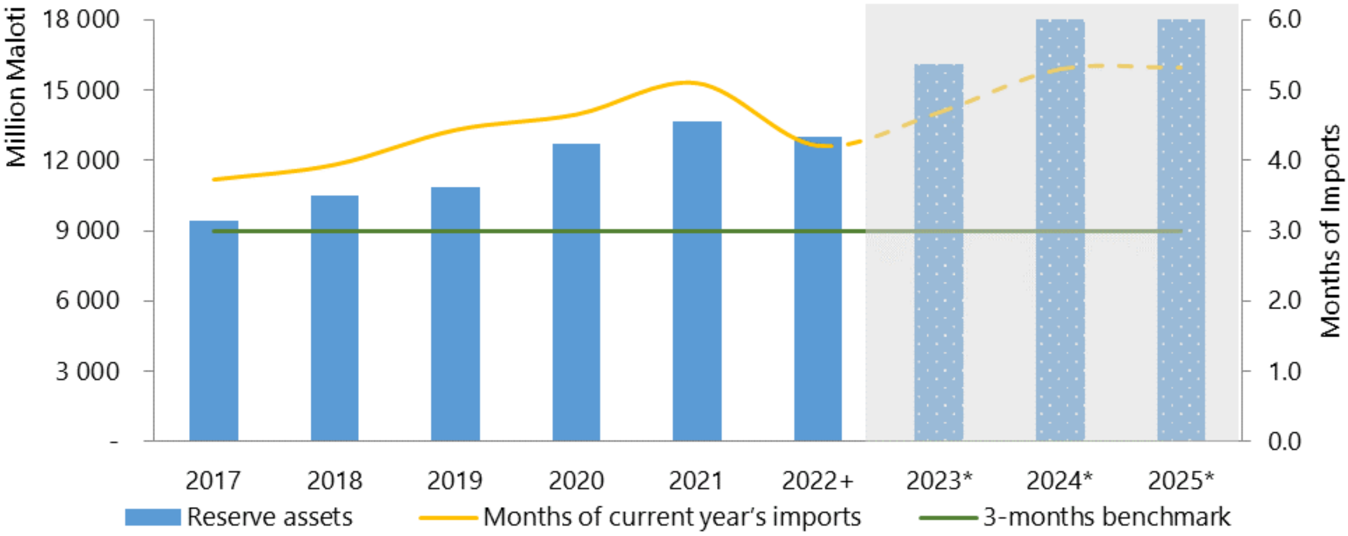
Figure 4: The External Sector



*Source: CBL, + Estimates, * Projections*

The capital and financial account balances are expected to remain in surplus during the forecast period. The capital account is expected to register surpluses equivalent to 12.5 per cent of GDP in 2023 and increase to an average of 13.9 per cent during 2024-2025. During the first half of 2023, capital inflows increased substantially as they more than tripled compared to the first half of 2022. The inflows were to finance the activities of the LHWP II which include construction of the Polihali dam, the Senqu Bridge and other smaller bridges, the transfer tunnel and access roads. More capital inflows related to the same project are expected to come during the forecast period. The financial account is projected to register net outflows equivalent to 6.7 per cent of GDP in 2023 and increase to an average of 6.9 per cent of GDP over 2024-2025. Official reserves are estimated to accumulate and reach an equivalent of 4.7 months of import cover in 2023 and improve to 5.3 months of import cover both in 2024 and 2025. The increased SACU revenue is expected to boost accumulation of reserves during 2023-2025. However, the increase is likely to be moderated by growth in government expenditure.

Figure 5: Official Reserves Outlook



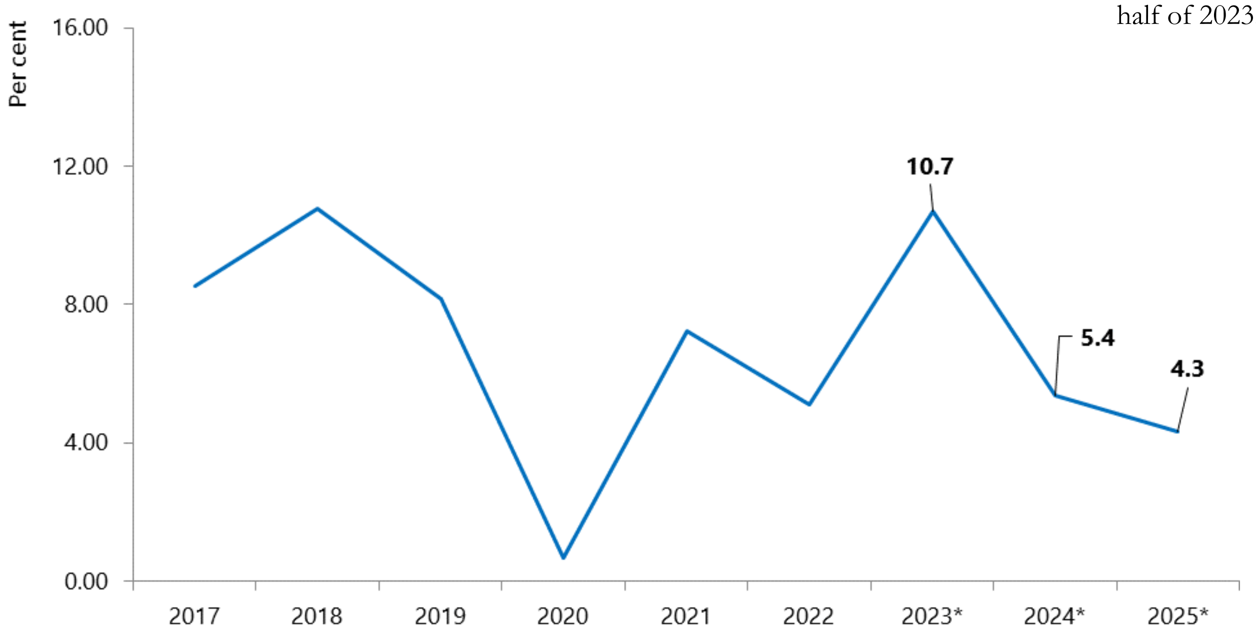
*Source: CBL, + Estimates, * Projections*

4. Money & Credit

Money supply and private sector credit are forecast to increase by an average of 8.3 per cent and 6.7 per cent, respectively in the medium-term. Increase in money supply reflects increases in both domestic and foreign assets. Growth in private sector credit has been revised up to 10.7 per cent due to increased uptake of credit by households in the first half of 2023. Private sector credit is expected to continue to be driven by households and grow by 4.9 per cent over 2024-2025. Nonetheless, credit extended to business remains subdued on the back underperforming economy and financing of the economy from non-banking sources.

There was increased uptake of credit by households in the first half of 2023...

Figure 6: Private sector credit growth



5. Risks to the Outlook

The balance of risks to the domestic outlook are tilted to the downside. Despite the recent moderation, inflation could remain high if some of the upside risks to inflation materialise. Global economic growth could come out weaker than projected, negatively affecting Lesotho's export-oriented industries.

The downward revision in the near-term economic growth forecast due to declining activity in the manufacturing industry poses a significant risk. A further deterioration in this sector could negatively impact economic growth and job opportunities.

Overreliance on construction activity to drive growth in the medium-term carries risks, as construction can be influenced by various factors, including project delays, funding issues, and changes in demand. This is further compounded by the uncertainty surrounding renewal of AGOA.

The disparity between credit growth for households and businesses is a risk. Stagnation in credit extended to businesses, despite expected growth in key sectors, may hinder business expansion and economic development.

6. Conclusion

The domestic economy is expected to underperform, held back by the recent crises in addition to structural challenges within key industries. The economy is forecast to grow by 1.8 per cent in 2023 driven by the construction and services industries, while manufacturing industry and agricultural sub-sector are projected to contract. In 2024 domestic growth is expected to increase to 2.9 per cent and slow down to 1.8 per cent in 2025. The medium-term growth is expected to be led by the LHWP II with the project reaching its peak in 2024/2025. The annual inflation rate is expected to average 6.2 per cent in 2023 and gradually moderate to 5.4 per cent and 4.9 per cent in 2024 and 2025, respectively.

Appendix A: Overview of Revisions to Forecasts

	Actual	Estimate	Sept 2022 projections			Differences from June 2022 projections		
	2021	2022+	2023*	2024*	2025*	2023*	2024*	2025*
Economic growth	**1.6**	**1.5**	**1.8**	**2.9**	**1.8**	**-0.2**	**0.1**	**0.1**
Primary Sector	**-2.2**	**2.0**	**5.9**	**0.2**	**4.2**	**1.3**	**0.8**	**0.5**
Agriculture	-16.0	2.7	1.4	-3.3	6.3	-0.1	1.3	1.0
Mining & Quarrying	22.8	1.2	11.5	4.3	2.1	3.1	0.1	0.0
Secondary Sector	**2.1**	**0.9**	**-1.7**	**7.3**	**2.6**	**-2.6**	**0.4**	**0.1**
Manufacturing	7.7	-6.4	-6.2	1.7	1.1	-4.1	0.4	0.2
Textiles & Clothing	11.4	-7.5	-7.5	1.6	1.3	-4.7	0.4	0.2
Building & Construction	9.8	24.5	13.0	27.6	6.5	0.6	0.0	0.1
Services Sector	**1.9**	**1.9**	**2.4**	**1.8**	**1.2**	**0.4**	**0.0**	**0.1**
Inflation rate (%)	**6.1**	8.3	**6.2**	**5.4**	**4.9**	**-0.5**	**0.0**	**-0.1**

Appendix B: Selected Macroeconomic Indicators

Appendix I: Selected Macroeconomic Indicators					Projections		
	2019	2020	2021	2022+	2023*	2024*	2025*
Output - Constant prices							
Gross Domestic Product (% p.a.)	-0.76	-5.62	1.56	1.49	1.76	2.88	1.83
Per capita GDP (% p.a.)	-1.23	-6.06	1.08	1.02	1.28	2.40	1.36
Gross National Income (% p.a.)	-1.21	-5.44	-1.06	3.94	-0.36	2.24	1.15
Per capita GNI (% p.a.)	-1.67	-5.89	-1.52	3.45	-0.83	1.76	0.68
Gross Domestic Product (M Million)	21314.67	20116.91	20430.27	20735.52	21100.65	21708.43	22106.72
Per Capita GDP	10461.74	9827.44	9933.62	10034.65	10163.35	10406.96	10548.09
Gross National Income (M Million)	28418.59	26871.38	26587.14	27634.93	27536.12	28152.77	28477.62
Per Capita GNI	13948.51	13127.11	12927.21	13373.52	13263.07	13496.35	13587.92
Output - Current prices	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Nominal GDP (% p.a.)	4.04	-0.97	0.63	8.98	7.41	7.18	6.19
Nominal GNI (% p.a.)	3.50	-8.88	-0.74	11.98	5.79	7.21	5.66
Nominal GDP (M Million)	35196.79	34855.97	35075.95	38225.37	41056.86	44003.93	46727.39
Nominal GNI (M Million)	45516.44	41476.41	41169.27	46101.57	48769.73	52285.61	55245.50
Sectoral Growth rates (% p.a.)							
Primary Sector	-4.13	-1.74	-2.23	2.04	5.88	0.24	4.24
Crops	-22.82	22.56	9.08	2.30	-5.22	-19.51	25.10
Mining and Quarrying	-9.68	-16.35	22.85	1.22	11.49	4.34	2.08
Secondary Sector	-6.08	-11.60	2.07	0.87	-1.69	7.33	2.60
Manufacturing	-0.69	-9.09	7.66	-6.36	-6.21	1.70	1.11
Construction	-20.26	-39.17	9.84	24.48	12.98	27.56	6.46
Tertiary Sector	2.87	-4.17	1.88	1.87	2.36	1.82	1.25
Wholesale and retail trade,repairs	-17.89	-26.21	-1.28	1.92	3.73	2.88	1.51
Financial and insurance activities	51.50	6.29	-3.14	1.16	2.73	2.59	3.01
Real estate activities	-2.44	-4.38	1.18	0.41	0.34	0.26	0.14
Public Admin, Education & Health	0.55	3.93	7.48	2.32	1.99	1.17	0.08
Savings and Investment - Per cent of GNI							
National Savings	29.80	28.20	15.43	11.54	17.56	21.18	19.45
Of which Government Savings	6.28	9.39	10.48	6.78	11.35	13.76	12.67
Of which Private Sector Savings	23.52	18.81	4.95	4.76	6.21	7.42	6.78
Investment	32.80	29.62	19.20	17.86	22.92	26.46	25.97
Of which Government Investment	9.57	10.50	10.58	7.96	7.69	7.52	7.39
Of which Private Sector Investment	23.23	19.12	8.62	9.89	15.23	18.94	18.58
Resource Balance	-3.00	-1.42	-3.77	-6.32	-5.37	-5.28	-6.52
Savings and Investment - Per cent of GDP							
National Savings	38.54	33.56	18.11	13.92	20.86	25.17	22.99
Of which Government Savings	8.13	11.17	12.30	8.18	13.48	16.36	14.97
Of which Private Sector Savings	30.41	22.39	5.81	5.74	7.38	8.81	8.02
Investment	42.41	35.24	22.54	21.53	27.23	31.44	30.70
Of which Government Investment	12.37	12.49	12.41	9.61	9.14	8.93	8.74
Of which Private Sector Investment	30.04	22.75	10.12	11.93	18.09	22.51	21.96
Resource Balance	-3.88	-1.69	-4.43	-7.62	-6.37	-6.27	-7.71

Appendix I: Selected Macroeconomic Indicators, cont'd					Projections		
	2019	*2020*	*2021*	2022	2023*	2024*	2025*
Inflation rate % (CPI)	5.20	4.98	6.05	8.27	**6.18**	**5.42**	**4.92**
External Sector - Per cent of GDP							
Current Account	-3.88	-1.69	-4.43	-7.62	-6.37	-6.27	-7.71
Imports of Goods	73.21	74.89	76.40	76.79	81.05	83.51	81.81
Exports of Goods	43.72	41.23	44.73	44.96	45.13	44.32	44.12
Capital Flows	3.56	4.35	5.46	4.81	12.46	13.63	14.12
Financial Account	-8.49	7.12	1.57	-6.44	6.09	7.35	6.41
Official Reserves (Months of Imports)	4.44	4.66	5.10	4.22	4.69	5.30	5.32
Government Finance - Per cent of GDP							
Revenue (excluding grants)	43.15	50.45	45.08	42.55	49.93	54.26	51.97
Tax Revenue	21.32	19.45	22.11	22.56	22.34	22.95	22.99
Recurrent Expenditure	38.52	41.97	38.91	39.80	40.95	40.67	39.72
Of which compensation of employees	16.83	17.29	17.48	17.57	17.82	17.11	16.58
Transaction in non-financial assets	13.16	11.23	18.17	14.06	13.38	13.08	12.79
Budget Balance (+ means a surplus)	-5.60	-0.16	-5.93	-6.26	-0.17	3.28	2.18
Monetary Aggregates - Nominal growth							
Money supply (M2)	-8.99	16.87	4.14	-3.40	11.59	7.18	6.19
Private Sector Credit	8.15	0.68	7.23	5.10	10.69	5.38	4.34

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