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THE STATEMENT OF THE MONETARY POLICY COMMITTEE IN VIEW OF THE GENERAL MACROECONOMY

The repo rate is pushed to its lowest level, inflation rate returns to the target range and the Rand continues to gain strength…………

Introduction

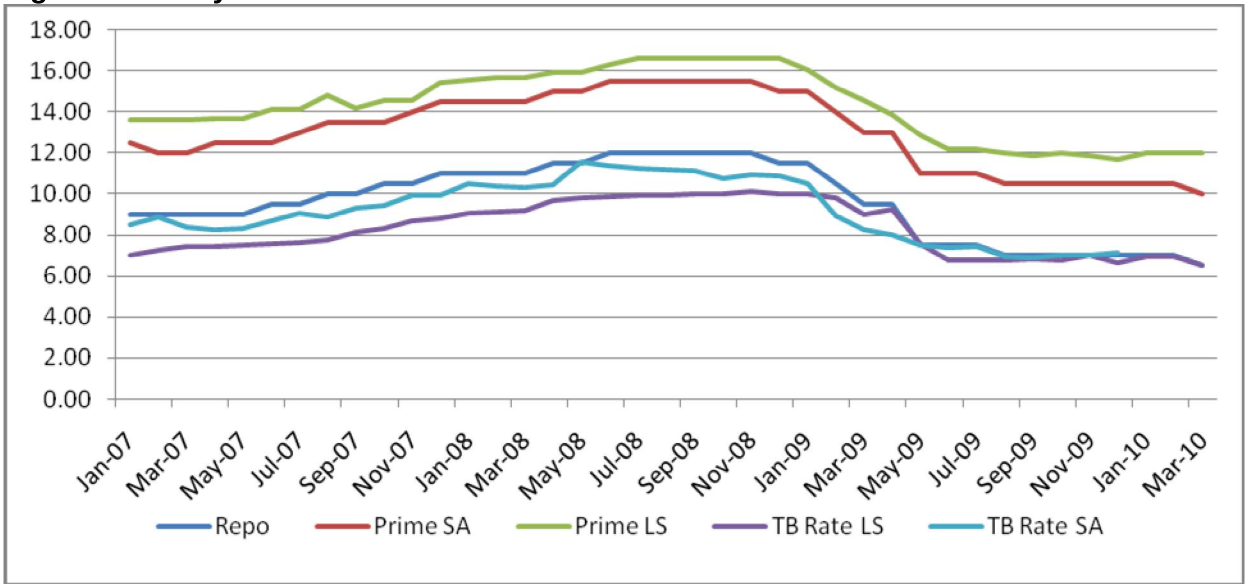
The South African Reserve Bank (SARB) reduced the repurchase (repo) rate by 50 percentage points with effect from the 26th March, 2010. This move came amidst the prediction by most economists that the repo rate would remain unchanged. The Monetary Policy Committee (MPC) cited the improved inflation environment as the basis for this additional monetary stimulus in order to reinforce economic upswing without jeopardizing achievement of the inflation target. The year-on-year inflation rate in South Africa, measured by the change in Consumer Price Index (CPI), returned to the target range and inflation expectations eased. In addition, the Rand has recently remained fairly strong against major trading currencies.

These developments have a direct impact on the economy of Lesotho because of Lesotho's membership of the Common Monetary Area (CMA). Therefore, this article intends to discuss recent developments in interest rates, inflation and exchange rates in Lesotho, and the macroeconomic implications thereof in light of the imminent economic recovery.

Interest Rates Movements

The global economic recession resulted in the widespread adoption of a more accommodating monetary policy globally to counter the recessionary environment by stimulating economic activity. The SARB conducts monetary policy within an inflation targeting framework wherein the repo rate is a tool used to control money supply, hence inflation. In South Africa, monetary policy easing began in December, 2008 and since then, the repurchase rate has been reduced by 550 basis points. The recent reduction of the repo rate from 7.00 per cent to 6.50 per cent put it at a lowest level since introduction of the inflation targeting monetary policy regime in 2000. The repo rate is the rate at which commercial banks borrow money from the SARB in exchange for securities in order to finance their short-term liquidity needs. It is used by commercial banks and other economic agents as a benchmark for the cost of funds in the economy.

Figure 1: Money Market and Commercial Banks Interest Rates



Source Data: CBL

The reductions in the repo rate imply lower money market and commercial banks interest rates not only in South Africa, but in the CMA as a whole because it allows for free movement of capital. To avoid undesirable capital flight, the interest rates differentials in the Area should be generally negligible. As shown in Figure 1 above, commercial rates have been moving in line with the repo rate. In addition, both the Treasury bills and the prime lending rates for Lesotho and South Africa have maintained the same trend and a marginal gap throughout.

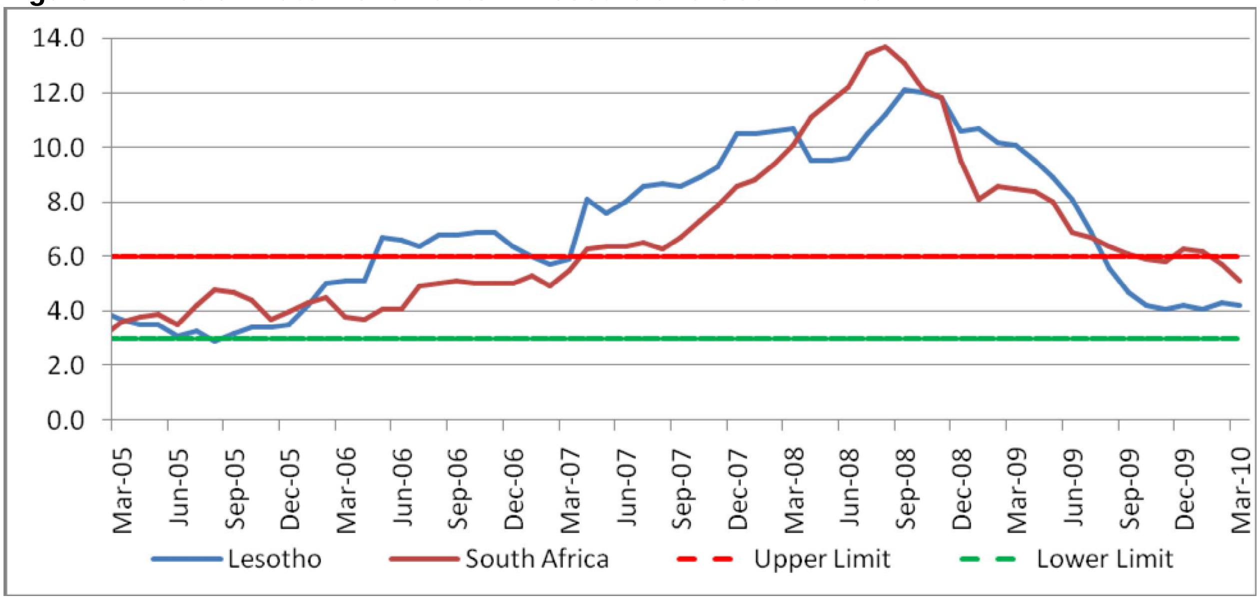
Although economic agents in South Africa react to the monetary policy decisions with a lag, the continuous cuts are beginning to bear fruit. Economic indicators for consumption, production and the composite leading business cycle indicator have, on the overall, improved. Retail trade and passenger vehicles sales indicators increased by 1.16 and 28.9 per cent, respectively, in March compared to December. Indicators of consumption for investment, like commercial vehicles and completed building indices have also improved in recent months. On the contrary, employment went down by 6.3 per cent on annual basis in the last quarter of 2009 but recovered by 0.7 per cent on a quarter-to-quarter basis.

Inflation Rate Movements in Lesotho and South Africa

Inflation is an occurrence that is impacted by changes in the money supply in an economy. As a result Central Banks use interest rates to control money supply and, hence, inflation rate. The inflation target range for the SARB is 3 to 6 per cent on a continuous basis. The SARB managed to contain inflation within the target range for the period September 2003 to March 2007. Since then, inflation rocketed to the high of 13.7 per cent in August 2009. From then onwards, inflation in South Africa has declined continuously until returning to the target range in October and November 2009. However, this rebound was not sustained and inflation crippled above the target range until it returned back again in February, 2010.

This downward trend has been largely at the back of declining food and fuel prices since the second half of 2008. Figure 2 below, shows inflation rate movements in Lesotho and South Africa. The decline in Lesotho's CPI is much steeper than that of South Africa and has been lower since August 2009. The reason behind this variation in CPI between the two countries is the different methodologies used and ways in which their respective baskets have been structured. Specifically, the weight for food and non-alcoholic beverages category is 39.8 and 15.7 per cent for Lesotho and South Africa, respectively. In Addition, South African CPI basket is inclusive of other items which are not captured in Lesotho's CPI.

Figure 2: Inflation Rate Movements in Lesotho and South Africa



Source Data: CBL

Monetary policy decisions are made on the basis of current and expected developments in inflation and in the wider macroeconomy both domestically and globally. It is therefore imperative to preview these expected developments and their likely impact on inflation going forward. According to the SARB, the indication is that inflation in South Africa is likely to return to within the inflation target range on a sustained basis from now on until the final quarter of 2011. These forecasts are in line with the inflation expectations by some analysts although other economic commentators still foresee inflation slightly above the upper target.

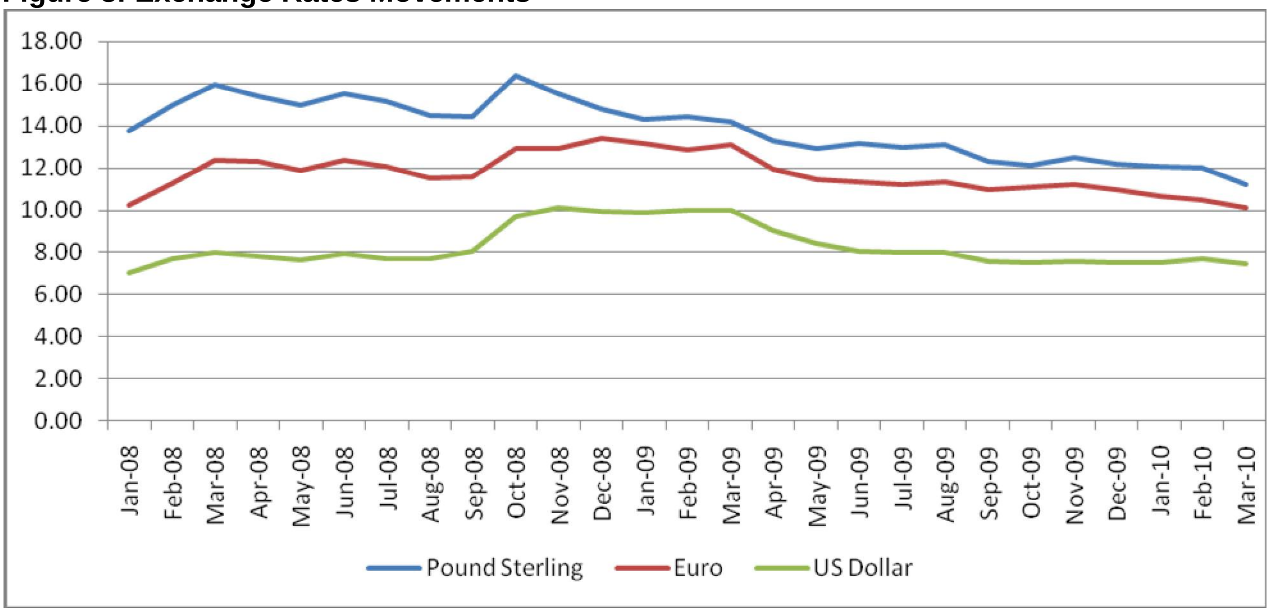
This lack of consensus and uncertainty signals some potential upside risks in inflation expectations. Demand side pressures on inflation are unlikely since consumption expenditure is expected to be constrained by high debt levels, low credit extension, slow recovery in labour market developments and a fragile recovery in domestic output.

On the supply side, food and fuel prices have exerted a downward pressure on inflation since 2008. Going forward these favourable base effects may only continue for food prices whereas fuel prices are expected to start rising. Therefore, this factor remains a risk on the inflation outlook. Notwithstanding some volatility, the Rand is not seen as a big threat to inflation expectations because it has remained strong as shall be discussed later in this paper. Finally, the global economic recovery remains fragile and there are still some doubts about the speed of recovery and its sustainability. The main factor that still poses an upside risk to inflation is administered prices like wages and electricity prices.

Exchange Rates Movements

Short-term movements in the exchange rate mainly reflect the flow of funds in and out of the country. These flows are mainly dependent upon the attractiveness of interest rates. If interest rates are comparatively high in South Africa versus the rest of the world (particularly advanced economies), ceteris-paribus, the Rand is bound to appreciate and vice-versa. This is because investors source funds in low interest rates economies where the money is cheap and invest in high interest rates economies in anticipation of higher returns.

Figure 3: Exchange Rates Movements



Source Data: CBL

In 2009 and the first quarter of 2010, the Rand has appreciated on a sustained basis against the Pound, the Euro and the Dollar. Compared with the peak registered in November 2008, the Rand has appreciated by 27.7, 26.5 and 21.4 per cent against the Pound, the Rand and the Euro, respectively. Despite its volatility, the Rand has in March traded at an average of R7.44 against the Dollar, R10.12 against the Euro and R11.21 against the Pound.

The strengthening of the Rand against these currencies is largely due to the relative weakness of the Dollar, the Pound and the Euro. Other factors that continue to impact on the exchange rate of the Rand include investor sentiment and the sustained capital inflows into emerging markets in response to abnormally low interest rates in advanced economies. The US benchmark interest rate stands at 0.25 per cent whereas the repo is 6.50 per cent. The recovery in commodity prices have pushed up the South African exports thereby improving the current account in the balance of payments. South African exports increased by 10.7 per cent in the fourth quarter of 2009 thus resulting in a lower current account deficit at 2.8 per cent of GDP. This could be an indication that the strong Rand has not offset the positive impact of commodity prices on export earnings. This, in turn, may have also contributed to the appreciation of the Rand.

Implication for Lesotho

The lower interest rates come as a debt relief to households and may spur-on credit extension leading to higher investment and consumption expenditures, and in turn, economic growth. On the producer's side, the lower cost of funds may lead to increased demand for credit for investment purposes. These will in turn boost the prevailing slow economic recovery. There are some indications that the real economy, in South Africa, is responding to the monetary policy stimulus. This augurs well for Lesotho's exports to South Africa, particularly because export earnings from South Africa are not affected by the exchange rate movement.

The low inflation will help protect consumers against erosion of their purchasing power. Low inflation is especially important to protect the living standards of workers and the poor. It will also facilitate better financial and economic planning therefore laying a platform for speedy economic recovery.

Although it is difficult to determine, with precision, an ideal level of the Rand, an excessively strong Rand may have adverse effects on the ailing textiles and clothing sector in Lesotho through erosion of price competitiveness and lower revenue when converted in Maloti. Other implications of the exchange rate appreciation are on the diamond mining sector in Lesotho and gold mining sector in South Africa often leading to layoffs. On the positive side, the strong exchange rate opens a window of opportunity in which the Government can use to pay off its foreign debt at a cheaper rate.

Conclusion

The current macroeconomic climate in general seems to be recovering from the impact of the financial crisis and the resultant world economic downturn. There is some evidence to support that the expansionary monetary policy direction by the SARB is largely contributing to this favourable economic cycle. The continuous repo rate cuts by the MPC are therefore justified and welcomed but this should not be done excessively and without jeopardizing the achievement of the inflation target.

2. Land Reform in Lesotho: Implications for the economy of Lesotho

The proposed Land Bill 2009 has been formulated to repeal the Land Act of 1979………………...

Introduction

Land has been a fundamentally important resource for economic development, food security and poverty reduction in many countries in the world over a long time. The importance of land to most economies and societies has been a major contributing factor in economic growth and employment and has constituted the main livelihood basis for a large portion of the population. Nonetheless, land has become increasingly scarce for majority of people mainly due to a variety of pressures, including population growth. These have resulted in tight competition for land between different groups within the nation, and foreign investors. To compound these pressures, socio-economic factors have, in many places, eroded the customary rules and institutions that have traditionally administered land rights, use and tenure.

In response to these challenges, many countries, especially in Africa, have adopted new policies and enacted new laws governing land tenure and administration. Other countries have repealed the long standing Land laws in order to respond to the internal pressures and international developments and donors' demands. In this respect, Lesotho has not been behind. The proposed land reform in the country has seen the Land Act of 1979 being repealed by the Land Bill 2009. The Bill proposes reforms in land Administration and Land Tenure Security.

The Role of Land in Economic Development

The role played by the Land reforms, the purposive change directed at the reorganization of land tenure structures, has been very critical in the economic development agendas and processes of many countries globally. Most of the now developed and developing countries have drawn up strategies, laws, policies and implemented programmes aimed at making land reforms a success in their national policies. The reform of the land implies the change of the current status of tenure that is geared towards fair redistribution of land to reduce poverty and achieve economic development which is necessary for welfare improvement of the country's population. These land reforms play a vital role in economic development through the following channels; redistributing income and wealth; stimulating capital formation; and improving agricultural productivity, which would eventually have spillover effects into economic growth and poverty eradication.

The transfer of land as a property and asset to the peasants from large landholders means the transfer of the purchasing powering (in terms of income) and a badly needed investment in human capital in agriculture. This makes it easier for the country to eradicate poverty at the grassroots level. The reduction of rentals and the redistribution of land by tenant farmers into owner operators would also alter the income and wealth distribution pattern. This further augments the power of eradicating poverty.

Land reform also affects economic development through capital formation. Land reform may contribute to formation of capital through stimulating accretionary formation of capital. This means that capital formation is characterized by incremental process which is weighted by the time dimension. That is, investment decisions involved are typically made in small segments spread over many seasons or gestation periods. Moreover, land reform may contribute to capital formation through transfer of capital, tied up in land, into industry and other investment opportunities. For example, in a case where land is sold, funds generated from the sale could be directed to investment in such developments as power houses, new industrial plants and fertilizer facilities, or land bonds could be given as security for industrial securities.

Land reforms could play a critical role in economic development through increased agricultural productivity. In order to improve agrarian productivity, greater tenure of security, consolidation of scatted land holdings and redistribution of land ownership could be necessary vehicles. Security of tenure can be improved through written leases, rent limitation, compensation for improvements and disturbance as well as deterioration and automatic renewals of lease holdings.

For Lesotho, land reform process has far-reaching implications for the rural as well as urban population; On one hand, the coming into full effect and implementation of the Land Bill 2009 will act as a conduit through which the poor will access funds from the banks. Under the old system of tenure lack of rights for holding land hampered economic development since people were not in a position to use land as collateral for accessing credit.

Second, granting of land titles to the foreigners is a positive step towards increased physical as well as financial investment. Under the new Bill, foreigners are allowed to hold land in Lesotho for industrial or commercial purposes. Spillover effects of foreigners coming into the country cannot be understated. They are likely to come with new methods of agricultural production and industrial development. Improved methods of technology and their utilization will also follow up should foreigners hold land titles in Lesotho.

Third, land reforms in Lesotho are likely to bring improvements and developments in the national infrastructure. For example, those people who will be granted titles to own mines will try their utmost to ensure the availability of access roads and utilities to their businesses. Infrastructure development has been recognized as a prerequisite to economic development and well being of a nation. Thus, its enhancement through land reform is a necessary step towards economic growth and poverty reduction.

It may also alter the climate of income inequality and distribution. Consolidating small farms into large ones where possible means people can pool resources for betterment of their economic life in order to reap benefits of land consolidation. Redistributing other land areas which are currently non- productive and which are too large can be potentially productive.

Nevertheless, land reform may not attain the intended objectives on the basis of the following constraints. Weak institutional capacity may hinder the smooth implementation of the reforms. The people, particularly the poor, may not be able to enjoy the benefits due to lack of adequate information and/ or financial resources. High costs of enforcement of land rights, which may lead individuals to be reluctant to defend their land rights and poor definitions of land rights, may be impediments to benefits arising from land reform process.

Rationale for the New Land Bill

The Government of Lesotho (GoL) decided to repeal the Land Act of 1979 mainly on the basis of its weaknesses. The main shortfall of the Act was that land administration and tenure were inefficient in a way that was hampering economic development because it did not consider utilization of land as an economic asset. The main features of the Land Act of 1979 included, but are not limited to the following items:

- Dual System: Under this system the land tenure and administration rested on the customary and statutory systems. Within the customary type of tenure, the land was allocated and acquired within the powers of the chief whereas the statutory system, the new allocating body presided;
- Foreigners were not allowed to hold or own land in Lesotho;
- There was inefficient control of urban and peri-urban areas, resulting from poor planning and creating problems for infrastructure development;
- Cumbersome procedures in terms of acquisition of land even to the citizens; and
- Lack of land tenure security.

These features of the Land Act of 1979 have been found to be irresponsive to the economic needs of the country. The land Act of 1979 is considered to be slow, highly costly, hampering development and non-transparent.

The Provisions of the New Land Bill

The Government of Lesotho decided to repeal 1979 Land Act at the back of its weaknesses as mentioned above. The proposed new Land Bill, among other things, is intended to reverse the ills that have been created by this Act. To achieve the desired goals, the Bill's main objectives include, but are not limited to the following:

- To abolish the allocative system under the customary law;
- To ease the provision of access roads and utility services through regularization and adjudication;
- To speed up land disputes through establishment of land courts. This would be a necessary vehicle for economic activities on land;
- To encourage property development and to use them as economic assets through secured titles;
- To provide people with certificates upon allocation of land as form of land tenure security;
- To improve efficiency in the transaction of land thus speeding up the utilization of land for productive purposes;
- To improve land markets since there will be more players; and
- To allow foreigners to have land rights.

Nonetheless, the Bill retains the fundamental principles that the land is vested in the nation of Basotho, and that rights to land are still granted by the King. The Bill further abolishes gender discrimination in land tenure. This has implications for economic development and eradication of poverty and inequality.

Conclusion and Recommendations

Land reform may have benefits for both urban and rural population as earlier noted. It may lead to increased access to credit markets, hence financial sector system; improve the human capital development through enabling beneficiaries to educate their children, increase the efficiency of resource mobilization and hence investment in physical capital, increase the agricultural productivity and become a good source of tax revenue for local government.

However, fragile institutions, information asymmetry, lack of financial resources and unclear implementation modalities of land reforms may undermine the benefits that those reforms would have.

In order to ensure the efficiency of land reforms and the purposes for which it was undertaken, there are some ways which can be used as important vehicles. First, the capacity of legal, social, political as well as economic institutions should be strengthened. Disseminating information in land matters that involve people at the grassroots level may also act as a brake on the failure and may prevent conflicts that do often arise as a result. In addition, legal services should be affordable even to the poor to protect their rights and enhance their chances of benefiting from the reforms.