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INTERNATIONAL DEVELOPMENT ASSOCIATION

COUNTRY ASSISTANCE STRATEGY

FOR

THE KINGDOM OF LESOTHO

May 17, 2010

Southern Africa Country Department 1
Africa Region

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LESOTHO
COUNTRY ASSISTANCE STRATEGY

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ACRONYMS

AAA	Analytic and Advisory Activities
AGOA	African Growth and Opportunity Act (US)
CASCR	Country Assistance Strategy Completion Report
CPI	Corruption Perception Index
CPIA	Country Policy and Institutional Assessment
CRP	Common revenue pool
CRW	Crisis Response Window
DFID	Department for International Development (UK)
DPCF	Development Partners Consultative Forum
EC	European Commission
FTI	Fast Track Initiative (EFA)
GEF	Global Environment Facility
GOL	Government of Lesotho
GTZ	German international cooperative agency
IDA	International Development Association
IFC	International Finance Corporation
LEWA	Lesotho Electricity and Water Authority
LHWP	Lesotho Highlands Water Project
LNDC	Lesotho National Development Corporation
MIGA	Multilateral Investment Guarantee Agency
MSME	Micro, small, and medium enterprise
NPV	Net present value
NSDS	National Strategy for the Development of Statistics
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PRSC	Poverty Reduction Support Credit
ROSC	Reports on the Observance of Standards and Codes
SACU	Southern African Customs Union
SADC	Southern African Development Committee
WASA	Lesotho Water and Sewerage Authority

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EXECUTIVE SUMMARY

i. The Country Assistance Strategy (CAS) for the Kingdom of Lesotho for FY2010–14 is developed within the context of the Government's strategy for growth and sustainable development as expressed in the 2002 "Vision 2020" and its Interim National Development Framework. The latter focuses on four strategic objectives: (i) accelerate shared and sustainable economic growth, ensure employment creation and protect the vulnerable; (ii) address the HIV/AIDS epidemic; (iii) foster good governance to improve public sector service delivery; and(iv) improve the quality of life by promoting human development. These reform priorities of the Government set an appropriate strategic policy direction for the country, and form the basis of the Bank's support under the proposed CAS.

ii. The CAS comes at a critical time as Lesotho confronts the macroeconomic and fiscal challenges arising from the global economic crisis. The crisis hit as Lesotho was gathering economic momentum driven by greater political stability and structural transformation of the last decade. The country had accumulated reserves from foreign direct investment (FDI) and windfall revenues from the Southern African Customs Union (SACU), and had become the largest exporter of clothing to the United States under AGOA. The public sector, expanded rapidly, with public spending increasing to 64.7 percent of GDP in 2008/09. This progress is now threatened by the global crisis, which has resulted in a significant contraction of export markets and SACU revenues. As a result, Lesotho confronts the challenge of adjusting to a major economic shock while finding new sources of revenue and growth.

iii. In the past, the Government of Lesotho (GOL) has demonstrated the resilience to rise to similar challenges and adapt to new circumstances, notably when they had to adjust to declines in remittances from the miners working in South Africa in the early 1990s. Between 1990 and 2005, remittances dropped by roughly 15 percentage points of GDP, and an estimated 65,000 mining jobs based in South Africa were lost. The GOL responded to this external shock by creating 40,000 new jobs, increasing public sector spending and attracting private sector investments, fostered by a liberalized foreign trade regime.

iv. Displaying the same spirit of resilience, the GOL is responding to the current external shocks with bold proposals of adjustment measures. To mitigate the impact of a projected sharp decline of SACU revenues from 35 percent of GDP in 2009/10 to just 14 percent of GDP in 2010/11, the GOL has responded with a bold medium term strategy of aligning budget expenditures with enhanced capacity to raise non-SACU revenues while reducing public spending in the short run. The budget for 2010/11 acknowledges the risks of continuing to treat the inherently unpredictable SACU revenues as an anchor for expenditure planning. It also proposes significant spending cuts, especially in major recurrent expenditure categories, in order to restore long term fiscal sustainability. At the same time, the GOL recognizes a need to get better value for public resources by increasing efficiency and effectiveness of service delivery. Implementation of such a major fiscal adjustment will, however, not be easy and poses major risks for GOL. The

proposed menu of interventions under the CAS is framed within the context of this challenge.

v. The global economic crisis has highlighted the country's economic vulnerabilities and points to the necessity of accelerating progress in laying the foundations for economic competitiveness and export diversification. Towards this goal the GOL is proposing in the short term to: (i) continue building effective institutions, and (ii) improve service delivery by promoting efficiency and performance through the introduction of a results-based budgeting and finance management in the health sector and improved education quality. In the medium term the GOL has committed to: (i) explore new opportunities for sustainable private-sector led growth through an improved business environment and infrastructure development, (ii) position the rapidly growing Maseru area as a competitive node for the region and a new driver of growth; and (iii) target support to smallholder farmers, and exploit the potential for developing commercial agriculture with strong links to value chains in South Africa.

vi. The GOL and the World Bank have agreed on three areas of engagement under the CAS: (i) fiscal adjustment and public sector efficiency, (ii) human development and service delivery, and (iii) competitiveness and diversification. Within these three areas, CAS activities will be grouped into six "results clusters" that take into account cross-sectoral impacts and aim to achieve results by strengthening institutional capacity as a cross-cutting issue. The CAS envisages increased budget support through annual Poverty Reduction Support Credits (PRSC), which would promote enhanced efficiency and quality of service delivery and economic competitiveness.

vii. Given the difficult nature of the transformation that the country will be undertaking, achieving visible results will take time. Therefore, the CAS follows the approach of strategic incrementalism that focuses on delivering development outcomes in key strategic areas, while supporting the Government to gradually shift direction toward a new development paradigm. The Bank and the GOL will review the CAS implementation annually to assess progress and define the next set of strategic steps. A CAS Progress Report will be prepared at mid-term or before then if deemed necessary. To enhance the effectiveness of assistance, the CAS will seek to achieve synergies from the full range of Bank instruments, lending, technical assistance, and analytical work to be delivered in partnership with the government and development partners.

viii. Effective approaches to promoting gender equity will be mainstreamed into the Bank's program. To maintain gender parity in primary education, the program will pay special attention to addressing the issue of primary school enrollment related to "herd boy" syndrome, where boys drop out from school to tend livestock. In health the Bank will support Lesotho to address the issue of maternal and newborn morbidity and mortality. As women continue joining the workforce, the Bank will support the GOL in expanding training opportunities with a focus on women under the Private Sector Competitiveness and Diversification Project. In FY2013 the CAS proposes a Poverty and Gender Study to review progress on poverty reduction and gender equity.

ix. The CAS will build on good practices established in the current CAS of leveraging the limited International Development Association (IDA) resources through strategic partnerships with the government and its many development partners using best

practices such as the Metolong Dam project where US$25 million of IDA resources helped mobilize US$300 million for the project, or the HIV/AIDS project, where US$5 million of IDA grant is being used to improve the government's capacity to implement projects worth more than US$ 100 million financed through the Global Fund and PEPFAR. In addition, the CAS will scale up successful ongoing interventions.

x. The World Bank program in Lesotho faces risks from three sources: the difficult scope and scale of the required adjustment; limited implementation capacity and weak institutions; and low demand for improved governance in the public sector. Any or all of these can undermine the achievement of the CAS objectives. However, the GOL is cognizant of the changes required and, given Lesotho's past history of effecting major transformations, these risks, while substantial, are manageable.

I. INTRODUCTION

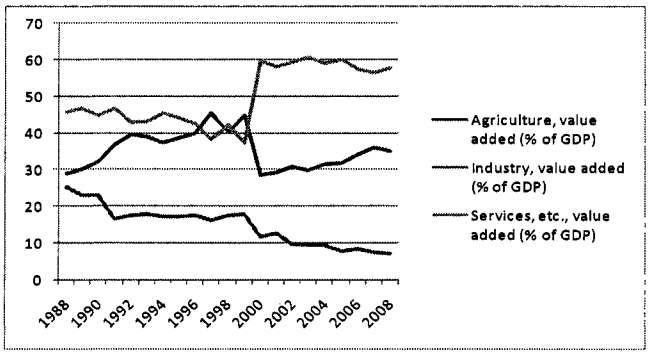
1. This Country Assistance Strategy (CAS) provides a framework for World Bank Group support to Lesotho for fiscal years (FY) 2010–14. It is aligned with Lesotho's Interim National Development Framework through 2012, when the Government intends to present a formal National Development Plan. The CAS comes at a difficult time as Lesotho confronts macroeconomic and fiscal challenges arising from the global economic crisis and a projected sharp decline in fiscal receipts from the Southern African Customs Union (SACU)[1]. The crisis has exposed the country's vulnerabilities to shifts in global markets and the continued dependence of the public sector on SACU revenues.

2. The CAS seeks to support Lesotho's efforts to sustain economic growth momentum in the face of the global crisis and to address critical human development challenges by supporting Government efforts to undertake fiscal adjustment and strengthen public finance management, improve efficiency, quality and equity in access to basic services, and strengthen the competitiveness of the economy.

II. COUNTRY CONTEXT

3. Lesotho, a small country of 1.9 million people and an area of approximately the size of Belgium, is completely surrounded by the Republic of South Africa. Highlands constitute more than two-thirds of the country less than 10 percent of which is suitable for cultivation. Lesotho, with its relatively cost-effective labor and abundant natural resources (diamonds and surplus water[2]), is well placed to take advantage of its unique location inside the economic powerhouse in the region.

Figure 1: Share of Primary, Secondary and Tertiary Sectors in Lesotho's GDP, 1996–2008



Source: World Bank 2009, *World Development Indicators 2009.*

[1] The Southern African Customs Union (SACU) is the world's oldest customs union with the first agreement signed in 1910. It includes Botswana, Lesotho, Namibia, South Africa, and Swaziland, and aims to maintain the free interchange of goods among member countries. The SACU provides for a common external tariff and excise tariff. All customs and excise revenues collected in the common customs area are paid into South Africa's National Revenue Fund for distribution among members according to a revenue-sharing formula.

[2] Water, an abundant natural resource in Lesotho, is being exploited through the 30-year Lesotho Highlands Water Project, initiated in 1986. The project is designed to capture, store, and transfer water from the Orange River system to South Africa's Free State and greater Johannesburg area.

4. Over the last 15 years, Lesotho has demonstrated that it can seize opportunities as they arise and has diversified its economy from a reliance predominantly on subsistence agriculture and remittances to an economy based on manufacturing and water exports and services (figure 1). It has achieved moderate economic growth, taking advantage of the preferential trade regime under the 2001 U.S. African Growth and Opportunity Act (AGOA) to attract foreign direct investment (FDI) and rapidly expand garment exports to the United States. It modernized management of natural resources and transformed its water surplus into sustained revenues by exporting it to South Africa. In addition, before 2009 Lesotho had managed relatively well the revenue windfall[3] from the SACU. However, these structural transformations were not sufficient to enable the economy to achieve high sustainable growth rates to withstand the external shocks, or to substantially improve Lesotho's social indicators. Poverty and inequality have remained high.

5. Poverty in Lesotho is concentrated in population living in isolated rural areas with limited income opportunities and high cost of service delivery due to the country's difficult terrain and scattered settlements. As a consequence, Lesotho's highland population has been migrating to the lowlands, attracted by economic opportunity and better services. As people move, Maseru, the capital, is emerging as an important economic node with the potential to become a growth hub and a key driver of Lesotho's development.

A. Political and Economic Context

i. Political Economy and Governance

6. Lesotho is a constitutional monarchy. The king is the nominal head of state, and executive power resides in a government led by the prime minister. At independence in 1966, Lesotho's political institutions were fragile and untested. This has changed significantly. Over the last decade, Lesotho has had three consecutive democratic elections, which have maintained the Lesotho Congress for Democracy Party in power. During the 1990s, declining remittances from Basotho[4] miners in South Africa combined with intense political contestation and constant splits of political parties overstressed the governance system and undermined stability resulting in elections-related protests in 1998. The economic transformation at the beginning of the 2000s has expanded economic opportunities and helped improve political stability.

7. As a small open economy within SACU and with its domestic currency pegged to the South African rand, Lesotho's macroeconomic performance is closely linked with that of South Africa. While maintaining a balance between economic integration and national sovereignty, the GOL has harnessed opportunities arising from its geographical location including through the Highlands Water Project, access to a large market and good infrastructure to boost economic growth and create jobs.

8. In the short to medium term, GOL will need to underpin its economic autonomy with a dynamic reform agenda. However, a combination of several factors makes this

[3] Large increase in SACU revenues from 25 percent of GDP in 2004/05 to about 40 percent of GDP in 2006/07 and 37 percent of GDP in 2008/09.
[4] Basotho is a Sotho-speaking ethnic majority in Lesotho constituting 99 percent of the population.

politically difficult. Substantial external resources in the form of SACU revenues have artificially cushioned the public finance system and weakened the Government's drive for needed reforms. Further internal demand for effective governance and accountability remains weak because of the ready availability of better paid jobs and services across the border. As a result, the society finds itself in a low level equilibrium in terms of government accountability with no strong pressure for change.

9. In order to strengthen the performance of public finance management systems and institutions the GOL has embarked on several reforms to bring the state and non-state actors closer together and to boost demand for good governance. Recent examples include parliamentary reforms to improve oversight through portfolio committees, a pilot local government and decentralization system (2005–10), and the Service Delivery Agenda. GOL is also proposing to consult with a broad cross section of stakeholders on the country's strategic directions in the context of preparing the National Development Plan. The current economic and fiscal shock is a trigger for a concerted effort by GOL to engage all stakeholders in the reform effort as a means to engender ownership and support for what will be a difficult period of adjustment.

ii. Growth and Macroeconomic Development

10. Lesotho's economic growth leading up to the recent global recession averaged a respectable 3.4 percent a year during 2004–08. The main drivers of growth are described in Box 1. The phase-out of the World Trade Organization Agreement on Textiles and Clothing, of which Lesotho had been a major beneficiary, adversely affected economic performance in 2005. However, performance picked up strongly in 2006 (GDP growth of 6.5 percent), driven by a recovery of the garment industry and increased diamond production. There was also a sharp increase in SACU revenues due to strong growth in South African imports in the midst of a booming global economy and restructuring of the SACU revenue sharing formula in favor of smaller SACU countries.[5] GDP growth slowed to 2.4 percent in 2007 as agriculture faltered affected by a severe drought, and then recovered well in 2008, reaching a growth rate of 4.5 percent. The current account recorded a surplus of about 10 percent of GDP in 2008, and gross official reserves topped US$1 billion by end-2009, far exceeding the official Central Bank of Lesotho target of US$640 million required to keep the loti's peg to the South African rand and providing more than seven months of import cover. However, the impact of the global economic crisis now risks unraveling this good overall progress.

[5] The 2002 SACU Agreement, which went into effect on July 15, 2004, revised the revenue sharing formula in favor of the smaller SACU members.

11. The global economic crisis hit the Lesotho economy hard. A sharp projected decline

Box 1: Recent Drivers of Growth in Lesotho

Lesotho's recent economic growth illustrates that the country can seize opportunities when they arise:

- *Lesotho has attracted considerable FDI into manufacturing to support its economic growth.* Over the past two decades, capital injections (largely from South Africa and Asia) in textiles and clothing manufacturing for export have driven GDP growth. More recently, foreign capital inflows have been motivated by Lesotho's eligibility for duty- and quota-free access to the U.S. market for textiles and clothing products under the 2001 U.S. African Growth and Opportunity Act (AGOA). With exports of US$365 million during October 2007–September 2008, Lesotho was the largest exporter of clothing to the United States under AGOA, surpassing South Africa, Mauritius, and Madagascar. Lesotho remains a leader in Africa in attracting FDI (in per capita terms), despite a drop in net FDI inflows from the peak of US$287 million in 1996 to US$81 million in 2009 (5 percent of GDP). Given its tremendous comparative advantages related to access to South African and SADC markets, Lesotho could still do better.
- *Lesotho capitalized on its abundance of water and its geographic proximity to South Africa* through a series of progressive reforms that attracted South African investments to construct the first phase of the Lesotho Highlands Water Project. Between 1998 and 2006, royalties from water exports averaged some US$20 million a year. On a parallel track, the country developed a strong institutional capacity, so that Lesotho Water and Sewerage Authority (WASA) is now widely recognized as one of the best performing sector agencies in Sub-Saharan Africa.
- *Lesotho successfully exploited diamond mining.* Beginning in 2003, as world diamond prices rose, diamond mining attracted FDI. By the end of 2006, the sector generated revenues of US$90 million a year by producing small quantities of high-value stones. This achievement positioned diamonds behind only the clothing industry in export importance. In 2008 the global economic slowdown hit the sector hard as diamond prices plunged 50 percent from the first to the second quarter of 2008. Only the largest (Letseng-la-Terae) of Lesotho's three operational diamond mines remains open today.

in SACU revenues coupled with a slowdown in exports and declining remittances from South Africa are threatening the country's macro stability. In 2009, GDP growth slowed to 0.9 percent,[6] held back by a major drop in U.S. demand for Lesotho's textile exports. An estimated 10,000 jobs had been lost in the textile sector as of end-2009, down from a peak of 50,000 jobs in 2004. Weak world diamond prices hurt production and exports, bringing the mining sector to a standstill in the last quarter of 2008.

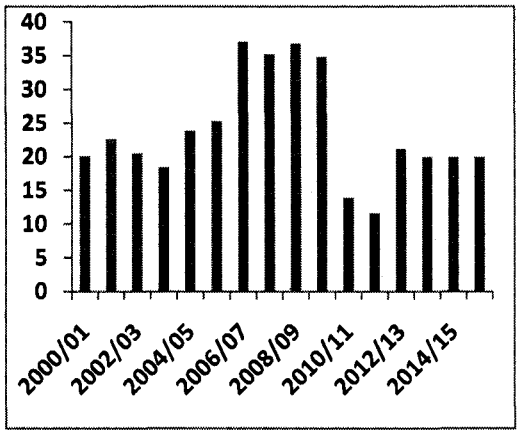
12. The biggest impact of the crisis, which is expected to last through the medium term, is the precipitous decline in SACU revenues. With the sharp decline in South African imports since the onset of the crisis, the SACU revenue pool is shrinking, resulting in much lower customs collection and reducing Lesotho's projected revenues (figure 2). After net repayments by Lesotho to the common revenue pool of approximately 5 percent of GDP,[7] net SACU revenues are expected to drop from an estimated 35 percent of GDP in 2009/10 to just 14 percent of GDP in 2010/11. This steep decline would move the fiscal balance from a surplus in 2008/09 to an estimated deficit of 19 percent of GDP in 2010/11.

[6] These estimates reflect a large downward revision in growth rates compared with pre-crisis projections of 5.2 percent for 2008 and 5.4 percent for 2009.

[7] SACU payments are made on the basis of the next year's projected common revenue pool (CRP), with payments the following year reflecting the actual CRP. The actual CRP in 2008/09 was well below the original projections, resulting in net repayments due by recipient countries.

13. The fiscal stance of the Government had been broadly prudent in the past; although public expenditures did shoot up during the past few years as a result of SACU windfalls. Initially the government saved a portion of additional SACU revenues by reducing public debt and increasing its deposits at the Central Bank. However, an expansionary stance in 2008/09 increased total expenditures from 48 percent of GDP in 2005/06 to just below 70 percent of GDP in 2009/10, with most of the increases coming in current expenditure categories, which are typically difficult to roll back.

Figure 2: Lesotho SACU revenues as share of GDP, FY08-16



14. Recognizing that very high levels of public expenditures were no longer sustainable, GOL has already initiated several belt-tightening actions under the 2010/11 budget to curtail recurrent spending and align it with sustainable levels of domestic revenues. Viewing the current financial crisis as an opportunity, the 2010/11 budget seeks to mobilize more domestic revenues and cut wasteful expenditures and fraud and corruption in all its activities, while also encouraging greater efficiency in delivering public services. The budget envisages a major reduction in recurrent expenditures, largely through containment of the wage bill (to bring it gradually from the current 18 percent of GDP to 14 percent of GDP in 2013/14) and reduction of expenditures on goods and services. On the revenue side the GOL is planning a wholesale revision of rates, charges and fines in line with inflation and is proposing extending the mandate of the Lesotho Revenue Authority to collect all revenues for the Government. These broad fiscal consolidation measures are promising, albeit necessary for ensuring fiscal sustainability. A crucial challenge ahead lies in preparing specific supporting proposals to ensure their proper implementation.

15. Following trends in South Africa and global food and fuel price increases, consumer price index inflation peaked at 12.1 percent in September 2008. Since then, again in line with South African trends, inflation has moderated, and despite the recent upward movement in international oil prices, inflation was recorded at 4.2 percent (year-on-year) in December 2009. Broad money growth moderated from approximately 35 percent in 2006 to approximately 18 percent in 2009.

iii. Macroeconomic Outlook

16. Lesotho faces tough challenges in the medium term stemming from the uncertain global environment and lower SACU revenues. As the global economy recovers, Lesotho's growth is expected to rebound modestly from the estimated 0.9 percent in 2009 to about 3.6 percent in 2010 and 2011 (table 1). Recovery will be driven by moderate expansion in the garment industry through product and market diversification, growth in the non-garment

manufacturing sector (although from a small base),[8] a pick-up in construction driven by public investment to support private sector growth,[9] and resumption of mining. A surge in mining and construction activity is expected in 2012 as a new diamond mine comes on-stream and the key works for the second phase of the Lesotho Highlands Water Project get under way.[10] As a result, GDP is projected to grow about 3.9 percent in 2012. If the highlands project is delayed, GDP growth would be about 2.3 percent instead.

17. South Africa's economic recovery will continue to affect Lesotho's prospects, with the most direct link being SACU revenues and workers' remittances. The rebound in the outer years will depend on how quickly the South African economy recovers from the global crisis. South African growth will also be important for Lesotho's external position; Lesotho's export diversification to cater to the South African market is expected to compensate for the projected sluggish near-term recovery of the U.S. markets.

18. The drop in SACU revenues in the medium term will lead to large fiscal deficit beyond 2009/10 on the order of 20 percent of GDP in 2010/11 and 2011/12. After 2012, SACU revenues are projected to return to the pre-boom level of about 20 percent of GDP. The buildup of government deposits at the Central Bank, estimated at more than 4 billion Maloti (about US$500 million at the current exchange rate) and largely saved from SACU revenue windfalls in the past few years, will provide a cushion in the short term and together with the measures cited earlier is expected to ensure that the budget deficit is fully financed.

[8] Phillips has started operations in Lesotho to manufacture light bulbs and television equipment for the regional market. Other non-garment sectors showing potential are pharmaceuticals, footwear, and plastic hangers to supply to the garment industry.

[9] Donor-supported investment in the Metolong Dam and the second phase of Lesotho Highlands Water Project are key elements of the public investment program.

[10] As in the first phase of the project, South Africa is the key financier, with Lesotho expected to contribute 25 percent of the costs of the project (more than 1 billion rand).

Table 1: Selected Economic and Financial Indicators, 2007-2013 1/

	2007	2008	2009	2010	2011	2012	2013
(Annual percentage change, unless otherwise indicated)							
National income and prices							
Real GDP	2.4	4.5	0.9	3.7	3.5	3.9	2.1
Consumer price index (period average)	8.0	10.7	7.2	6.3	6.0	5.7	5.0
(As percent of GDP)							
Government budget 1/							
Revenue and grants	62.1	66.2	66.3	49.0	50.1	57.0	52.8
SACU revenues	35.2	36.8	34.9	13.9	11.6	21.1	19.9
Non-SACU revenues	25.3	27.7	27.0	27.4	27.5	27.5	27.5
Grants	1.5	1.7	4.4	7.7	11.1	8.4	5.4
Total expenditure and net lending	53.3	64.6	69.0	68.3	68.4	64.0	55.5
Current expenditures	40.3	47.9	51.5	44.4	41.5	40.4	38.6
Overall balance (excluding grants)	7.2	-0.1	-7.2	-27.0	-29.4	-15.4	-8.1
Overall balance (including grants)	8.7	1.6	-2.7	-19.3	-18.3	-7.0	-2.7
Non-SACU overall balance (including grants)	-26.5	-35.2	-37.6	-33.2	-29.9	-28.2	-22.6
Balance of payments and reserves							
Current account balance (excl. official transfers)	-25.7	-22.4	-32.3	-39.5	-33.9	-35.7	-26.4
Current account balance (incl. official transfers)	14.0	9.5	-0.3	-22.1	-22.4	-18.5	-7.9
Gross official reserves in millions of U.S. dollars	946.2	923.1	1131.0	854.8	650.3	650.8	712.5
As months of imports of goods and services	6.6	6.2	7.7	5.2	4.0	3.8	4.3

Sources: Lesotho authorities; and IMF and WB staff estimates and projections.
1/ Fiscal data are reported on a fiscal year basis; the fiscal year begins in April.

19. Over the medium term, the Government will need to embark on a course of strong fiscal consolidation, balancing cuts in Government spending and financing to address emerging fiscal deficits as represented by the fiscal framework agreed under the Article IV consultations. That will involve increasing the efficiency of spending, especially capital expenditures, and rationalizing the payroll, while improving tax administration to boost compliance with the value-added tax (VAT), income tax collections, and other non-SACU revenue collection (see par. 37-41for a more detailed discussion of fiscal consolidation). The Government has indicated its intention to put in place measures to contain the projected fiscal deficit (excluding outlays for Metolong Dam) to approximately 15 percent of GDP in 2010/11. However, these measures will need to be sustained and reinforced beyond 2010/11 for the fiscal deficit to reach sustainable levels.

20. Declining SACU revenues and falling garment exports will worsen the current account balance. While the impact will be countered somewhat by the resumption of mining, risks to the external balance remain in the medium term. The current account balance is expected to shift from a surplus of more than 9 percent of GDP in 2008 to a deficit of 22

percent of GDP in 2010. Capital inflows, donor financing, and partial drawdown of reserves would sufficiently cover the current account deficit in 2010. The current account deficit recovers to about 8 percent of GDP by 2013, largely because of some recovery in SACU transfers, exports, and remittances, which would also enable re-accumulation of foreign exchange reserves to more comfortable levels.

21. Preliminary debt sustainability analysis shows Lesotho to be at moderate risk of debt distress over the medium term. The risk has increased relative to 2009 assessment, reflecting large fiscal and external deficits expected through 2012/13. Debt ratios are projected to remain manageable over the medium term, assuming that the fiscal position returns to balance. At end-2008, the present value of external debt stood at 33.2 percent of GDP.

22. Under the baseline scenario, Lesotho's present value of debt to GDP ratio is projected to increase from 29 percent in 2009 to 35 percent by 2012 as a result of debt incurred to finance fiscal deficits. The present value of debt to GDP ratio is projected to rise to 43 percent by 2019, above the 40 percent indicative threshold,[11] due almost entirely to borrowing for the second phase of the Highlands Water Project. The ratio is then expected to decline to 21 percent by 2029, as the fiscal position remains in balance. The present value of debt to exports and revenues would also rise through 2019 but remain well below indicative thresholds for debt distress. There would also be a modest increase in the ratio of debt service to exports (from 4 percent to 5 percent) and debt service to revenues (from 3 percent to 6 percent), reflecting the increased stock of outstanding debt. The highly concessional nature of both existing debt and new borrowing (except for the rescheduled SACU payments and the borrowing for the Highlands Water Project) helps to contain the increase in debt service ratios and contributes to their return to lower levels as the impact of the SACU revenue shock begins to recede.

B. Poverty and Human Development

23. Lesotho's progress in moving from predominantly subsistence economy relying on overseas remittances to a lower middle income, diversified economy exporting natural resources and manufacturing goods has brought higher, more secure incomes to a significant portion of the population, and the percentage of the population living below US$ PPP US$1.25/day fell from 48 percent to 44 percent between 1995 and 2003.[12] Opportunities in the urban labor market have been especially important for women, with the textile sector providing prospects for young women migrating from rural areas. But Lesotho's unequal income distribution (the Gini coefficient of 0.63 is among the highest in the world) and high level of unemployment (at 22.7 percent in 2008)[13] dampened the effect of growth on poverty. Poor agricultural performance and declining opportunities for low-skilled Basotho in South Africa caused poverty to persist in rural areas, so that a substantial portion of the population

[11] The indicative thresholds for debt sustainability, proposed under the framework for low-income countries are 40 percent for the net present value (NPV) of the debt to GDP ratio, 150 percent for the NPV of the debt to exports ratio, 250 percent for the NPV of the debt to fiscal revenues ratio, 20 percent for the debt service to exports ratio, and 30 percent for the debt service to revenue ratio.

[12] *World Development Indicators* Table 2.8

[13] According to the Integrated Labor Force Survey in June 2008, the self-reported unemployment rate - not an internationally comparable number - was 22.7 percent.

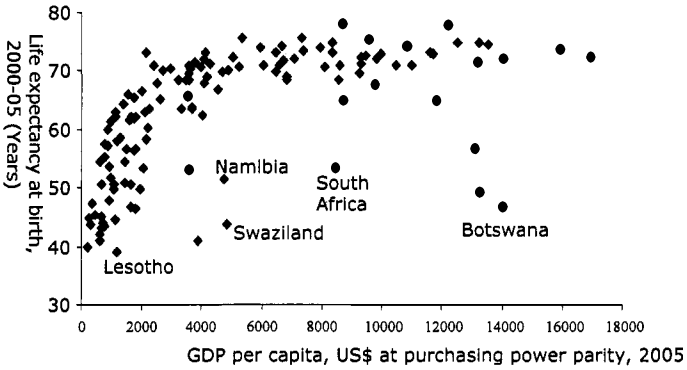
that was unable to diversify their sources of income did not directly benefit from economic growth.

24. Lesotho has used public expenditures as a key tool in the fight against poverty. To reduce exclusion and inequality in opportunities, and ensure that all citizens are able to benefit from economic opportunities, Lesotho has substantially expanded access to social and economic infrastructure. The expansion of access to services led to progress in education and water supply, but the health care delivery system remained weak and combined with the scourge of HIV/AIDS caused Lesotho's relative performance on the Human Development Index (HDI) ranking to fall from 127 of 174 countries in 1998 to 156 of 182 countries in 2007.

25. Lesotho has the third highest adult HIV prevalence in the world, at 23.2 percent: 26 percent of women and 19 percent of men ages 15–49 are infected. Each day, an estimated 62 people are newly infected and 50 people die due to AIDS. At the end of 2007, an estimated 270,000 people in the country were living with HIV, 11,800 of them children. The number of AIDS orphans was estimated at 108,700 in 2007.

26. GOL regards HIV as one of its most important development issues, and the Government is addressing the pandemic through its HIV/AIDS National Strategic Plan.[14] Coverage of some key HIV/AIDS interventions has improved, including prevention of mother to child transmission and antiretroviral therapy. Prevention of mother to child transmission coverage increased from about 5 percent in 2005 to 31 percent in 2007. Significant progress has been made in the roll-out of antiretroviral therapy has made good progress, with 38,586 people receiving treatment by 2008. The "Know Your Status" campaign boosted the number of people being tested for HIV to 229,092 by the end of 2007, 12 percent of the population and three times the number tested in 2005. As a result, the annual rate at which adults in the population who are HIV-negative become HIV-positive declined from 2.9 percent in 2005 to 2.3 percent in 2007, lowering the estimated annual number of new infections from 26,000 to 21,560. These are the first signs of a decline in the HIV epidemic, but it is not yet clear what accounts for these reductions in new infections (most prevention programs were rolled out and scaled up after the reductions were observed; see Box 2 for additional information).

Figure 3: GDP per Capita and Life Expectancy, 134 Low- and Middle-Income Countries



Source: World Bank 2008, World Development Indicators, 2008.

[14] National HIV/AIDS Policy, National Orphan and Vulnerable Children Policy, HIV Testing and Counseling.

27. HIV/AIDS has had a negative impact on social indicators. Lesotho has the lowest life expectancy at birth among countries with similar income per capita (figure 3), and other indicators have also deteriorated. Infant mortality rose 2.5 percent, and under-five child mortality rose 33 percent over the last decade. The most recent maternal mortality estimates range from 762 to 960 per 100,000 live births, placing Lesotho in the 80th to 90th percentile globally.[15]

Box 2: HIV/AIDS Pandemic: Trends, Challenges, Response, and Prospects

Following a steep increase in HIV prevalence through the 1990s, the epidemic stabilized after 2000 at very high levels—almost a quarter of adults ages 15–49 are HIV positive. Migrant labor was the key driver of epidemic, while multiple, concurrent sexual relationships before and during marriage are the main contributing factors. Although the rate of growth in new infections declined from 2.9 percent in 2005 to 2.3 percent in 2007, many preventable HIV infections still occur each year in adults and children.

The Government's policy framework for HIV prevention is comprehensive, but it has not yet been translated into fully scaled-up programs. In 2006/07, only 10 percent of HIV/AIDS funding went to prevention, while 33 percent went to care and treatment, 24 percent to program management, 13 percent to support for orphan and vulnerable children, and 11 percent to social protection, putting prevention in fifth place. Behavioral and social change interventions received only 2 percent of prevention funding in 2006/07.

Recently, most behavioral messages have been related to the national campaign "Know Your HIV Status," which helped tens of thousands of people learn their HIV status but which lacked a proper referral system for people testing positive and adequate post-test counseling for those testing negative.

Partner reduction must be at the center of a successful behavioral and social change strategy. The country needs to redouble its efforts to reduce multiple partners among unmarried and married adults and youth. A key complementary measure is male circumcision, which can prevent up to 60 percent of new infections in men. Today, only about 15 percent of Basotho men are fully circumcised. Lesotho also needs more rigorous evaluations to determine what works in changing behavior to reduce new HIV infections.

These actions to sharpen and refocus prevention are essential. In September 2008, antiretroviral therapy reached just 45 percent of those in need. Unless more new infections can be prevented, it will be difficult for Lesotho to maintain—let alone expand—access to treatment.

28. There are some areas, however, in which the Government has been making progress. Immunization coverage has remained above 80 percent, and antenatal care coverage is among the highest in Africa, at 90 percent. The share of children with diarrhea who receive oral rehydration therapy has nearly doubled since 2000. The Emergency Human Resources Plan seeks to strengthen training and recruitment, improve remuneration, introduce quality assurance mechanisms, and implement a ministry-led initiative to improve maternal health.

29. Lesotho has achieved substantial gains in education since introducing free primary education in 2000. The net primary enrollment rate rose from 60 percent in 1999 to 82 percent in 2008, among the highest in Sub-Saharan Africa. Lesotho has achieved gender parity in primary education. Most importantly, the probability of attending primary school is equal for the children from the richest and the poorest households. However, secondary and tertiary enrollment rates remain low—50 percent and 4 percent in 2008—and budget allocation is skewed toward tertiary education (some 35 percent of the education budget).

[15] World Bank 2008, *World Development Indicators 2008.* These child and maternal mortality indicators are based on 2004 Demographic and Household Survey data; the next survey is expected to be finalized in several months.

Legal and regulatory framework to support a demand-driven technical and vocational education and training system is quite weak.

30. Lesotho also has made notable advances in water services. Sustained investments in urban water supply since the late 1970s have paid off. Approximately 80 percent of the population has access to safe drinking water. A strengthened national Water and Sewerage Authority has reduced unaccounted-for water loss from 40 percent to 26 percent over the last five years. Lesotho was ranked 3rd among 24 African countries sampled over 1995–2005 in moving populations away from the use of surface water to higher levels of service, including increased access to piped water, longer hours of service and improved quality.

III. LESOTHO'S VISION

31. The GOL development goals are reflected in its "Vision 2020" and the Interim National Development Framework. "Vision 2020," issued in 2002, articulates the long-term strategic priorities so that by 2020:

> *Lesotho shall be a stable democracy, a united and prosperous nation at peace with itself and its neighbors. It shall have a healthy and well developed human resource base, a strong economy, a well managed environment and an established technological base.*[16]

32. Lesotho issued its Poverty Reduction Strategy in 2004 but has yet to fully implement it. In 2009, the Government developed the Interim National Development Framework, to serve as an interim strategic plan for the next two fiscal years while the four-year National Development Plan for 2011/12–2015/16 is being drafted. The interim framework ratifies four priorities: (1) accelerate shared and sustainable economic growth, ensure employment creation, and protect the vulnerable; (2) address the HIV/AIDS epidemic; (3) foster good governance to improve public sector delivery; and (4) improve the quality of life by promoting human development.

33. The Budget Speech for fiscal 2010/11 remained focused on the economic fundamentals of pursuing high, shared and sustainable growth; reducing poverty; creating jobs; and protecting the poor, orphans, and other vulnerable groups. [17] While dealing with the consequences of the global economic crisis in the short term, the Government is also addressing medium- and long-term development needs. The 2010/11 budget calls for belt tightening and for using the crisis as an opportunity to mobilize more domestic revenues and cut wasteful expenditures, fraud, and corruption in all Government activities by increasing efficiency in delivering public services and collecting taxes, fees, and other charges. It calls for reversing the growing culture of dependency on state hand-outs and for adopting a long-term fiscal strategy aligning expenditures and long-term domestic revenues and non-SACU revenues. In the medium term, public expenditures will focus on promoting growth through the development of a minimum infrastructure platform—roads, power, water, and telecommunications—to support private sector investment and build the necessary skills,

[16] http://www.lesotho.gov.ls/articles/Vision%202020%20-Executive%20Summary.htm

[17] "An aggressive domestic resource mobilization and expenditure prioritization is an Imperative," Budget Speech to Parliament for the 2010-11 Fiscal Year by Minister of Finance Timothy Thahane.

institutions, and structures. As appropriate, private sector financing for some large projects will be mobilized through public-private partnerships.

34. In response to a request from the Minister of Finance and Development Planning, the World Bank prepared a series of economic policy notes, "Reshaping Lesotho's Position in SACU to meet the Challenges of Sustained and Shared Growth." The policy notes have provided an analytical underpinning for the Government's growth strategy and the 2010/11 budget. The main points deriving from the policy notes and from the recent poverty and gender assessment are reflected in the next section.

IV. LESOTHO'S DEVELOPMENT OPPORTUNITIES AND CHALLENGES

35. Lesotho's opportunities to sustain growth in the wake of the global crisis depend on its ability to manage the fiscal shock caused by the decline in SACU revenues in the short term and to develop new sources of growth over the medium and longer term, shifting its development paradigm from reliance on the public sector to reliance on the private sector as the chief economic engine. To do so, Lesotho needs to address three main challenges: (i) undertake a fiscal adjustment to absorb the sharp decline in SACU revenue and increase public sector efficiency, (ii) enhance economic competitiveness, especially within SACU, and (iii) advance human development and reverse the spread of HIV/AIDS. In addition, Lesotho will need to address its weak institutional capacity, a major bottleneck to sustainable growth. Lesotho's transformation path is likely to be long and bumpy, particularly in light of a much changed external environment following the global crisis.

A. Fiscal Adjustment to Absorb the Sharp Decline in SACU Revenue and Increase Public Sector Efficiency

36. Following a path toward fiscal sustainability over the next five years is critical for dealing with the major immediate challenge of the expected sharp decline in SACU revenues. In the past, Lesotho authorities have demonstrated that they can effectively respond to such challenges. For example, in early 1990s they successfully adjusted to a significant decline in remittances from the miners working in South Africa. Between 1990 and 2005 remittances dropped by roughly 15 percentage points of GDP and an estimated 65,000 mining wage jobs were lost. The GOL responded by increasing public investments and attracting FDI, fostered by a liberalized foreign trade regime, and creating 40,000 new jobs.

37. To mitigate the current fiscal shock, the GOL will need to reprogram its fiscal priorities, improve tax collection, mobilize alternative sources of financing, and increase expenditure efficiency. The fiscal adjustment will require restructuring expenditures (identifying spending categories that can be reduced or postponed), while protecting allocations to social and growth-supporting activities. The Government has taken the first steps with the 2010/11 budget, which assumes aggressive cuts in expenditures by reducing waste and inefficiency.

38. The short-term possibilities for increasing non-SACU revenues are limited because Lesotho's tax system is already relatively well designed. Tax collection was recently improved, and non-SACU revenues already constitute about 27 percent of GDP.[18] However,

[18] See Policy Note on "Fiscal Challenge in Lesotho: Diagnosis and Options for Reform."

on the revenue side, the 2010/11 budget assumes a comprehensive revision of rates, charges, and fines and considers extending the mandate of the Lesotho Revenue Authority to collect all revenue for the Government. Over the medium term, the tax system can be enhanced by strengthening tax collection, improving the system of nontax revenues, increasing transparency, and expanding the tax base by improving the business environment to attract more investment.

39. Fiscal consolidation on the expenditure side will need to be driven by cuts in both recurrent and capital expenditures. Substantial downward adjustments in the public sector wage bill and spending on goods and services should be the main elements of current expenditure consolidation. Cuts in expenditures on goods and services will require careful management and corresponding increase in the efficiency of expenditures to ensure delivery of key public services.

40. Strengthening the effectiveness of public spending and the accountability framework is at the core of fiscal consolidation. Lesotho's public sector is large, with expenditures of approximately 70 percent of GDP (one of the highest in the world). The country has historically had a poor record of public sector governance. Transparency International ranked Lesotho 89 of 180 countries on its 2009 Corruption Perception Index. Lesotho's ranking has declined steadily since 2005, when it ranked 70, picking up only in 2009. To address these concerns, the Government started a comprehensive reform program in 2005 covering the budget cycle from formulation to legislative scrutiny and audit. The 2009 Public Expenditure and Financial Accountability scores showed only slight improvement because of the complexity of reform and limited implementation capacity. Remaining challenges include low utilization of the budget, especially of the public investment budget, and weak institutional capacity in development planning and project implementation.[19] Compliance with procurement rules is weak. Decentralization has transferred procurement decisions from the Central Tender Board to tender boards under the line ministries, while delays in adopting the Audit Bill and Public Financial Management and Accountability Bill have impeded oversight. In addition, the limited availability of budget information constrains oversight by civil society, the legislature, and the media in assessing Government policy implementation.

41. To mitigate the consequences of the fiscal adjustment on poor people, the government will need to continue improving service delivery, including better provision of social safety nets, and to rely on the private sector to generate growth and employment opportunities. These challenges are discussed in turn below.

B. Advance Human Development and Reverse the Spread of HIV/AIDS

42. As mentioned earlier Lesotho's human development indicators deteriorated over the past decade despite high levels of government social spending. Major challenges in human development stem from the country's topography (about two-thirds of the population live in the hard-to-access highlands), high prevalence of HIV/AIDS, and weak service delivery. Facilitating access to social services while improving the quality and equitable coverage of services will become more difficult because of the fiscal squeeze following the economic

[19] The recent public expenditure management reforms were triggered by chronic underspending (72 percent of the total budget in 2009/10), a reflection of major weaknesses of budget formulation and execution.

crisis. However, there is considerable room for efficiency gains in the provision of health, education and social protection services.

43. The health sector suffers from systemic weaknesses. Despite a serious HIV/AIDS epidemic, demand for health care (outpatient visits per capita and bed occupancy ratios) is very low. Quality of care, high transportation costs, long waiting times, and shortages of some drugs and equipment limit access and create a false impression of a low demand for services. The situation is exacerbated by severe human resources shortages, and even available trained staff is used sub-optimally. The problem is not a lack of resources. Lesotho spends about 6.4 percent of its GDP on health and social welfare, and the development assistance to health[20] as a share of total health spending has progressively increased from 6.4 percent in 2002 to a high of 18.4 percent in 2008[21]. At the same time, utilization of donor and budget funds is poor (the execution of the health sector budget was 87 percent in 2006/07) mainly because of low capacity, weaknesses in public finance management and incomplete decentralization. The main task is to introduce a system of results-oriented budget planning and finance management using innovative models of performance-based financing aimed at addressing the perverse incentives both for managers of health programs and for the health personnel directly involved in service delivery.

44. Lesotho declared HIV/AIDS a national emergency in 2000 and has taken steps to reduce the incidence rate. Limited progress in containing the epidemic arises not from lack of resources, which are abundantly available from development partners as mentioned above, but from the complexity of implementation, which requires a coordinated, multisector response that strains the Government's limited capacity. The challenge is to improve coordination to ensure that the substantial resources available to fight HIV/AIDS are used effectively. Experience suggests that harmonized support could improve results. For example, with the help of a previous World Bank HIV technical assistance project, which focuses on strengthening the GOL's capacity in the sector, performance of the Global Fund grants has improved considerably.

45. Important education challenges also remain. In recent years, Lesotho has demonstrated considerable commitment and leadership in improving basic education, which has delivered good results, especially in improving access. The next step is to improve the quality of education (there is a dire shortage of school furniture, teaching materials, and textbooks in the language of instruction for grades 1–3 and repetition rates average 20 percent and are as high as 29 percent for grade 1) by upgrading school infrastructure (only 48 percent of schools meet the minimum physical standards conducive to learning) and enhancing the quality of teaching and learning (as much as 42 percent of teaching staff is unqualified), which need to be addressed.

46. Lesotho also needs to better align the curricula and skills mix with the needs of the country. The higher education and technical and vocational education curricula are poorly matched to labor market needs, and students perform weakly in mathematics and science at all levels. Reforms—a training levy on industries, industry involvement in managing training and staffing to align the sector with industry requirements—have faced strong resistance.

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[20] The most important sources of development assistance for health are: the Global Fund, the Government of Ireland, World Bank, African Development Bank and the European Commission.
[21] WHO, 2010, National Health Accounts Database.

There is no market-driven system to fund university education and technical and vocational training. International migration, mainly to South Africa, exacerbates the skills shortages and undermines Lesotho's already weak capacity.

47. Developing a social protection strategy and putting in place effective social safety nets should be a key priority in an environment of economic downturn and fiscal squeeze. Currently, the GOL spends about 4.2 percent of GDP on social protection, including old age pension, public assistance scheme, school feeding program, disability and other programs. The old age pension alone costs approximately 1.4 percent of the country's GDP. However, social protection programs remain fragmented, uncoordinated, limiting the GOL's capacity to respond quickly to new challenges. A review conducted by the CARE NGO in 2006 provides evidence that traditional village and family networks are increasingly strained by new social vulnerabilities, and the piecemeal social protection approach currently in effect excludes a part of the population in need of assistance. Consolidation and better targeting would increase the efficiency of social protection programs in promoting inclusion and protecting the poor.

C. Enhance Economic Competitiveness and Diversification

48. Lesotho faces the challenge of creating an environment that generates adequate employment opportunities for the currently unemployed and for those who will soon join the unemployed ranks as a result of the fiscal squeeze. Although creating new jobs will take time, an improved investment climate, combined with an educated, cost-effective labor force and a strategy for harnessing new export opportunities, including better exploiting the regional markets, will improve Lesotho's growth prospects. To support growth over the long term, Lesotho will need to address its infrastructure gap, especially for the rapidly growing Maseru area, and position this area as a competitive node for the region and as a new driver of growth. The country also can benefit from creating conditions for expansion in local entrepreneurship, improving the environment for agribusinesses, targeting support to smallholder farmers, and exploiting the potential for developing commercial agriculture with strong links to value chains in South Africa. The GOL will initially have to rely on FDI to support growth, while continuing efforts to strengthen the domestic private sector.

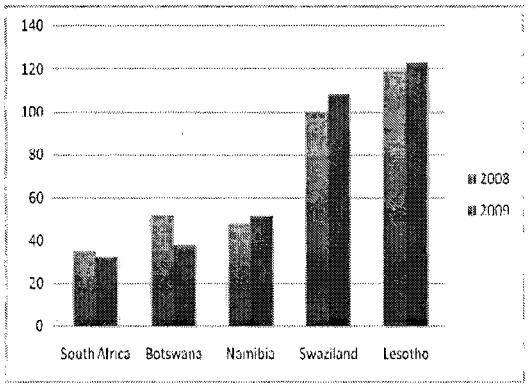
49. Lesotho's domestic private sector is small and weak. A reliance on FDI as the driver of growth led to the neglect of domestic entrepreneurship in the past. The large public sector leaves little space for the domestic private sector, which is poorly organized and lacks influence over Government decision making. The Government has tried to address this challenge, through the Lesotho National Development Corporation (LNDC) and the Basotho Enterprises Development Corporation (BEDCO). BEDCO in particular has a mandate to train and support local enterprises to overcome the lack of skills and managerial capacity, provides physical space for businesses, and creates links to larger firms in Lesotho. However both these agencies have not been able to make significant inroads in supporting the domestic private sector due to organizational capacity and other challenges. Efforts to strengthen domestic entrepreneurship will need to be redoubled while working in parallel to attract foreign investors.

50. A stable macroeconomic environment, a relatively low-cost and good-quality labor force, proximity to South Africa's modern transport infrastructure, and a free trade environment within SACU – the biggest market in Africa – make Lesotho attractive to

regional and global companies seeking access to regional markets.[22] Lesotho's competitive potential for agriculture, tourism, and other sectors remains largely unexploited.

51. To harness new growth opportunities and attract FDI, Lesotho needs to become more **competitive**, particularly within SACU, where Lesotho performs the worst in terms of Doing Business indicators (in 130th position in 2009). The Doing Business report reveals striking variation in indicators. Performance was worst on access to land, trade across borders, company start-up, licensing, and investor protection. Inefficient customs procedures and processes on Lesotho's borders with South Africa hamper trade with this important neighbor.

Figure 4: Lesotho Lags behind SACU Neighbors on Doing Business Indicators, 2008 and 2009



Source: International Finance Corporation and World Bank 2009 *Doing Business 2009.*

52. GOL recent efforts include the establishment in 2007 of a One-stop Business Facilitation Center for the issuance of import and export permits, rebate certificates, trade enterprise licenses, work permits (for textile companies), and residence permits for manufacturers. The processing time has dropped from 2–3 days to 5–6 hours for export permits and from 4 days to 1.9 days for import permits during the previous CAS period. Nonetheless, Lesotho still lags behind other countries in the region (figure 4). An immediate priority is adoption of the Companies Bill and the Industrial Licensing Bill, which has been held up by the political process, which would facilitate registration and ease licensing requirements.

53. Besides the business environment, Lesotho needs to deal with other barriers to economic activity such as access to land, infrastructure bottlenecks, and a skills mismatch exacerbated by the exodus of skilled personnel.

54. Easing **access to land** is critical to promoting investment in industrial property development and agriculture. Foreign investors have no direct access to land titles in Lesotho, and there are sensitivities to foreign land ownership. With usable land scarce, Lesotho's land policy aims to prevent a few from acquiring excessive land. Although leasing is a politically acceptable alternative, only citizens and firms with majority control by Lesotho citizens may lease land. The present system, in which the Land National Development Corporation leases land from the Government and subleases it to investors, is not functioning well.

[22] *World Development Report 2009* highlighted that closer regional integration helps countries remove some supply-side constraints by enlarging markets, generating economies of scale in infrastructure and public good provision, and facilitating greater trade integration with the global economy.

55. **Agriculture** has significant growth potential in both the lowlands and the highlands and is the only source of income for many households in rural areas. Apart from land access, other barriers to achieving Lesotho's agricultural potential includes agro-ecological and climatic conditions, including recurrent cycles of drought, erratic rainfall, hail and frost, and limited areas of arable land. Poor farming practices, limited use of quality seeds, and inappropriate selection of crops prevent achieving available production potential. In addition, the development of viable, market-oriented crop and livestock production faces multiple constraints. The land tenure system discourages investments in land improvements (irrigation, soil and water conservation measures, and tree planting). Commercialization efforts are undermined by market distortions caused by the Government's involvement in commercial activities that are either not viable or should be left to the private sector. The Government is focusing on improving marketing infrastructure and the investment climate for commercial agriculture, targeting support to smallholders to increase their income opportunities, and addressing sustainable land-use practices.

56. Overgrazing and **climate change** are likely to have a negative impact on agriculture and the quality of water. Lesotho is the water tower of Southern Africa, but its fertile soils are highly erodible. Inappropriate land-use practices and rising levels of human occupation have resulted in considerable erosion, depleting topsoil, reducing the quality of arable land, and contaminating water streams. In addition, several climate change models forecast that global climate change will reduce precipitation in Southern Africa, leading to higher evaporation losses and less runoff and groundwater recharge. Rangeland conditions may deteriorate as a consequence of changes in climate, lowering the quality of livestock and livestock products. Addressing soil erosion and increasing the resilience to climatic changes can have multiple benefits, including restoring soil productivity and improving crop production.

57. To support long-term growth, Lesotho needs to reduce the **infrastructure** gap, especially for the rapidly growing Maseru area, and position that area as a competitive node for the region and a new driver of Lesotho's growth. Fiscal constraints imposed by the decline in SACU revenues mean that great selectivity is needed in prioritizing investment in infrastructure to high-growth, high-potential areas. The rapidly growing Maseru region, which is increasingly being held back by inadequate urban infrastructure, including the availability of water services and lack of factory shells for new and expanded businesses—all identified as bottlenecks to business development by potential South African investors.

58. Inadequate, irregular **water** service is a constraint on new growth, particularly in Maseru and its environs, where most textiles and light manufacturing are based. The Metolong Dam and Water Supply Program, which will more than double the availability of treated water by 2014, will eliminate the source constraints for the existing water network in the greater Maseru area, but additional investments will be needed to accommodate new households in peri-urban areas.

59. Lesotho also needs to complete its ambitious **road network** program and develop the institutional capacity of the Road Directorate. Road transport is the most common mode of transportation in Lesotho, handling more than 90 percent of passenger traffic and some 66 percent of goods transport. The quality of the national road network improved from 27 percent good and 38 percent fair in 2006 to 34 percent good and 43 percent fair in 2009. Average travel cost to services and markets along the Southeastern Corridor declined 20

percent between 2006 and 2009. In 2008, user fees accumulated in the Road Fund financed 72 percent of routine and periodic road maintenance, up from 50 percent in 2005. However, falling SACU revenues will make it difficult to meet the substantial financing needs of the sector without scaled-up donor support.

V. WORLD BANK ASSISTANCE STRATEGY

A. Lessons from the Last Country Assistance Strategy

60. The 2010 Country Assistance Strategy Completion Report (CASCR) finds that Bank programs achieved good results in areas where World Bank involvement was sustained and where institution building received strong attention, such as in water and education. The CASCR also found that analytic and advisory activities (AAA) were well aligned with country needs and priorities, that delivery of the lending program was on target, and that portfolio performance was satisfactory.

61. However, the CASCR notes limited progress on key challenges, many of which remain as they were at the time of the 2005 CAS: high incidence of HIV, mixed likelihood of reaching Millennium Development Goal targets, high levels of poverty and inequality, and weak competitiveness. Efforts to catch up with structural reforms, delayed by the political instability in the 1990s, were found to be straining limited government capacity, thus weakening the impact of World Bank and other development partners' efforts. Observing that implementation has been impeded by the slow legislative process and incomplete reforms, the CASCR advises focusing on areas of reform where the Government shows strong leadership and building up capacity to ease critical implementation constraints in these areas.

62. In addition, the CASCR calls for a sharper focus on the shared growth agenda to take advantage of the analytical work produced during the last CAS period. This work emphasizes agricultural and rural development, encouragement of entrepreneurship, and a rethinking of the role of the state, which now absorbs more than half of GDP. To bolster the country's competitiveness, the CASCR sees a need to harness regional trade opportunities, beginning with trade facilitation and regional integration, especially with SADC.

63. To better measure the development impact of the Bank's program, the CASCR emphasizes the importance of monitoring and evaluation to continuously assess the development impact of the Bank's program. The Bank should help the authorities develop monitoring capacity to track progress and improve the policy dialogue.

B. Current World Bank Group Program

64. *International Development Association (IDA).* Lesotho's IDA portfolio comprises six projects with net commitments of US$100.7 million as of May 1, 2010. Portfolio performance is mixed with is one problem project in the portfolio – the Water Sector Improvement Project (FY2005). On the positive side, the disbursement ratio of 38.6 percent in FY2009 was above the regional average of 24.0 percent.

65. The bulk of IDA financing is for infrastructure development—transport, water, and urban development. IDA is also funding projects in health and HIV/AIDS, and private sector

development. The Poverty Reduction Support Credit series has provided the overall policy reform framework. The IDA portfolio is supplemented by several grants. A Fast Track Initiative (FTI) grant supports primary education. A Global Partnership on Output-Based Aid grant supports a public-private partnership to replace the country's 50-year-old main public hospital in Maseru through a joint undertaking with the *International Finance Corporation (IFC)*, the transaction adviser for this project. A pioneering initiative, the project seeks to provide high-quality health care services to public patients at an affordable cost to the Government. IFC has also provided technical assistance on private sector development in tourism and export promotion.

66. The *Multilateral Investment Guarantee Agency's (MIGA)* portfolio consists of two guarantees totaling US$10 million in gross and net exposure in the services sector.

C. Principles of Engagement

67. The CAS follows three guiding principles: partnership and alignment with Government strategic priorities, leveraging of resources for greater impact, and selectivity.

68. *Partnership and alignment with Government strategic priorities.* The Bank's engagement with Lesotho is demand driven and builds on a strong relationship with the Government. In July 2009, the Prime Minister and Cabinet invited a Bank team to discuss a series of Policy Notes prepared by the Bank on how to improve Lesotho's competitiveness and make its economy more resilient during a period of a global economic downturn.[23] That discussion provided a framework for the CAS, opened new opportunities for engagement, and ensured close alignment of the Bank's program and Lesotho priorities.

69. This CAS benefited from extensive consultations with stakeholders in the country. Consultations, organized through two major workshops (at the onset of the CAS in September 2008 and after the upstream review in March 2010) were attended by more than 150 participants—Government officials and representatives of academia, the private sector, and civil society. Participants supported the CAS strategic focus and provided their insights on Lesotho's social challenges, growth potential, and the ways the Bank could better assist the country. The GOL has endorsed the CAS's strategic focus and program. Annex 3 describes the consultation process in more detail. The CAS aims to continue strengthening the partnership with the Government and civil society through policy dialogue informed by analytic work and through the involvement of civil society in project implementation. The Bank will strengthen its communication strategy to improve its dialogue with state and non-state actors.

70. *Leveraging of resources for greater impact.* The CAS will continue to play a catalytic role in leveraging other donor resources and building effective collaboration with development partners. It will build on the comparative advantages of development partners to complement IDA resources, particularly for large infrastructure projects; to scale-up successful IDA and other donor projects; and to provide technical assistance to strengthen

[23] The one-day seminar with the Cabinet, titled "Reshaping Lesotho's Position in SACU to Meet the Challenges of Sustained and Shared Growth," considered four issues: fiscal challenges and options for reform; effective use of public resources, particularly for capital expenditure supporting growth; agriculture—challenges and directions for agribusiness; and realizing FDI to diversify Lesotho's exports .

Government capacity to use donor funds effectively. The CAS also seeks to achieve maximum synergy among interventions by the Government, World Bank Group, and other development partners by seeking complementarity across sectors and interventions, including lending, grants, and AAA.

71. *Selectivity*. Because IDA's allocation is small relative to Lesotho's needs, the CAS strives to be selective in the number and choice of lending instruments, applying four selection criteria to new operations: strong Government ownership and commitment, improved governance and accountability mechanisms in the sector to support sustainability, cooperation with development partners, and past success that can be scaled up. In line with the latter, and taking into account the lesson from the CASCR that sustained engagement in a sector is important for success, the CAS envisages additional financing for projects in sectors such as water and transport that have made good progress in institution building and need to consolidate achievements to enhance sustainability. The principle of selectivity will also be reflected in a new approach to the AAA program, which will be more focused and better coordinated than in the past. This approach is described in the section on the IDA program.

D. Strategic Areas of Engagement

72. The FY2010–14 CAS seeks to assist the Government in addressing its short-term needs to deal with the sharp decline in SACU receipts and improve social development indicators. It will also work with the Government to enhance competitiveness and foster private sector–led growth over the longer term. To achieve these objectives, the Government and the Bank have agreed that the CAS would focus on three areas of engagement that are fully aligned with the country's Interim National Development Framework:

- Fiscal adjustment and public sector efficiency.
- Human development and service delivery.
- Enhanced competitiveness and diversification.

73. Applying the lessons of the previous CAS, this CAS will embed institutional strengthening and capacity development in all interventions, including IDA credits, AAA, technical assistance, knowledge sharing, and development partnerships. Project design will be simplified and tailored to institutional capabilities. A Governance and Capacity Assessment Study will be conducted early on to detect governance weaknesses, institutional and capacity constraints, and bottlenecks that can inform the Bank program. The Bank will support demand-side governance through involvement of non-state actors to the extent possible in preparation and implementation of the Bank program.

74. The World Bank Group will follow the guiding principles of the Bank's Regional Integration Assistance Strategy (RIAS) to assist Lesotho in taking advantage of "win-win" possibilities in the regional context created by specialization and higher efficiency levels not accessible through the national development programs. To address the regional challenges of Lesotho (e.g. HIV/AIDS, TB), the CAS will rely on country-specific as well as regional initiatives be it AAA, knowledge sharing or the institutional complementarities of the neighboring countries.

E. Proposed IDA program

75. Lesotho's IDA envelope for FY2010–14 is indicative and assumes that country performance will improve. The CAS covers the last two years of IDA15 and the full three years of IDA16. The indicative IDA15 allocation is approximately US$71 million (SDR44.8 million, including SDR20 million in grants and SDR24.8 million in credits) and US$15 million from the Crisis Response Window. US$55 million has already been committed in FY2009 and FY2010. The indicative IDA16 allocation is assumed to be approximately US$28 million a year. The proposed IDA program (lending, grants, and AAA) is presented in table 2.

76. The IDA envelope is small relative to the country's needs. Therefore, as discussed before, the Bank will seek to leverage other donor resources and tap into supplemental sources of financing, such as grant facilities and trust funds. The program will also be delivered in partnership with IFC. To enhance the effectiveness of Bank assistance, the CAS will rely on synergies among lending, technical assistance, and analytical work to be delivered in partnership with the Government, other development partners and the Bank team, which itself will work as a one well coordinated team. In line with this, the policy reform agenda supported by the Poverty Reduction Support Credits (PRSC) series, will serve as an umbrella for other lending operations.

77. IDA lending will be complemented by a strong, demand-driven AAA program, which will follow a new approach. The AAA program will be developed with the Governance and Capacity Study as the centerpiece with other tasks, such as Public Expenditure Review and other AAA, being parts of the umbrella activity. The AAA studies are expected to be mutually reinforcing. This will allow the analytical studies to be prepared in an integrated manner, using the political economy angle, including strengthening the demand for good governance, in all Bank activities. It will also help the team to better integrate the sectoral analytical work under a common agenda. To illustrate this approach, the Public Expenditure Review will be prepared in close cooperation with the GOL and will discuss strategic expenditure choices and the Governance and Capacity Study will assess governance constraints and capacities to implement these choices. Other studies, e.g., the Post-basic Education Study and Poverty and Gender Assessment, will be informed by these two studies. The Bank will pay greater attention to dissemination of AAA to large audiences and will use it as a tool in strengthening communication with state and non-state actors in Lesotho.

78. The CAS envisages some degree of flexibility to address the complexity of the current challenges and the need to adjust to changing circumstances. CAS implementation will be reviewed annually together with the GOL to assess progress and propose necessary adjustments to the Bank program and strategic approach. A CAS Progress Report will be prepared at mid-term or even before then if deemed necessary. Projected lending in the outer years (FY2013 and FY2014) will be reviewed at the time of the CAS Progress Report and may be adjusted depending on IDA allocations and progress toward CAS objectives. The IDA portfolio performance will also be reviewed periodically and projects will be restructured as needed and freed up resources will be redirected to emerging priorities.

Table 2: World Bank Program for Lesotho, 2010–14 CAS (US$ million)

	2010	2011	2012	2013	2014
Lending	HIV/AIDS **($5)**		Human Development Project **($5)**		
	Poverty Reduction Support Credit II (PRSC-II) **($25,** incl. **$10** from IDA CRW)	PRSC-III **($15)**	PRSC-IV **($15)**	PRSC-V **($15)**	PRSC-VI **($15)**
	Additional Financing Integrated Transport Project **($15,** incl. **$5** from IDA CRW)		Additional Financing Water Sector APL-2, **($10)**		Maseru Urban Development Project **($15)**
		Agriculture Development Project **($10)**		Infrastructure Development **($10)**	
Total IDA	**$55**	**$25**	**$30**	**$25**	**$30**
Grants	FTI II **($20)**		FTI II **($10)**		
Non-lending	County Economic Memorandum, Policy Notes	Public Expenditure Review	Maseru Urban Development Study	County Economic Memorandum	
	Investment Climate Assessment	Governance and Capacity Study	Technical assistance statistics	Poverty and Gender Assessment	
	Report on the Observance of Standards and Codes Accounting and Audit	Post-basic Education Study	Technical assistance in public financial management		

79. Effective approaches to promoting gender equity will be mainstreamed into the Bank's program. To maintain gender parity in primary education, the Bank program will pay special attention to addressing the issue of primary school enrollment related to "herd boy" syndrome, where boys drop out from school to tend livestock. In health the Bank will support GOL to address the critical issue of maternal and newborn morbidity and mortality. As women continue to participate in the workforce, the Bank will support the GOL in expanding training opportunities with a focus on women under the Private Sector Competitiveness and Diversification Project. Finally, the Bank's AAA program will look into gender inequality from different angles be it access to tertiary education or poor governance and institutions that often take higher toll on women. In FY2013 the CAS envisages a Poverty and Gender Study to take stock of poverty reduction and gender equity.

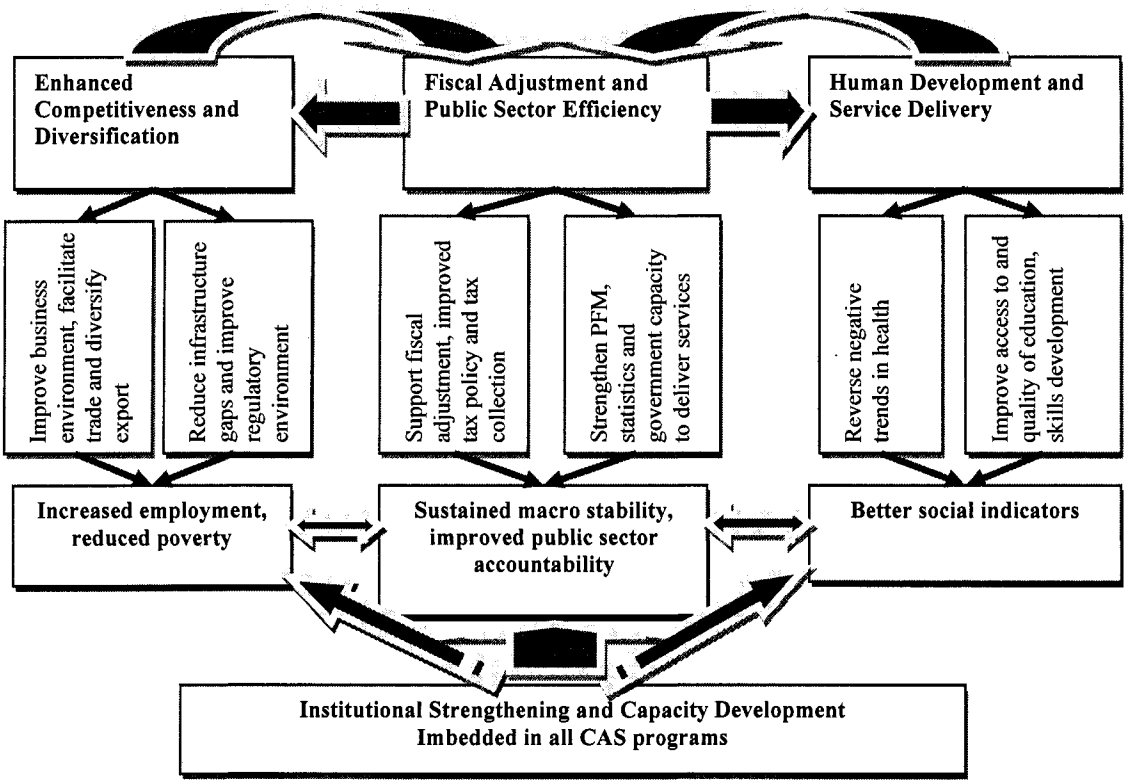
80. The Bank expects that positive and timely implementation of the CAS program will pave the way for Lesotho to move to blend status under the next CAS. In the meantime, Lesotho can benefit from IBRD financing through enclave projects, as was done in financing the first phase of the Lesotho Highlands Water Project.

F. CAS program and results

81. The Bank will focus on specific achievements (outlined in the Results Matrix) in areas considered critical for success following an approach of *strategic incrementalism*. Given the difficult nature of the transformation through which the country is moving, achieving visible results likely will take time. Therefore, the focus will be on achieving specific modest outcomes in key strategic areas which can then be built on over time.

82. The CAS results framework is organized in six results clusters, with attention to some early results to build momentum for reform. Figure 5 illustrates the CAS areas of engagement, results clusters, and potential impact of the Bank's program. Outcomes in the three areas of engagement are expected to reinforce and complement each other. The CAS will support Lesotho in unleashing potential for private sector growth with the focus on improved business environment for FDI and local entrepreneurship development. It will also assist in prioritizing the budget spending and increasing public sector efficiency to avoid any major negative impacts of the fiscal adjustment on critical public services important for human development and longer term growth. In turn, improved business environment will allow expanding the tax base and increasing non-SACU budget revenues in the long run, facilitating the fiscal adjustment. Better social outcomes will enhance labor force competitiveness and facilitate sustainable growth. Special attention will be given to ensuring that the needs of the most vulnerable groups of population, especially women, are taken into account, particularly during the period of fiscal consolidation.

Figure 5: CAS Areas of Engagement, Result Clusters and Impact



i. Fiscal Adjustment and Public Sector Efficiency

83. To help Lesotho make the necessary fiscal adjustments in response to the sharp decline in SACU revenues, the World Bank Group will support the Government's efforts to curtail budget spending, improve public sector performance and the efficiency of resource use. The Bank's engagement will be aligned with the key priorities of the Government's Public Sector Improvement and Reform Program.

84. World Bank Group assistance in this area is grouped into two results clusters: fiscal adjustment and increased public sector efficiency (results cluster 1) and stronger public financial management, statistics, and institutional capacity (results cluster 2).

Results Cluster 1: Fiscal Adjustment and Increased Public Sector Efficiency

Long-term objectives	Results/outcomes at end of fiscal 2014
Undertake fiscal adjustment to ensure macro stability	• Non-SACU revenues, including grants, increased above 27 percent of GDP • Wage bill as share of GDP reduced
Use public resources effectively	• Reprogrammed capital expenditures and improved capital budget execution • Improved selection of investment projects based on the new project cycle management process

85. The CAS will support the Government's efforts to develop options to address the decline in SACU revenues. To assist with fiscal consolidation, an expanded Poverty Reduction Support Credit (PRSC) series will help to close the financing gap resulting from the decline in SACU receipts by supporting policy reforms and providing additional resources. The PRSC series will accompany expenditure restructuring into the medium term, supported by a programmatic Public Expenditure Review prepared by the Bank and the Government. The CAS emphasis on improving the business and investment climate is expected to expand the tax base in the longer run.

86. With Government spending already high and prospects for new spending limited, public investments need to be prioritized. The CAS will support Government efforts to reprogram capital expenditures, directing resources into investments and programs to enhance growth and development. The CAS will focus on strengthening institutions and removing capacity constraints that have slowed capital expenditures (only an estimated 72 percent of capital appropriations have been used in 2009/10). The CAS will support the revival of the Project Appraisal Committee and provide technical assistance to strengthen project cycle management across the Government. A joint team with World Bank Institute will train officials in critical areas identified by the authorities, including project management, contract management, procurement and financial management, and leadership.

87. The Bank will support Lesotho's effort to better protect poor and vulnerable groups of population through analysis of social protection expenditures, social safety net targeting and coverage, efficiency, and institutional arrangements. A resultant set of policy recommendations will feed into Government effort to develop a comprehensive social

protection strategy for Lesotho. The Bank will also engage with other development partners to assist Government efforts to address the needs of orphans and vulnerable children.

Results Cluster 2: Strengthen Public Financial Management, Statistics, and Institutional Capacity to Deliver Better Services

Long-term objectives	Results/outcomes at end of fiscal 2014
Improve policy-based budgeting, financial reporting, external audit, and oversight	• Improved quality of the sector strategies and Budget Framework Papers • Timely and better quality financial statements • Timely and thorough legislative scrutiny of external audit reports
Improve availability and quality of data to underpin decision making	• On-track implementation of the National Strategy for Development of Statistics action plan

88. With expenditures constrained over the medium term, to build institutional capacity to deliver services and improve public sector governance, the CAS will focus on three areas that are reducing the quality of outcomes and the efficiency of budgetary expenditures: bringing transparency, accountability, and credibility to the budget; introducing policy-based budgeting and improving the statistical system; and upgrading public investments. With support from the World Bank (PRSC and technical assistance) and other development partners, work is under way in areas from policy design to procurement and implementation. The work emphasizes training in procurement, accounting, and financial management based on an upgraded qualification framework.

89. The CAS supports a public financial management reform agenda to improve budgetary outcomes through fiscal discipline, strategic allocation of resources, and efficient service delivery. To track progress in the Public Service Improvement and Reform program, the Bank and other development partners will use Public Expenditure and Financial Accountability assessments.[24] The emphasis will be on improving alignment between budgetary allocations and national priorities, improving reporting and transparency, modernizing procurement practices, and developing a culture of audit. A Report on the Observance of Standards and Codes accounting and auditing diagnostic exercise and follow-up capacity building activities will strengthen accounting and auditing infrastructure. Qualified personnel (including accountants and auditors), backed by high quality standards, monitoring, and enforcement, are expected to become safeguards against malpractice and instruments for improving governance and anticorruption programs, generating citizen confidence and trust in public institutions. The Bank team will mobilize technical assistance, including Institutional Development Fund grants, governance and anticorruption funding, and trust funds, to support Government capacity building and improve governance. The Bank and other development partners are considering a basket fund to support public financial management reforms.

[24] The Public Expenditure and Financial Accountability (PEFA) program is financed jointly by the World Bank, European Commission, and the UK Department for International Development.

ii. Human Development and Service Delivery

90. During the CAS period, the Bank Group will assist Government efforts to enhance human development. Bank Group engagement in Lesotho in human development and service delivery has covered a broad set of interventions in health and HIV/AIDS, water, education, and skills development targeting improved access, equity, and quality of services. Skills development has been progressing well, but social indicators have not improved, signaling that more work lies ahead.

91. World Bank Group assistance in this area is grouped into two results clusters: reversing negative trends in health and improving access to services (results cluster 3) and building skills to enhance competitiveness (results cluster 4).

Results Cluster 3: Reverse Negative Trends in Health and Improve Access to Services

Long-term objectives	Results/outcomes at end of fiscal 2014
Contain and reverse the incidence of HIV/AIDS	• Improved HIV awareness in the population • Increased coverage of effective HIV/AIDS interventions
Improve health sector outcomes and service coverage through deepen sector reform	• Increased access to hospital services • Improved quality of health services
Improve efficient use of public resources	• Improved budget execution in health
Increase access to clean, safe drinking water	• Increased number of people with access to improved sources of water

92. The CAS will support Government efforts to contain the incidence of HIV/AIDS by assisting the Government institutions responsible for the national HIV/AIDS response to access international funds, use them effectively, and measure their impact. Better coordination and implementation capacity are expected to increase disbursements and satisfactory implementation of subprojects financed through the Global Fund to Fight AIDS, Tuberculosis, and Malaria grant. Prompt evaluation will permit development partners to adjust their approaches as needed. Although the Bank's contribution in resources is small, it can have a major impact by boosting the effectiveness of the substantial resources available from other development partners. The CAS seeks to strengthen the capacity for implementing the HIV/AIDS Strategic Plan and scaling up effective HIV interventions. In addition, the CAS results will be reinforced through implementation of the regional IDF grant (Regional Capacity Building and Knowledge Sharing in Strengthening Health Systems), which includes capacity building support to Lesotho on TB lab strengthening.

93. The CAS will continue assisting Lesotho's efforts to increase access to hospital services and improve their quality, comply better with health service standards, and reduce post-operative infections. Progress will be measured through periodic surveys of client satisfaction. IDA and IFC are helping the Government establish a public-private partnership to build and operate Lesotho's new National Referral Hospital, which will serve the bulk of the population. Better management practices are expected to improve service delivery and, complementing other efforts such as the fight against HIV/AIDS, should result in better health outcomes. The Bank will focus on strengthening the foundation for this public-private partnership through the ongoing grant under the Global Partnership on Output-Based Aid.

94. A complementary program that will contribute directly to better health outcomes is the Bank's ongoing support to increase access to potable water. As mentioned under results cluster 6 (below), the Bank will continue to implement phase 2 of the Water Sector Improvement Project, which is part of a multidonor-funded program to improve the supply of water to Maseru and nearby areas, and will support capacity building of an independent water regulator and continued strengthening of water sector institutions and the policy framework.

Results Cluster 4: Build Skills for Enhanced Competitiveness and Improve Incentives

Long-term objectives	Results/outcomes at end of fiscal 2014
Improve quality of primary education	• Improved teaching and schooling standards
Improve access to secondary education	• Increased secondary schools enrollment
Reform post-basic education to improve the development of appropriate and relevant skills for growth in the labor market	• Reform program in post-basic education prepared • New forms for funding of post-basic education piloted

95. The CAS will support Lesotho's efforts to improve the quality of primary education, boost enrollment in post-basic education, and better align higher education with labor market needs. The country's strategy is to deepen the reforms in basic education to improve quality, as measured by periodic examinations, and to increase access to secondary and tertiary education as more young people complete primary education. To improve primary education, the CAS intends to increase the proportion of classrooms that meet basic standards of adequacy and to upgrade teachers' qualifications through the multidonor Catalytic Fund Grant for the Education for All Fast Track Initiative (FTI) managed by the Bank. This operation is expected to lay the foundation for a sector pool fund that will channel donor funds to the sector strategy.

96. The Bank program will continue to emphasize skills development and capacity building so that the education and private sectors can better respond to labor market needs. The CAS will support activities to improve the quality of university education and technical and vocational training standards. The Bank will also assist in the process of reforming post-basic education so as to make it more consistent with the economy's growth path, less expensive, and more financially accessible for all. This work will be undertaken initially through AAA (the Post-Basic Education and Growth Study), which will inform a proposed education project later in the CAS period The CAS will also evaluate the experience of the public-private partnerships in the skills development program for the textiles and garments industry, supported under the Private Sector Competitiveness and Economic Diversification Project and explore opportunities to expand this program

97. In partnership with the World Bank Institute and the Government of Lesotho, the Bank will customize its knowledge and learning program to enhance Lesotho's capacity in selected areas on a pilot basis. A governance and capacity assessment will examine capacity constraints that limit sustainable growth. The Bank will work with Lesotho to develop and implement a strategy to attract and retain qualified members of the diaspora from the region and globally. The CAS will also support the Government in establishing incentive structures to retain qualified staff and attract those who have left. Through a proposed Institutional Development Fund grant, the Bank's Africa Region Diaspora Team will work closely with the Government to develop and implement its strategies for engaging the diaspora in selected sectors, such as health and education.

iii. Economic Competitiveness and Diversification

98. The CAS will assist Lesotho to take advantage of its competitive labor costs, proximity to South Africa's modern transport infrastructure, and duty-free access to regional markets. The CAS program targets two result clusters: improving the business environment, trade facilitation, and export diversification (results cluster 5) and reducing the infrastructure gap and improving capacity to regulate infrastructure services (results cluster 6). These efforts will unleash the growth potential of the country and enable the Maseru area to attract more investment. CAS support for a better business environment, improved interface with South Africa, access to factory shells for new business, reduced transportation costs, and increased availability of skills will all contribute to building Lesotho's economic potential.

Results Cluster 5: Improve the Business Environment, Trade Facilitation, and Export Diversification

Long-term objectives	Results/outcomes at end of fiscal 2014
Increase domestic and foreign investment	• Strengthened legal framework for private sector development and Doing Business Indicators improved (Company Bill and Industrial Licensing Bill approved and under implementation) • Improved industrial infrastructure and new factory shells developed • Fully functional One Stop Business Facilitation Center as a single administrative unit
Facilitate regional trade	• Computerized single-window and customs clearance system established
Increase agriculture production and marketing	• Improved access to all season roads in targeted rural areas • Increased private investments in agribusiness • Improved productivity and diversification from crop production and livestock on pilot basis

99. The CAS will support improvements in the business environment, economic diversification and the capacity of small and medium-size enterprises through the ongoing Private Sector Competitiveness and Economic Diversification Project, PRSC series, and targeted AAA. Strengthening the legal framework will be a priority, along with building capacity to streamline the regulatory environment and implement the reforms. These steps should help Lesotho improve its Doing Business ranking in at least four categories: trading across borders, setting up a company, accessing land, and protecting investors. The CAS also will support measures to ease access to land and promote investment in industrial property development. The CAS will support strengthening the performance of the Land National Development Corporation and Basotho Enterprises Development Corporation and the charting of a path to a stronger and more effective role for both.

100. IFC will explore ways to facilitate access to finance for micro, small, and medium-size enterprises in Lesotho and will strengthen ongoing discussions with stakeholders including local banks, the Government, and multilateral agencies. Subject to economic viability and identification of appropriate partners, IFC's potential interventions in Lesotho over the CAS period will include the following:

- *African Micro, Small, and Medium Enterprise Program*, to support financial institutions in rapidly and profitably ramping up banking services for these enterprises, while maintaining good asset quality.
- *Microfinance investment*, to identify and invest in a commercial microfinance institution.
- *Small and Medium-size Enterprise Risk Capital Fund*, to replicate in Lesotho IFC's successful partnerships with fund managers focused on small and medium-size enterprises in Kenya and Madagascar, subject to the underlying proposed fund being commercially viable.
- *Small and medium-size enterprise management solutions*, to improve the business performance and competitiveness of firms: the *Small and Medium-size Enterprise Toolkit*, a web-based solution offering free business management information and training to firms in accounting and finance, business planning, human resources, marketing and sales, operations, information technology, and other resources to help entrepreneurs start, finance, formalize, and grow their businesses; and the *Business Edge*, a comprehensive set of practical and flexible management training products and services to improve enterprise performance, including an international standards curricula tailored to management training needs and local markets for small and medium-size enterprises.

101. The CAS will support a trade and diversification agenda to develop the domestic private sector and increase FDI. The strategy will encourage collaboration between the Lesotho Revenue Authority and the South African Revenue Service, opening new opportunities for trade and investment facilitation. A new area for Bank support, this is a key component of Lesotho's regional integration agenda designed to lower trade costs and expand the private sector. To facilitate trade between Lesotho and South Africa, customs infrastructure at the Maseru Bridge and Maputsoe can be transformed into a one-stop border for processing applications from both agencies by establishing a computerized single window and customs clearance system and reducing infrastructure constraints. If successful, this partnership could become a model for the SACU/SADC region. To support this undertaking, the Bank will provide financing through the recently launched Trade Facilitation Facility managed by the International Trade Department and implemented by AFTFE.

102. Responding to the Government's request, the CAS will step into a new area of engagement in Lesotho with potentially high social returns and impact on wealth creation: agriculture and rural development. The focus would be on increasing income and employment opportunities in smallholder agriculture by boosting crop diversification through attracting private investments and enhancing the productivity and marketability of agricultural products and by encouraging sustainable land management. Support would come from a World Bank–International Fund for Agricultural Development co-financed program for investments in productivity improvements, agricultural technology, sustainable land management, value chains, and market access.

103. In the area of environment and biodiversity protection the Bank will be prepared to respond to potential GOL's interest in mobilizing resources as part of GEF 5 to continue its biodiversity activities.

Results Cluster 6: Reducing the Infrastructure Gap and Improving Capacity to Regulate Infrastructure Services

Long-term objectives	Results/outcomes at end of fiscal 2014
Strengthen Government capacity to regulate infrastructure services	• Regulatory decisions based on strong economic analysis • Mandate of Lesotho Electricity Authority expanded to cover water regulation
Improve the road network	• Improved quality of national road network • Reduced average travel cost to social services and markets in targeted areas
Increase the availability of water for domestic and industrial use	• Increased quantity of safe, bulk water supplied to Teyateyaneng

104. The CAS will continue to support the road and transport sector to consolidate progress in improving key transport networks that open new corridors. The CAS will also support upgrading selected rural roads to improve access to isolated areas and deliver a better managed and more affordable transport system. These programs are expected to reduce travel cost to social services and markets. The Bank will continue to support institutional strengthening of the sector, including the recently established Roads Directorate and the Road Maintenance Fund, and efforts to achieve sustainable financing for road maintenance through the ongoing Integrated Transport Project and proposed additional financing.

105. The Bank will continue its engagements in the water sector to meet the growing demand for good quality water from industrial users in the Maseru area and to increase Lesotho's water exports to South Africa. The Bank will follow a programmatic approach involving the Government and development partners through the Ministry of Natural Resources, the Commissioner of Water, and the Water and Sewerage Authority. The instruments are the ongoing water projects and a proposed new operation for the Maseru area. The CAS program will continue to provide technical assistance for the development of regulatory tools and other capacity development for the water and electricity regulator. In addition, the Bank is prepared to explore the possibility of a new IBRD enclave project in support of the second phase of the Lesotho Highlands Water Project.

106. Finally, the Bank will provide support to the Maseru City Council to develop an effective urban planning and transport system. Under the Integrated Transport Project, an institutional and financial overview of urban planning and management activities will be carried out, focusing on transport services to Maseru in the short and long terms. The Maseru Urban Development Study will identify the gaps and bottlenecks expected to emerge as the city grows and will propose solutions, including housing development and better urban services.

G. Results Monitoring and Management

107. The CAS results matrix developed in partnership with the Government of Lesotho tracks progress in the main areas of engagement. The Bank team will track progress through annual impact reviews at the time of the joint GOL/Bank CAS review, using a recently piloted Country Program Results Monitoring tool. The Bank teams will work directly with Government agencies to track results and identify factors affecting them. The CAS Progress

Report will reevaluate the results framework in light of implementation, exogenous developments, and adjustments to the Bank's program.

108. In addition, the CAS will help the Government of Lesotho strengthen its statistical capacity. The Bureau of Statistics has begun to develop a National Strategy for the Development of Statistics based on the Paris 21 Principles. The Bank supports these efforts through the PRSC series and will complement them with self-standing technical assistance and a potential project in cooperation with other development partners. The 2006 census provided solid benchmarks for tracking progress toward development outcomes, particularly on social issues, for which results-tracking has been weak. To further address the issue of data inadequacy to enhance the decision making, the Bank jointly with other development partners stands prepared to assist in strengthening capacity for collecting regular and better quality data and developing tools to analyze it.

H. Development Partners

109. Strong development partnerships will continue under the CAS. Donor coordination, alignment, and harmonization have improved since the formation in 2005 of the Development Partners Consultative Forum, co-chaired by the United Nations Development Program and Irish Aid. The forum includes resident and nonresident development partners. The resident development partners are the European Commission, UN agencies, World Bank, Peoples Republic of China, German Technical Cooperation (GTZ), Irish Aid, Government of Libya, U.K. Department for International Development, U.S. Government, and French and Danish Honorary Consuls. The nonresident development partners include the African Development Bank, the International Fund for Agricultural Development, and Japan, among others. The forum seeks to improve communication and promote transparency between development partners and the Government by strengthening aid coordination, promoting harmonization, and supporting the Government in strengthening ownership of development processes as set forth in the Paris Declaration and Accra Agenda of Action. The forum enables partners to discuss current and planned activities, coordinate programs, and promote efficient and effective delivery of projects to benefit Lesotho. The donor activities mapped along the CAS areas of engagement are captured in annex 4.

110. World Bank partnerships with other donors will build on successful operations jointly financed with other donors, such as the Integrated Transport Project (with the European Commission) and the US$300 million Metolong Dam project (with the U.S. Millennium Challenge Corporation, the European Investment Bank, the Arab Bank for Economic Development in Africa, the OPEC Fund for International Development, the Kuwait Fund, the Saudi Fund, the Republic of South Africa, and the Government of Lesotho). The Bank's US$25 million credit for the Metolong Dam Program supports critical environmental and social safeguards and finances the construction of a transmission main to the town of Teyateyaneng. The Bank's HIV/AIDS Technical Assistance Project, a US$ 5 million IDA grant, helps to fill the capacity gap impeding implementation of the HIV/AIDS National Strategic Plan.

111. Under the CAS, IDA funds will be used to catalyze donor resources through several instruments, including joint donor budget support with the African Development Bank, UK Department for International Development, and the European Commission; a joint agricultural project with the International Fund for Agricultural Development; and sector-

wide approaches (SWAps) with Irish Aid. The World Bank Group will explore possibilities for other operations to be prepared and implemented in close partnership with donors, building on successes and lessons learned.

VI. RISKS

112. The Bank program in Lesotho faces *substantial risks* stemming from three sources: the difficult scope and scale of the required adjustment; limited implementation capacity and weak institutions; and weak demand for good governance. The issue of data inadequacy is a serious constraint to effective monitoring of the program performance that exacerbates the risks. The CAS program has been designed to help Lesotho sustain reforms while mitigating these risks.

a) The sharp decline is SACU revenues will affect the macroeconomic framework and the capacity of the GOL to carry out its development agenda. The GOL will confront the need for substantial adjustments over the medium term which will reduce the preponderant role of the government. Effectively, a new development paradigm will need to be put in place, in which the role of the public sector is limited to the efficient provision of key public services and growth is generated by the private sector. This adjustment will necessarily take time and with general elections scheduled for 2012, there is a risk that the needed reforms may not be sustained. The GOL is aware of this risk and views the current situation as an opportunity to address long-standing structural weaknesses. Lesotho's success in the past in affecting such shifts offers hope that this risk can be managed. The CAS, for its part, will assist the GOL by providing additional resources within an agreed fiscal framework, and providing key support in areas constraining this adjustment. Jointly with the International Monetary Fund and other development partners, the Bank will work with the GOL to develop options, ranging from fiscal consolidation and improved tax collection to greater mobilization of external resources, including eventually from reaching IBRD status. To expand the tax base, the CAS supports the GOL's effort to penetrate new markets, especially regional markets, and to position Lesotho as a regional hub for FDI.

b) The GOL's limited capacity and weak institutions present an important risk to CAS implementation, while its limited capacity for political follow-through can serve to reduce impact. To address this risk, the Bank has aligned the CAS program with GOL priorities and, through program selectivity, will try to avoid overwhelming the GOL with too ambitious an agenda. In addition, all CAS activities focus on institutional strengthening and capacity building, taking account of a key conclusion of the CASCR. The Bank intends to continue working with development partners so that their joint and complementary efforts leave in place self-sustainable institutions that can carry on the sector reform agendas.

c) Governance in Lesotho remains relatively weak, and communication between the Government and citizens is poor. The capacity building and institution strengthening efforts built into the CAS program will be complemented by assistance to improve dialogue between the Government and the citizenry, especially by fostering discussion around AAA and program designs. In particular, the envisaged AAA program with the Governance and Capacity Assessment at the center will provide

specific recommendations as to how to enhance the bottom up accountability. The Government's initiative to improve the citizen's voice in service delivery, the Service Delivery Agenda, and its commitment to engage in policy dialogue with the non-state actors for the preparation of the National Development Plan represent encouraging steps toward bottom up accountability. The coordinated AAA program will explore how the new tools for monitoring and evaluating public sector performance in service delivery could be used to enhance the dialogue between the Government and citizens. Through the AAA program, the Bank jointly with development partners will leverage new data collection and dissemination to enable citizens to more effectively communicate and hold their government accountable for improving public spending performance in delivering broad public goods.

113. Any or all of the above risks can undermine the achievement of the CAS objectives. However, the GOL is cognizant of the changes required and, given Lesotho's past history of effecting major transformations, these risks, while substantial, are manageable.

Annex 1: CAS FY10-14: RESULT MATRIX

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
Area of engagement 1. Fiscal Adjustment and Improved Efficiency of the Public Sector				
Results Cluster 1. Fiscal Adjustment and Increased Public Sector Efficiency				
1.1. Undertake fiscal adjustment to ensure macro stability	Macro and fiscal vulnerability to fluctuations in SACU customs receipts necessitates significant fiscal adjustments in face of SACU revenues shortfalls	Non-SACU revenues, including grants, increased as share of GDP *Baseline: 27% in 2009* *Target: 30% in 2014* Wage bill reduced as share of GDP *Baseline: 18% in 2009* *Target: 14% in 2014*	A wholesale revision of tax rates, charges and fines undertaken and implemented On-going reform of Lesotho Revenue Authority completed, including computerization of income tax returns, training of tax auditors etc. Measures to contain the wage bill (reducing size of public service, eliminate vacant posts etc.) developed and adopted	**Ongoing Projects**: PRSC II **Non-lending** PER **Pipeline:** PRSC III, IV **Other Partners** DFID, EU
1.2. Ensure effective use of public resources	Inefficient use of budgetary resources Substantial under-spending in the capital budget	Reprogramming of capital expenditures on track and capital budget execution improved *Performance Indicator:* Capital budget execution *Baseline: 70% in 2009* *Target: 90% in 2014* Improved selection of investment projects *Performance Indicator:*	Stock taken for the current portfolio of investment projects, and strategy to reprogram and improve implementation performance developed Project Appraisal Committee revived and new Project Cycle Management Process	**Ongoing Projects**: PRSC II **Non-lending** PER Policy Note, TA **Pipeline:** PRSC III, IV **Other Partners** DFID, EU

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
		% of new investment projects (in number) follow the new PCMP *Baseline: 0% in 2009* *Target: 50% in 2014*	(PCMP) adopted	
Results Cluster 2. Strengthen PFM, statistics and institutional capacity to deliver better services				
Public Sector Reform 2.1. Improve policy based budgeting, financial reporting, external audit and oversight	Significant weaknesses in budgeting, budget execution and reporting, external audit and scrutiny	*Public Finance Management performance improved through:* Stronger multi-year budgeting perspective as measured by: • Improved quality of the sector strategies and Budget Framework Papers (BFP) • Enhanced consistency between sector strategies and aggregate fiscal forecasts *Performance Indicator: PEFA PI-12 rating* *Baseline: C+ in 2009* *Target: B in 2014*	Sector strategies and BFPs fully costed and consistent with MTEF Audit Bill and Public Financial Management and Accountability (PFMA) Bill adopted Roll-out of the IFMIS advanced to cover all ministries	**Ongoing Projects**: PRSC II IDF PFM Qualification System **Non-lending** Accounting and Audit ROSC **Pipeline:** PRSC III, IV **Other Partners** PFM Basket Fund (to be explored with development partners)
	The GOL progress on a number of recently introduced sophisticated PFM reforms constrained by limited institutional capacity. These reforms have yet to result in significant improvements in PFM outcomes	Timely and better quality financial statements *Performance Indicator: PEFA PI-24, PI-25 rating* *Baseline: D in 2009* *Target: C in 2014* Timely and thorough legislative scrutiny of	Capacity of the MoF to prepare annual financial statements and in-year budget execution reports strengthened Capacity of the Public Accounts Committee to	

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
		external audit reports *Performance Indicator: PEFA PI-28 rating* *Baseline: D+ in 2009* *Target: C in 2014*	review audit reports strengthened	
2.2. Improve availability and quality of data to underpin decision making	Statistics capacity inadequate to underpin informed policies and decision making	Implementation of the National Strategy for the Development of Statistics (NSDS) Action Plan on track *(Yes/No)* *Baseline: No NSDS Action Plan in 2009* *Target: NSDS Action Plan developed and under implementation in 2014*	National Strategy for the Development of Statistics Action Plan developed and approved	**Ongoing Projects**: PRSC II **Non-lending** TA on NSDS **Pipeline:** PRSC III, IV **Other Partners** EU
Area of engagement 2. Human Development and Improved Service Delivery				
Results Cluster 3. Reverse negative trends in health and improve access to services				
Health 3.1. Improved health sector outcomes and service coverage through deepened health sector reform	Inefficient and ineffective health spending that is not results-based Shortage of human resources Lack of incentive for good performance	Access to health care services increased *Performance Indicator:* Annual visits made to the new national referral hospital *(including the filter clinics)* *Baseline 164,624 in 2009* *Target: minimum 285,000 visits in 2014* *Quality of health services improved as measured by*: • percent of women using modern family planning method	Satisfactory progress in implementing the health reform strategy, including: • Public-Private Partnership (PPP) for Queen Elisabeth II Hospital in place • Performance-based contracts to NGOs piloted • Cash incentive scheme for community health workers piloted	**Ongoing Projects**: GPOBA Project, Results-based Health Financing **Pipeline:** Human Development Project **Other Partners** IFC Queen Elizabeth II Hospital Project

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
		Baseline: 35% in 2009 *Target: 40% in 2014* Improved efficiency in the use of public resources in health *Performance Indicator*: Budget execution rate *Baseline:85% in 2008* *Target: 90% in 2014*	Results-based financing introduced	
HIV/AIDS 3.2. Reverse the HIV epidemic, reduce incidence rate	Low awareness on HIV status of the population Weak coordinating capacity for multi-sector response; Weak implementation capacity to scale up those effective interventions that address the key drivers of the epidemic;	Improved awareness of population on their HIV status *Performance Indicators*: % of women and men aged 15-49 who received HIV test in last 12 months and know their results (UNGASS indicator 7) *Baseline: 6% in 2006* *Target: 50% in 2014* PMTCT coverage *Performance Indicator*: Coverage of people eligible for ART *Baseline: 36% in 2008* *Target: 60% in 2014*	NSP 1 successfully completed and NSP 2 under implementation. Implementation capacity to address HIV/AIDS epidemic in coordinated manner improved The number of sites providing ART treatment increased from 171 centers in 2009 to XXX in 2014	**Ongoing Projects**: HIV/AIDS TA Project **Pipeline:** Health Sector Project PRSC III, IV **Other Partners** IFC Queen Elizabeth II Hospital Project
Water 3.3. Increased access to clean, safe drinking water	Inadequate supply and distribution infrastructure given manufacturing and population pressures	Improved access to clean and safe water *Performance Indicators*: Percentage of population within program target areas with piped water supply	28 kms of pipeline laid and operational between the Metolong water treatment works and Teyateyaneng	**Ongoing Projects**: Water Sector Improvement Project, Phase 1 Water Sector Improvement Project, Phase 2

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
		Baseline: 50% in 2009 *Target: 65% in 2014*		**Pipeline:** Infrastructure Project **Other Partners** MCC, EIB, BADEA, OFID, Kuwait Fund, Saudi Fund
Results Cluster 4: Build skills for enhanced competitiveness and improve incentives				
Education and Skills Development 4.1. Improved quality of primary education.	Poor infrastructure at primary schools. High proportion of unqualified teachers especially in remote and/or difficult to access areas.	Improved teaching and schooling standards *Performance Indicators*: • percentage of classrooms meeting the national quality standards increased *Baseline:* 48% in 2008 *Target:* 53% in 2014 • percentage of qualified primary teachers *Baseline: 58% in 2008* *Target: 70% in 2014*	A de-concentrated approach to school construction that makes use of district tender panels for procurement, district firms for supervision of civil works, and targeting local small contractors introduced. Sustained operation of the Distance Teacher Education Program (DTEP) and the Thaba-Tseka teacher training campus.	**Ongoing Projects**: FTI 2 **Pipeline:** FTI 3 **Other Partners** FTI support via education pool fund (with Irish Aid)
4.2. Improved access to secondary education.	Limited capacity in secondary schools. Fees in secondary schools reduce access for the poorest.	Secondary schools enrollment increased *Baseline: 97,900 in 2007* *Target: 130,000 in 2014*	A three-year costed plan for education sector under implementation	**Ongoing Projects**: PRSC II **Pipeline:** PRSC III **Other Partners** JICA
4.3 Initiated reform in post-basic education to improve	Lack of vision on post-basic education sub-sectors and	Reform program in post-basic education prepared and	Stakeholder consultation on the nature of post-basic	**Ongoing Projects**: PRSC II

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
the development of appropriate and relevant skills for growth in the labor market	unarticulated provision of education and training. Higher education and TVET poorly matched to labor market needs	new forms for funding of post-basic education piloted *Baseline: No reform program in post-basic education in 2009* *Target: reform program in post-basic education prepared and proposals for new forms of funding the sub-sector piloted*	reform with government, public and private sector conducted Preliminary policy reform program drafted	**Non-lending** Post-basic education study **Pipeline:** PRSC III Human Development Project **Other Partners**
Area of Engagement 3. Enhanced Competitiveness and Diversification				
Results Cluster 5: Improve Business Environment, Trade Facilitation and Export Diversification				
Business Environment 5.1. Increased domestic and foreign investment through improved investment climate (against 130th ranking out of 183 countries, Doing Business indicators, 2010)	Weak and poorly organized private sector and ineffective public-private dialogue Slow pace of business environment reforms	Legal framework for private sector development strengthened and Doing Business indicators improved *Performance Indicators*: • Time taken to register a business is less than 14 days *Baseline: 40 days* *Target: less than 14 days by 2014* • Time taken to get an industrial license at the One Stop Business Facilitation Center is less than 14 days *Baseline*: 35 days	Company Bill and Industrial Licensing Bill approved and implementation on track Capacity of LNDC and BEDCO in supporting industrial development, improving business environment and supporting growth of MSMEs strengthened Companies registration incorporated into OBFC	**Ongoing Projects**: PRSC II PSCDP **Non-lending** TA post-ICA **Pipeline:** PRSC III, IV PSCDP add.fin. **Other Partners**

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
		Target: 14 days by 2014 Time to export reduced to less than 14 days *Baseline: 44 days*		
5.2. Facilitated trade region-wide	Inefficient customs clearance system	Customs clearance through implementation of Computerized Single Window and single customs clearance system improved *Baseline: two customs clearance processes at the border in 2009* *Target: single customs clearance process in 2014*	Collaboration between customs authorities of Lesotho and South Africa strengthened	**Ongoing Projects**: PRSC II Trade Facilitation Facility **TA** TA post-ICA **Pipeline:** PRSC III, IV PSCDP add.fin. **Other Partners**
Agriculture Development 5.3. Increased agriculture production and marketing	Poor road infrastructure makes it difficult to access markets, especially for smallholder farmers	Number of rural population with access to an all-season road (at project area: Mantsonyane-Lesobern) *Base line:500 in 2009* *Target: 15,000 in 2014*	XX km of rural roads constructed (TBD under ITP add. fin.) 34 km of rural roads rehabilitated	**Ongoing Projects**: ITP **Pipeline:** ITP add.fin. **Other Partners**
	Low grain yields (maize yields have fallen from 1.4t/ha, in the mid - 1970's to 0.45 -0.5t/ha in 2008-09). Low productivity from crop and livestock Lack of supplies of	Productivity and diversification from crop and livestock production through improved smallholder farming practices increased, on a pilot basis At least one private investor	Milestones TBD at project preparation stage	**Ongoing Projects**: **Pipeline:** Agriculture Development Project **Other Partners** IFAD

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
	agricultural inputs in many rural areas Excessive fragmentation and subdivision of landholdings	in the horticulture out-growers scheme (*Performance indicators TBD at project preparation stage to be reflected in CAS PR*)		
Results Cluster 6: Reducing the Infrastructure Gap and Improving Capacity to Regulate Infrastructure Services				
Infrastructure 6.1. Strengthen regulation of infrastructure services	Lack of regulatory tools and systems; no independent water regulator	Regulatory decisions based on strong economic analysis and rationale *Performance Indicator*: Quality of economic analysis underpinning regulatory decisions in the water and electricity sectors *Baseline:* Inadequate economic analysis for regulatory decisions, including tariff setting, in the water and electricity sectors *Target:* Regulatory decisions, including tariff setting based fully on strong economic rationale in the water and electricity sectors Mandate of Lesotho Electricity Authority (LEA) expanded to cover water regulation *Baseline:* Divided regulatory function between electricity	A financial and economic regulatory model for water and electricity sectors in place and used by the operators Regulatory accounting guidelines in place	**Ongoing Projects**: WSIP I, II PPIAF grant **Pipeline:** ITP add.fin. **Other Partners**

Country Long-Term Goals	Major Issues and Challenges	CAS Outcomes and Indicators	CAS Milestones	Bank Program and Partners
		and water *Target:* Regulation by contract in the water sector and regulatory agency for electricity sector		
6.2. Road network improved	Inadequate road network to meet the needs of competitive economy	Quality of national road network improved *Baseline: 27% good and 38 % fair in 2009* *Target: 39 % good and 46 % fair in 2014*	User fees cover 90% of routine and periodic maintenance needs Autonomous road sector management and Road Maintenance Fund performing as baselined with other African road funds	**Ongoing Projects**: ITP **Pipeline:** ITP add.fin. **Other Partners** EU
Water 6.3. Increased availability of water for the greater Maseru area for domestic and industrial use	Low capacity and financial resources to implement a large-scale infrastructure program	Quantity of safe, bulk water supplied to Teyateyaneng increased *Baseline: 1.5 megaliters/day in 2009* *Target: 3.5 megaliters/day in 2014*	28 kms of pipeline laid and operational between the Metolong water treatment works and Teyateyaneng Environmental and social safeguards program for the MDWSP completed.	**Ongoing Projects**: Water Sector Improvement Project Second Phase **Other Partners** US MCCA, Arab Funds

Annex 2: CAS COMPLETION REPORT

Country: Kingdom of Lesotho
Date of CAS: March 27, 2006
Date of Progress Report(s): None
Period Covered by the CAS-CR: FY2006-2009

I. Introduction

1. The Completion Report for the FY06 Lesotho Country Assistance Strategy (CAS) builds on contributions from the World Bank Country Team plus available documentation on projects, analytical work, and existing reviews. In addition, a Strategic Portfolio Review Note (2008) provided valuable insights that fed into the analysis. A 2008 management decision to produce a new CAS rather than prepare a CAS Progress Report meant that the results framework was not adjusted during implementation.

II. FY06–09 CAS: Background, Design, and Relevance

2. Over the 10 years prior to 2005, Lesotho underwent major economic transformations, and its economy grew at a rate faster than the rest of Sub-Saharan Africa (SSA). Garments went from being a nascent industry to being a major source of export earnings. The growth of this industry was aided in part by the 2000 African Growth and Opportunity Act (AGOA), which attracted foreign direct investment (FDI) from East Asia. The mining sector attracted FDI in response to rising world diamond prices and became one of the drivers of economic growth from 2000 onward. In addition, South Africa's investment in the Lesotho Highlands Water Project (LHWP) attracted large capital inflows during construction. Even if the project's long-term impact on the labor and goods markets was limited, water exports have become an additional source of revenue for the public sector. Strengthening the domestic economic base to produce for export markets helped reduce reliance on remittances from workers in South Africa. Until the late 1980s, remittances had amounted to 50 percent of national income. By 2005, they had dropped to 20 percent of national income. Overall, manufacturing and mining became dynamic sectors; but services stagnated, and agriculture declined.

3. At the time of the CAS design, despite these advances, Lesotho faced several major challenges:

- *Risks to economic growth.* By 2005 the stability of the international agreements that had been sustaining economic growth came under threat from (a) phasing out textile quotas under the World Trade Organization (WTO)'s Agreement on Textiles and Clothing (ATC); (b) the expected removal of AGOA provisions on third-country fabrics; (c) the decline in Southern African Customs Union (SACU) revenues following trade liberalization in the region, and (d) the likely effect on remittances of proposed changes to South African legislation covering immigrants. These risks called for caution regarding growth prospects and for concrete actions to improve competitiveness to ensure alternate sources of economic growth.

- *Vulnerability to the HIV/AIDS pandemic.* At 23 percent, in 2005 Lesotho posted one of the highest adult HIV/AIDS prevalence rates in the world, much higher than the average of SSA countries. Ineffective Government of Lesotho (GOL) and development partners' HIV/AIDS prevention programs contributed to the high incidence level. Besides the deleterious welfare consequences for the victims and their families, the estimates of expected long-term economic losses likewise were high. In addition, high HIV/AIDS incidence was having a high negative impact on overall health indicators. Life expectancy was decreasing.
- *High levels of poverty.* The limited information available during CAS preparation suggested that roughly two-thirds of the country's people were living below the poverty line (defined domestically). Most of these poor were living in rural areas. There, approximately 70 percent of the country's population derived their livelihoods from working on plots of land smaller than one hectare (ha) with declining productivity due to environmental degradation. The deteriorating performance of the agricultural sector gave reasons for concern.
- *Uneven access and quality of public services.* Human development indicators ranked Lesotho as 149 of 177 countries. In some sectors, such as primary education, Lesotho outperformed most other African countries. In other sectors, the country lagged them. This lag raised serious concerns about the effectiveness of public expenditure, especially when Lesotho's level of public expenditure equaled approximately 50 percent of its GDP.[25]

4. In 2005 the Lesotho authorities drafted a Poverty Reduction Strategy Paper (PRSP) in which they proposed ways to address these challenges. The authorities involved most of the country's key stakeholders and communities in the preparation of the strategy, which the government organized around three main pillars:

a. Employment and income generation through higher economic growth
b. Sharing the benefits of growth: health, education, and the environment
c. Improving governance and public service delivery.

The PRSP also identified three cross-cutting issues: HIV/AIDS, gender, and children and youth. In September 2005, the IMF's and the Bank's Executive Boards endorsed the PRSP.

5. The CAS aligned its strategic objectives with those of the three PRSP pillars and built the program of support around the perceived comparative advantage of the World Bank in Lesotho: "analytical strength and convening powers, combined with development finance and its ability to leverage other partners."[26] The resulting CAS was grounded on four strategic objectives:

a. Fight the HIV/AIDS pandemic
b. Establish sustainable pro-poor growth and job creation

[25] Lesotho receives the bulk of its public revenues from revenue-sharing of customs collections within SACU. South Africa collects and distributes the shares. Lowering external customs fees and duties within SACU affects Lesotho's fiscal position.
[26] Country Assistance Strategy for the Kingdom of Lesotho, March 27, 2006.

c. Improve human development outcomes
d. Strengthen decentralization, service delivery, and monitoring and evaluation (M&E).

As can be seen, the CAS followed the architecture of the PRSP but, to highlight the urgency of facing up to the epidemic, elevated the HIV/AIDS efforts from a crosscutting theme to a strategic objective.

6. The bulk of the results framework proposed by the CAS and summarized in a Results Matrix[27] relied on the contributions of then-active operations, which covered HIV/AIDS, health, education, infrastructure (water and electricity), and the environment. Table A1 presents the operations that were active at the time of the CAS preparation.

7. The proposed new operations under the CAS focused on development themes that had received less attention in the past, specifically: (a) economic growth and (b) management of public resources. Given the challenges that Lesotho faced and the authorities' emerging priorities, the shift in focus, particularly the emphasis on economic growth and competitiveness, was both timely and relevant. However, no major impact was expected during the CAS period because it was foreseen that getting the new programs off the ground would take the country and the development partners beyond the CAS timeframe.

8. The proposed analytic work under the CAS was consistent with emphasizing economic growth and diversification, improving management of public resources, and reducing poverty. However, due to the absence of supporting analytical work, the CAS did not provide an adequate roadmap of how the Bank's program could help reduce poverty in the country. Some of the analytical work needed to spell out a shared growth strategy was subsequently prepared during the CAS period. With hindsight, the 2005 CAS program was relevant to the strategy of the country and responded to emerging concerns, but its design was affected by the limited analytical work available at the time.

9. The CAS emphasized flexibility in program implementation, building the country's implementation capacity, harmonizing development partners, and improving M&E. Again, the CAS was scarce in details on how these principles would be implemented. The CAS could have spelled out with more precision the proposed approach to capacity building, and M&E, or could have proposed a roadmap to strengthen donor coordination.

[27] The partners did not modify the results matrix during implementation.

III. Progress toward Development Goals

10. Lesotho posted mixed progress toward the PRSP goals. On the positive side, the rate of economic growth exceeded expectations. Between 2006 and 2008, the average rate of economic growth was 4.5 percent. The CAS had foreseen an average rate of 3.0 percent, which turned out to be unduly pessimistic.[28] Lesotho's exports (garments and diamonds) and large SACU transfers were the main contributors to the recent spurt in economic growth until the global economic crisis hit Lesotho hard in 2008–09.

11. The 2008 global crisis affected the country through several channels.[29] As a result, GDP growth was expected to be only 0.9 percent in 2009. After rising sharply from 25 percent of GDP in 2004–05 to approximately 40 percent of GDP in 2006–07, SACU revenues fell somewhat to 37 percent of GDP in 2008–09. They are expected to decline sharply to approximately 14 percent of GDP in 2010–11. This steep decline in SACU revenues is expected to translate into deteriorations in both the fiscal and the current account balances.

12. Access to primary education improved significantly, and universal primary education and gender parity are within reach in Lesotho. However, as is typical in many developing countries, educational quality is now the main concern, along with the provision of secondary education as the number of graduates of primary education increases. Tracking progress in the quality of education is difficult because a monitoring system is not in place and information is weak and sporadic. Tracking the impact of economic growth on poverty with certainty is impossible at this time. The last comprehensive information on poverty levels came from the 2002–03 Household Budget Survey (HBS) and the 2004 Demographic and Health Survey (DHS). The information available suggests that in 2002–03 roughly half of the population lived below the national poverty line; poverty remains 50 percent higher in rural areas than in urban areas; and inequality in Lesotho is very high.[30] The country's HIV/AIDS rate remains among the highest in Africa, with limited progress achieved only recently, as described below. The likelihood of meeting the Millennium Development Goals (MDGs) overall is mixed.

13. Lesotho's governance indicators consistently are far above the SSA average and, recent progress in the governance rankings has been relatively limited.[31] More importantly, Lesotho and Swaziland rank lower on governance than their neighbors: Botswana, Mauritius, Namibia, and South Africa. Lesotho's lower ranking represents a disadvantage as the

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[28] Estimates of the annual rate of economic growth stand between 5%–6%. It was expected by the Bank that (1) mining would continue to lead growth; (2) performance of manufacturing would depend on improving the business environment; and (3) the recovery of agriculture after the 2007 drought would contribute to economic growth.

[29] The main channels of crisis impact are (1) economic slowdown in the United States (Lesotho's main export destination for garments) has hurt Lesotho's textiles industry leading to job losses; (2) slump in diamond prices and the global credit crunch have resulted in reduced production and export of diamonds; (3) slowdown in the South African economy has led to a sharp decline in its imports and, as a result, significant decline in SACU revenues; and (4) large-scale job losses have occurred in the mining sector, in which Basotho are employed.

[30] It is likely that, in Lesotho, the limited impact of high aggregate economic growth on reducing poverty and improving social indicators is related to the high level of inequality.

[31] As tracked by WBI Governance indicators.

country competes for investment within a common economic space. The country ranks particularly low in regulatory quality (business environment). Its highest rankings (over 50 percent) come in control of corruption, voice, and accountability.

14. Political stability also is a concern as evidenced by the highly contested elections of February 2007, divided political support (rural support to the ruling party and urban support for the opposition), and continuous splits of the political parties.

IV. Results from the Bank Assistance Program

15. This section of the CASCR takes stock of the results contributed by the World Bank's program under the CAS. To the extent possible, the section examines the contribution of the program and its results toward reaching the country's long-term development objectives. For ease of presentation, table 1 presents a summary of progress against the key result indicators, which are analyzed in the remainder of this section pillar by pillar. A matrix in the appendix presents achievements against expected results in more detail (table A7).

Strategic Objective 1: Fighting HIV/AIDS

Table 1. Key Results of 2006 CAS against expected outcomes, Strategic Objective 1

Strategic Objective	Expected outcome and performance indicator for end-2006 CAS period	Progress to 2009	Main instruments
Increase capacity and effectiveness of GOL, private sector, and NGOs to manage national and local HIV/AIDS programs	At least 50% of projects financed by Global Fund for AIDS, TB and Malaria (GFATM) are to be implemented satisfactorily.	***Achieved.*** As of December 31, 2008, 94 percent of GFATM Grants had been disbursed. 14 of 15 total financed subprojects rated satisfactory.	HIV/AIDS Capacity Building and TA Project Health Sector Reform Project Phase II
	26 VCT sites function appropriately with required test kits, counselors, and following national protocols.	***Achieved.*** 102 sites had functional VCT centers as of end-December 2007; 50% of them fully equipped.	

16. Prioritizing the work on HIV/AIDS under the CAS was highly relevant. Had such high levels of incidence gone unattended, the welfare and economic costs could have escalated rapidly. The major concern was the low pace of implementation of the government's and development partners' initiatives. To address this concern, the Bank defined its role as helping the (a) National AIDS Commission (NAC) to implement the GOL's program and (b) GOL to mobilize resources from the Global Fund and other development partners. To achieve these objectives, the Bank relied on its ongoing HIV/AIDS Capacity Building Project, patterned after the Bank Multi-Country HIV/AIDS Program under implementation in Africa. Consequently, the $5 million IDA grant focused on improving the implementation capacity at the Ministries of Finance and Development Planning, and Health and Social Welfare; and at the Secretariat of the National AIDS

Program. In addition, the grant targeted working with civil society and the private sector to raise awareness and enhance the national implementation capacity.

17. The IDA grant succeeded in meeting all of the project development objective indicators. The capacity to implement and utilize resources under the Global Fund for AIDS, TB and Malaria (GFATM) and assess the impact of resources for the national response substantially increased for both governmental and non-governmental institutions. The project disbursed 94 percent (US$32.25 million) of the Round 2 GFATM Grants by December 31, 2008, easily surpassing the 80 percent target. The project contributed to a sharp turnaround in the Global Fund portfolio from poor performance to very good performance. In addition, Bank assistance has contributed directly and indirectly to the (a) design and approval of a National HIV/AIDS strategy, (b) communication and training of youth (approximately 490,000 of young people out of school underwent life skills education; number of condoms distributed to youth corners and general population increased 220 times), and (c) advancing testing and retroviral treatment.

18. As a result, the pace of implementation of the HIV/AIDS Strategic Plan is picking up. By the end of the project, the number of sites with functional Voluntary Counseling and Testing (VCT) centers reached 102 sites, almost doubling the project target of 55 sites and 50 percent of these sites are fully equipped. The antiretroviral (ARV) program was established. The number of people receiving ARV treatment reached approximately 23,000, exceeding the project target of 20,000. As to the impact of these efforts on the development objectives of the country, the escalation of the epidemic appears contained. Nevertheless, the magnitude of the problem is such that major gaps remain in both prevention and mitigation. Thus, adult HIV prevalence remains stagnant: 2005 and 2007 surveillance data showed no major differences in incidence among women attending antenatal clinics. On the positive side, incidence among youth (ages 15–24) fell from 11 percent in 2005 to 8.9 percent in 2007. Regretfully, female incidence at 14.9 percent far exceeded male incidence at 5.9 percent. By the end of 2009, only 40 percent of eligible patients had been covered with advance testing and retroviral treatment.

19. The limited impact of the project and the overall development partner support on prevalence is understandable given the time it took to speed up implementation. However, other factors may be at work. The GOL and development partners should pay greater attention to investigating the determinants of the epidemic through, if possible, joint analytical work. Lessons that have emerged from assessments of past donor support include avoiding unrealistic and over-ambitious project designs, ensuring that the institutions needed to implement them are in place, and working continuously at capacity building. In August 2009, the Bank approved a follow-up project that continues to focus on helping to (a) draw on international funds that are available to fight HIV/AIDS and (b) improve coordination and implementation capacity. At this time, the ICR for the previous project is available. The challenge for the new project will be to go beyond the previous efforts and seek impact on the ground through the development and implementation of a good monitoring system that would track changes of behavior in the population consistent with a future reduction in HIV/AIDS incidence.

Strategic Objective 2: Strengthen Sustainable Pro-Poor Growth and Job Creation

Table 2. Key Results of 2006 CAS against expected outcomes, Strategic Objective 2			
Strategic Objective	**Expected outcome and performance indicator for end-2006 CAS period**	**Progress to 2009**	**Main instruments**
Reduce constraints and associated costs to private sector development to enhance domestic and foreign investment	Days required to start up a business reduced from 92 days in 2005 to fewer than 38 days by December 2007.	***Partially achieved.*** Days required to start up business reduced from 92 days in 2005 to 40 by November 2009.	Private Sector Competitiveness and Economic Diversification Project PRSP
	Transparent concessioning procedures established for tourism investment opportunities.	***Achieved.*** Concessions manual adopted; sets out transparent procedures. Concession agreements on three sites have been signed.	
Improve access to services and infrastructure to rural households, local communities, and rural enterprises to foster growth in rural sector	Number of customers with less than 18-hour water supply reduced from 94,000 in 2005 to 76,000 in 2008.	***Achieved.*** Number of customers with less than 18-hour water supply fell from 94,000 in 2005 to 2,700 in 2009.	Water Sector Improvement Project APL Integrated Transport Project
	Average travel time to social services and markets for beneficiary population in targeted areas along the South Eastern Corridor reduced by 25%.	***Achieved.*** Average travel time to social and economic services in targeted area (Senqu-Senqunyane) reduced from 5 to 1 hour (80%).	

20. Under the second pillar, Bank assistance sought to help Lesotho develop new areas of economic growth and employment opportunities. The CAS foresaw three results clusters under this pillar. The first cluster centered on creating an enabling environment for private sector development (foreign and domestic). The second cluster combined emphasis on increasing access to good infrastructure and rural development. The third cluster concerned the sustainable use of natural resources. As already has been mentioned, the Bank had not been engaged in working on diversification directly, and no major breakthroughs were expected. The main emphasis was on setting a good institutional foundation for diversification in the future.

Improving the Business Environment

21. To improve the business environment, the Bank aligned its support with GOL's ongoing efforts to reduce behind-the-border constraints. The main instruments have been (a) the Private Sector Competiveness and Economic Diversification Project (PSCEDP), FY07–12 and (b) the PRSC series. PRSC I was approved in FY08 and PRSC II was approved in FY10. Analytical work including an Investment Climate Assessment (ICA) and a Private

Sector Development Strategy[32] has informed the program design and provided underpinning for policy dialogue. A second ICA is under preparation. In addition, at the request of the government, the Bank prepared a series of Policy Notes, on various issues including an examination of the conditions for attracting FDI and diversifying the sources of growth. These notes were discussed with the Cabinet in July 2009.[33]

22. The implementation of the PSCEDP was mixed. The project has been downgraded to moderately satisfactory mainly because of the delayed process of finalizing and adopting the Companies Bill and the newly separated Business Reporting Bill and Industrial Licensing Bill. A draft Companies Bill has been approved by the Attorney General for submission to Cabinet and is targeted for adoption by June 2010. Adoption of the new Companies Act would reduce the time taken to register a business to fewer than 28 days as of December 2009. Likewise, the PSCEDP is supporting drafting new legislation on industrial licensing. The new legislation is expected to be adopted and implemented in 2010. When it is, it will significantly reduce the administrative burden and cost of obtaining industrial licenses in Lesotho. The Ministry of Trade, Industry, Cooperatives and Marketing (MTICM) in collaboration with Private Sector Development Division (PSDD) of the Ministry of Finance and Development Planning and PSCEDP are amending the Trading Enterprise Regulation of 1999. The amendments could gain Lesotho 4 places in the World Bank's 2011 competitive ranking in addition to gaining an additional 4 places through the new Companies Act.

23. A key achievement of the PSCEDP has been strengthening the dialogue with the GOL around financial and private sector development; and increasing coordination among the development partners. The Bank has been working closely with DfID in supporting the One-stop Business Facilitation Centre (OBFC)[34] under the Ministry of Industry. The PSCEDP has supported the development of a strategic plan for the OBFC and is expected to support the implementation of the OBFC strategic plan after DfID support expired in 2009. The PSCEDP is also focusing on consolidating the gains made through DfID support by

[32] Other analytical work included a Program to Reform the Company Registry and Licensing Regime, as well as a study on skills requirements for productivity and growth, a program to reform the immigration and customs services, and the value chain analysis for strategic sectors.

[33] The one-day seminar with the Cabinet, titled "Reshaping Lesotho's Position in SACU to Meet the Challenges of Sustained and Shared Growth," considered four issues: (a) Fiscal Challenges and Options for Reform; (b) Effective Use of Public Resources, Particularly for Capital Expenditure Supporting Growth, (3) Agriculture: Challenges and Directions for Agribusiness; and (4) Realizing FDI to Diversify Lesotho's Exports .

[34] The One Stop Business Facilitation Centre (OBFC), previously called One Stop Shop (OSS), established by MITCM is operational to facilitate issuance of manufacturing and trading licenses and process import permits and export visas. OBFC manages issuing export permits, import permits, business registration and licenses, and work permits. OBFC also provides application forms for residence permits for investors (the actual processing is still done at Ministry of Home Affairs and Public Safety, or MHAPS). Since its inception in 2007, OBFC has issued 692 export visas and 857 import permits. Average time taken to process import permits has dropped from 4 days to 1.9 days. Time taken to process export visas has dropped from 2–3 days to 5–6 hours. OBFC also has issued more than 5,000 business licenses through a slightly simplified administrative process. Additional opportunities exist to streamline processes by adopting new legislation and simpler procedures. The OBFC Steering Committee has approved the appointment of a director for OBFC under MITCM—a key step to strengthen institutional capacity.

building an effective OBFC and by drafting legislation, as already noted, to achieve the CAS objectives under the business environment.[35]

24. In addition, satisfactory work is underway to increase the transparency of the allocation of licenses, especially for tourism. The Ministry of Tourism has adopted a Concessions Manual, which sets out transparent procedures for concessioning tourism sites. A Task Force has been established under the Lesotho Tourism Development Corporation to concession a pilot tourism site with the support of technical assistance (TA) provided under the PSC Project. An information package had been prepared, and the concession process is expected to be completed by May 2010.

25. Concerning the impact of all of these efforts on long-term development objectives, at 130 in the 2010 Doing Business Database, Lesotho ranks the lowest among countries in the Southern Africa region. The other countries are South Africa (32), Botswana (38), Namibia (51), and Swaziland (108). The 2010 Doing Business Database continues to rank Lesotho low at 130 of 183 countries, because the efforts underway, including the legislative initiatives, have not been finalized. Nevertheless, the agenda under implementation is on track and likely will improve the business environment and the institutional effectiveness of OBFC through support for the implementation of the new Companies Act. The Act will strengthen OBFC and focus on the delivery of quick wins in registration and licensing requirements. The institutional strengthening includes the creation of the Private Sector Development Division (PSDD in the Ministry of Finance and Development with support from DfID. Finally, work under the project has helped identify constraints such as the lack of built factory space to support the growth of the manufacturing sector. Through the PSCEDP, the World Bank has initiated dialogue with the GOL to provide support for the Lesotho National Development Corporation (LNDC) to develop and manage industrial facilities and possibly restructure the LNDC.

26. The challenge ahead is great. With public expenditure at 70 percent of GDP in 2009/10, the GOL has limited capacity to design and advance strategies for growth and diversification through public spending. Therefore, the challenge continues to be to improve the private business environment and promote domestic entrepreneurship. Given the size of the GOL expenditure, many of the government's activities impinge on or otherwise negatively affect investment opportunities. Addressing the most critical reforms requires (a) a strong capacity at the central government level to design and coordinate reform, because today all of the initiatives are dispersed; and (b) interest and commitment in each agency to carry out the necessary reforms. Only thus will GOL be able to deliver on its commitment to open space for the private sector. Unfortunately, the domestic private sector's weak capacity to organize itself means that it cannot be an effective counterpart in identifying constraints and proposing and implementing solutions.

[35] The needed legislation covers a wide range of areas—registration and reporting/industrial licensing. The approval and implementation of this legislation is expected in 2010. Work is underway to simplify the visa requirements to enter and to work in Lesotho and the issuance of a National Identification Card. In addition, the Ministry of Tourism adopted a concessions manual, which sets out transparent procedures to assign concessions in tourist sites.

Improving Infrastructure Services

27. For some years, the Bank has been working on improving the investment climate through better infrastructure. The 2005 CAS continued this support through 2 ongoing operations: (a) Phase 1 of the Water Sector Improvement Project Adaptable Program Loan (APL) (WSIP1) and (b) the Lesotho Utilities Reform Project (LURP.) The strategy was that a new initiative—the Integrated Transport Project (ITP), to be co-financed with the EU—would support institutional reforms in the transport sector. Second, and quite importantly, the project would also finance rural roads as a key strategic move to link isolated rural areas to the market. PRSC support for decentralization focused likewise on improving service delivery. The Bank's assistance in infrastructure has been and continues to be highly relevant to creating a competitive investment platform in the sliver of land at the foot of the mountains that surrounds the capital city (Maseru). The transport project also is relevant to the connection of Lesotho's rural areas to the main markets and the connection through the mountains of the main industries around the capital city to the port of Durban in South Africa.

28. *Water.* The long history of World Bank support for the water sector began in the late 1970s with water supply to seven small towns.[36] This history continued with the Bank's involvement in the Lesotho Highlands Water Project (LHWP), which supported the implementation of the engineering studies in 1986. The first Bank project, approved in 1991, was to support Phase 1 of the LHWP, a massive investment to build dam and transmission infrastructure to export water from the water-rich Lesotho Highlands to Gauteng Province of South Africa. Although it financed only 4 percent of the total investment, the Bank played a central role in the completion of the project.[37] The Bank also financed similar assistance through Phase 1B of the LHWP, approved in 1998, which included studies to investigate potential sources of water supply to the Lesotho Lowlands.

29. Afterwards, WSIP1, approved in 2004, focused on improving domestic supply in Maseru and supported WASA, the public water company, to improve management practices. By all accounts, WASA's improvement has been a success story. Among other achievements, WASA has lowered the number of customers who receive fewer than 18 hours' supply, reduced the percentage of biological samples failing testing, reduced unaccounted-for water, and increased the collection of water bills (to 96 percent.) WSIP1 also has contributed to implement the institutional reforms outlined in the 1999 Water Resource Management Strategy, in particular, the establishment of the office of the Commissioner of Water (CoW). One of the CoW's key outputs has been to draft the Water Resource Bill, passed in December, 2008, which provides a comprehensive legal framework for the sector.

[36] The World Bank's involvement in the water sector began in the late 1970s with support for the construction of piped water systems in 7 small towns to serve approximately 50,000 inhabitants. This construction was complemented by measures to strengthen the Water and Sewerage Branch, which ultimately became WASA.

[37] The Bank project that supported this initiative closed in 2007. The team's ICR rated the project as satisfactory on both outcomes and Bank performance. IEG concurred on Bank performance but rated the outcomes as moderately satisfactory.

30. Regarding long-term development goals, the evidence is that, regarding quantity, Lesotho's water service coverage has remained at approximately 80 percent of the population for the last 5 years. However, the quality of the services has improved. Indeed, of 24 African countries sampled between 1995 and 2005, Lesotho ranks third in moving populations away from surface water to higher levels of service. The country's annual gain in piped water has been approximately 2.7 percent over the last decade. As the population in the Lowlands increases through in-migration, the challenge will be to provide these new residents with adequate services. This challenge is being addressed in part through Phase 2 of the WSIP (WSIP2), approved by the Board of Directors in May 2009. This is part of a multidonor program of support to the GOL's Metolong Dam and Water Supply Program (MDWSP). The MDWSP finances construction of the Metolong Dam; a water treatment plant; and downstream conveyance to the Maseru and the surrounding towns of Roma, Morija, Mazenod, and Teyateyaneng. The MDWSP will provide 75,000 m3 per day of additional treated water to the region.

31. Lesotho's experience in the water sector yields valuable lessons. First, the good results achieved at WASA follow from the use of targeted incentives and innovative management tools. The use of incentives was combined with an independent performance audit function, requirement to publish results, and dual oversight agreement. The approach has not only produced results but also built confidence, developed leadership skills, and raised awareness among decision makers of the efforts and inputs needed to improve public utility performance. Most important, the improvements at WASA were internally driven by dynamic management with the support of government stakeholders. These changes could not have been achieved through the support of the World Bank project alone. This experience highlights the importance of government-driven and donor-supported initiatives.

32. *Electricity and telecommunications.* The Lesotho Utility Reform Project (LURP) (FY01) focused on improving service delivery in electricity and telecommunications. It sought to help to consolidate the privatization of the Lesotho Telecommunications Corporation (LTC). It also sought to privatize the Lesotho Electricity Corporation (LEC). In both sectors, it fostered the introduction of regulatory institutions.

33. The strategy to improve the delivery of electricity was, first, to engage a private operator through a management contract and then to privatize. However, in 2003 the GOL decided against an outright sale.[38] The existing management contract continued until December 2006.[39] It yielded major improvements in the quality of the service and the finances of the company.[40] Many of these achievements took place during this CAS period. From 2001 to 2007, the number of customers doubled—to approximately 55,000. Bill collection stands at approximately 100 percent. The percentage of electricity losses dropped from 35 percent to 11 percent. The electrification rate rose from 1 percent in 2001 to 18 percent at the end of 2009.

[38] In the meantime, however, Lesotho continued to issue a concession.

[39] The management contract was extended continuously for brief periods—an approach that created undue uncertainty.

[40] The original project did not include investment funds as the funds were to be provided by the private concessionaire. The project was not reprogrammed to provide these funds. Fortunately, resources generated internally financed an effective investment and expansion program. Still, the Bank and the AfDB funded approximately 11,000 connections, slightly above 50% of the 20,000 connections that LEC had built.

34. After the management contract ended in 2006 and LEC's concession failed, the GOL hired individual managers and appointed a managing director in 2007. The development partners have highlighted the risks that this strategy introduces to the achievement of national commitments, such as reaching 35 percent nationwide electricity coverage by 2015. The partners have called on the GOL to hold the new managers to the same standards of accountability as it did the management company. Given the critical importance that the electricity sector plays in the country's economic growth strategy, it is important for the partners to address the concerns about the sustainability of the reform efforts.[41] In hindsight, the Bank could have moved faster to accept the shifting attitude toward privatization of utilities, in which Lesotho's position mimics the position of other countries in the region.

35. *Transportation.* Lesotho has faced the challenge of improving and maintaining the road network, particularly the connection of isolated rural markets. A previous Bank operation[42] developed the conceptual groundwork, tested the options, and drew the lessons that underpinned the design of the Integrated Transport Project (ITP) (FY07) relevant to this CAS. ITP objectives include (a) improving transport sector institutions, (b) connecting isolated (mountainous) areas to services and market opportunities, and (c) mainstreaming the fight against HIV throughout the project components. The project is on target to deliver the results set by the CAS, but it is too early to report definite outcomes.[43] Contracts for civil works aimed at reducing the travel time to markets and social services have been awarded, and the work has commenced. All civil works contracts include clauses calling for actions to increase workers' awareness of HIV/AIDS prevention methods.

36. With the creation in 2005 of an independent Roads Directorate (RD) in the Ministry of Public Works and Transport (MPWT), institutional reform of the road sector is underway. The Roads Directorate operates on commercial principles and is a proxy of the Road Authority but with its own board. The Roads Directorate is in the final stages of becoming fully staffed. All indications are that, when fully operational, it will catapult Lesotho road sector management from a traditional departmental and politicized entity to one of technical excellence. The long-term benefit to the Lesotho economy is that the professional approach and technical and resource-based planning for the network—including prioritization of maintenance, rehabilitation, and development of the network—will result in optimal use of available resources at any time. A less pronounced but gradual improvement is found in the Road Fund functions. The government is increasing the user fees for the Road Fund, which are used to finance routine and periodic maintenance of the road network. Coverage of maintenance by user fees is up from 50 percent to approximately 72 percent.

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[41] Other concerns include (a) weakening the regulator by removing an independent source of finance; (b) weakening monitoring and reporting (previously done by the concessionaire); and (c) closing the Privatization Unit, which held valuable experience in managing IDA and AfDB projects.

[42] Road Rehabilitation and Maintenance Project (RRMP).

[43] Results on the ground will come in the next CAS. However, due to escalation of costs, additional financing will be required to complete the works that already have been programmed.

Sustainable Development

37. The majority of the population and the poor live in the highlands. Given the limited arable land in a fragile environment, the strategy for sustainable development centers on enabling local communities and authorities to better manage their natural assets. Through the Maloti-Dakensberg Trans-frontier Project (MDTP), the Bank supported efforts in targeted areas to develop and test mechanisms to empower communities to manage their environmental assets. The CAS had foreseen an additional operation to support the environment financed with regional GEF funds. However, that funding went to a different program.

38. The MDTP closed in December 2009. It met its development objectives: (a) community-based planning principles were adopted to facilitate management of natural resources in the areas supported by the project; and (b) good cooperation between South Africa and Lesotho helped to address threats to biodiversity and conservation such as fires. In addition, the MDTP contributed to the development of the 20-year bio-regional trans-frontier conservation strategy, development of the tourist strategy, and conservation measures for threatened species. The current challenge is to work on the sustainability of these initiatives and expand achievements beyond the targeted areas under the project. Much hinges on the success of the decentralization strategy and the effective empowerment of the local communities to manage their natural resources.

Strategic Objective 3: Improve Human Development Outcomes

Table 3. Key Results of 2006 CAS against expected outcomes, Strategic Objective 3

Strategic Objective	Expected outcome and performance indicator for end 2006 CAS period	Progress to 2009	Main instruments
Improve health systems management and efficiency to provide essential health services	Reduction in average waiting period from 4.5 hours to 2.0 hours at health facilities by 2009.	***Partially achieved.*** Average waiting period reduced to 3 hours and 20 minutes in 2009.	Health Sector Reform Project Phase II PRSP
	Increase in TB cure rate from 52% to 60% by 2008.	***Achieved.*** For 2008/09, the average TB cure rate reached 66.5%.	
Increase access and performance in primary and secondary education	National Performance Level (NPL) in numeracy at grade 6 increased from 49% in 2003 to 55% by December 2007.	***Achieved.*** NPL in numeracy at grade 6 was 58% in 2006.	Second Education Sector Development Project Phase II PRSC ITP
	NPL in Sesotho literacy at grade 6 increased from 58% in 2003 to 65% by December 2007.	***Achieved.*** NPL in Sesotho literacy at grade 6 was 69% in 2006.	

39. As mentioned, Lesotho's challenge was to deliver better outcomes in education and health. In primary school education, Lesotho ranked high among SSA countries in access, but quality was a concern. On the other hand, low enrollments in secondary and tertiary education did not bode well for an economy aspiring to compete and grow into middle-income status. The health of the population appeared to have declined over the previous

decade. Morbidity and mortality from communicable deceases had increased, a problem made even more critical by the high incidence of HIV/AIDS.

Health

40. Bank support for health came through the Health Sector Reform Project (HSRP) Phase II (FY06) operating as a sector-wide approach (SWAp) agreement with other development partners. The five triggers for moving to Phase III of the APL have been met.[44] Nevertheless, performance of the 15 key indicators tracked by GOL and partners under the SWAp is mixed. Based on the original design, Phase III would have provided support mainly to the national referral hospital, which already has been supported by the public-private partnership (PPP). Thus, it is planned that a Health Sector Results-based Financing Project, instead of Phase III of HSRP, will be prepared.

41. With the support of the CAS program, major achievements include (a) improved capacity for service delivery at the district level; (b) higher immunization rates; (c) improved access to essential health services, that is, antenatal care and preventing mother-to-child transmission (PMTCT); (d) increased HIV testing coverage and TB detention rates; and (e) improved M&E and fiduciary capacity.[45] Despite the work and progress in putting in place new institutional arrangements that emphasize local responsibility for health services, the full impact on the ground has yet to come. Lesotho remains behind in reaching the MDG targets—with low life expectancy, high child mortality, and the third highest adult HIV prevalence in the world.

42. As with HIV/AIDS, the achievement of development outcomes such as moving closer to MDG targets and reversing declining trends will depend on removing capacity constraints. For instance, the shortage of health professionals is severe. The country needs to develop a medium-term plan rather than rely on stop-gap measures—often under the advice of development partners to produce immediate results. The decentralization of health services, a basic pillar of the reform design, further illustrates how capacity limitations hinder delivery of outcomes. Three years after decentralization commenced, the District Health Management Teams are not yet fully operational. Transferring responsibility for delivery to the district level requires very intensive coordination (planning, implementing agencies, budgeting). Such coordination does not happen by itself, and health authorities currently are not able to implement it by themselves. In addition, the lack of health professionals is even more severe at the local level than at the center. The Bank, under the GPOBA grant, and IFC

[44] The 5 triggers are (a) the District Health Management Teams have their own budgets and authority to incur expenditure; (b) the TB program has been strengthened. The latest data (2008–09) indicated a treatment success rate of 67%, somewhat lower than in 2006 (73%); (c) the PPP contract for the new national referral hospital achieved financial closing; (d) disbursement stands at more than 90%; and (e) formulation of the national health financing policy is in progress.

[45] In greater detail, progress under the project includes (a) District Health Management Teams (DHMT) have been established in 10 districts and provided with equipment and in-service training; (b) a five-year Emergency Human Resources Plan has been developed and aims at fast-track recruitment of the resources needed to effectively deliver health services; (c) the PPP to replace the National Referral Hospital Queen Elizabeth II is on track; (d) key studies on how best to allocate resources to districts has been completed; (e) the MOHSW has undertaken a functional review of its administrative structure; and (f) procurement of incineration equipment and incinerator repairs to properly manage medical waste has been completed.

are helping GOL to put in place a PPP to build and operate Lesotho's National Referral Hospital, which serves the bulk of the Basotho population.

Education

43. As stated in Vision 2020, the overall aim for education in Lesotho is to develop and implement "education policies which ensure the acquisition of functional literacy among all Basotho and the development of a productive, quality human resource base through education and training."

44. The Bank has provided support for the country's education efforts since 1975. Significant progress has taken place, especially with regard to basic education. Free primary education was introduced in 2000. Progress in access and retention led to gross and net enrollment rates of 118 percent and 82 percent, respectively, in 2008. Completion rate for the same year was 93 percent. Gender parity has been achieved, and Lesotho is expected to reach the MDGs for education on time. Bank support during the CAS period came through an IDA operation—the Education Sector Development Project (ESDP) Phase II—and two sequential grants from the EFA Fast Track Initiative (FTI) Catalytic Fund.

45. The outputs of these interventions are visible in the (a) construction and renovation of classrooms and a new campus for the Lesotho College of Education in the mountainous area of Thaba-Tseka; (b) provision of primary school textbooks and learning materials; (c) increased number of teachers including qualified teachers; and (d) introduction of a distance education teacher training program.[46] The proportion of the total education recurrent budget devoted to primary education increased from 57 percent in 2004 to 64 percent in 2008–09. The share of budget allocation to education was 22 percent in 2008. However, important challenges are still to be faced. Repetition is very high, especially in first grades (29 percent repetition rate in grade 1). More than half of the school infrastructure for primary education (52 percent) does not meet basic standards. Forty-two percent of the teaching staff is unqualified. Enrollment in post-basic education in general is still low (42 percent gross enrollment rate for secondary education), and there are questions about the quality of basic education.

46. Bank assistance has been hampered by the limited capacity in the Ministry of Education and Training (MoET). To support implementation of ESDP Phase II, a Project Support and Coordination Unit (PSCU) was established with project and counterpart funds. This unit grew substantially over time. It became a parallel structure to MoET, on which it depended not only for project implementation but also for M&E, overall procurement, and financial management. This unit was dismantled in December 2008. Since then, MoET has been going through a transition aimed at creating in-house capacity. As stated in the ICR, in 2008 MoET's capacity was diminished by the closure of the project, resulting in the loss of

[46] In greater detail, 38 new primary schools were constructed under the ESDP II; 29 schools were reconstructed or extended under the FTI funds. However, a significant number of pupils remain in temporary structures and overcrowded conditions. In 2007 FTI funds helped provide 389,000 books for core subjects (English, Sesotho, mathematics, and science). The number of teachers has increased to over 10,000, reducing the average pupil: teacher ratio to 41. The number of unqualified teachers has stabilized at approximately 41 percent. The Distant Teacher Education program produced its first 450 graduates in 2006.

most of the PSCU personnel. In 2007 the MoET began to create public service posts to replace some of the tasks, and many of the PSCU staff was absorbed. However, there were significant losses of expertise in financial management, procurement, and supervision of construction.

47. Resistance to reform in post-basic education was another factor that hampered Bank support. ESDP II was expected to advance the reform agenda in post-basic education, but both internal and external resistance prevented it from moving forward. The lack of progress has important consequences. Current post-basic education is both inefficient and quite costly. The expenditure line for the bursaries scheme is approximately 35 percent of the overall education budget.

48. Donor coordination in Lesotho has been very successful in the education sector. The local education donor group has supported the preparation of the Education Sector Strategy 2005–2015, and its update, the Education Sector Medium Term Plan 2009–2012. Both have been endorsed by the donor group and the FTI partnership. Three applications for grants from the FTI Catalytic Fund were submitted and succeeded. Annual joint technical reviews take place regularly, and joint supervision has taken place regarding the implementation of the FTI grants. Irish Aid is the lead donor.

49. Looking forward, education in Lesotho faces three major challenges:

a. Improve the quality of primary education to complement the significant gains in access.
b. Improve access to secondary education. As primary completion rates improve, larger cohorts move into secondary education, in which fees and lack of infrastructure (buildings, teaching materials, qualified teachers) limit access, especially by the poor.
c. Increase the relevance of tertiary education and its ability to support growth. To date, the sizable allocation of public resources has not been followed by the emergence of qualified graduates.

Strategic Objective 4: Improve Service Delivery through Government Reform

Table 4. Key Results of 2006 CAS against expected outcomes, Strategic Objective 4

Strategic Objective	Expected outcome and performance indicator for end 2006 CAS period	Progress to 2009	Main instruments used
Improve capacity for management of public resources at central and decentralized local GOL levels	MTEF introduced in at least 10 ministries by 2009.	*Achieved.* All ministries used MTEF and produced Budget Framework Papers for 2009–10 and 2010–11.	PRSC PEFAR CPAR
	Government approves and put in place a harmonized mechanism for monitoring the PRS by June 2008.	*Achieved.* Joint Government-donors PAF has been developed and progress annually reviewed.	

50. Under the fourth pillar, the CAS foresaw support for GOL's commitment to involve local communities in their own development, following on the election of district and local councils for the first time in 2005. [47] These elections proved that the GOL was committed to decentralization. It follows that attention to decentralization was highly relevant for two reasons. It was a priority for GOL, and effective decentralization was important to achieve various objectives of the strategy, including in health and environment. However, the Bank had not previously worked to develop the capacity of local governments. Of the other development partners, only Gessellschaft fur Technische Zusammenarbeit (GTZ) had.

51. The Bank's strategy was to accompany decentralization through a PRSC series, while strengthening the capacity of the GOL to manage public resources. The latter also was an area in which the Bank had had limited engagement. However, other development partners such as UNDP and DfID had been engaged in this area.

52. The Bank's Board approved the first (of three) PRSC operations for Lesotho in May 2008 and the second on March 30, 2010. The PRSC I operation covered three themes: (a) creating a conductive environment for private sector growth, (b) improving the public expenditure management and fiduciary framework, and (c) improving access to basic services through decentralization and empowerment of communities. Work under the last two themes supports this pillar. Although GOL has made significant progress in implementing its reform program supported through PRSC I, the approval of only the first operation and preparation of the second during this CAS means that outcomes under the program will not manifest until the new Country Assistance Strategy.

53. Most recently, the PRSC has successfully promoted the adoption of better budgeting practices.. They include the adoption of the Medium Term Expenditure Framework (MTEF), and as an integral part of MTEF development, the annual preparation of a Medium Term Fiscal Framework (MTFF). On April 1, 2009, a new Integrated Financial Management Information System (IFMIS) became operational. All ministries now prepare their MTEF budgets by using the budget module of the IFMIS, the new chart of accounts, and the new budget classification system. Individual ministries also prepare Budget Framework Papers (BFPs), which set out their visions, objectives, proposed revisions to their programs, and proposed changes to their pattern of resource use.

54. Six pilot ministries prepare MTEF information on a program basis. In 2007 Lesotho revised its Public Procurement Regulations to align them with international practices. The new procurement system is decentralized and supported by a Procurement Policy and Advisory Division. A Country Procurement Assessment Review (CPAR) identified areas in which some fine-tuning will improve and clarify the design of the procurement system during the PRSC implementation. Amendments to the Public Procurement Regulations have been drafted; however, their finalization is awaiting passage of the revised PFM Act. To provide an appeal mechanism, instead of the proposed establishment of an Independent Procurement Regulatory Authority (IPRA), the GOL is establishing a Procurement Tribunal.

[47] Note that the title of this pillar differs between the main text and the results matrix found as an appendix in the CAS. The title in the main text is "Decentralization, Service Delivery, and Monitoring and Evaluation."

55. On decentralization, the most notable result was the enactment into law of the Local Government Service Bill, which is highly relevant. Local elections and the establishment of Community and District councils in 2005 launched a variety of local activities and expectations that could not be properly addressed under the existing institutional framework. The Local Government Service Act of 2008 helped clarify responsibilities as it was the first law to clarify the roles and responsibilities of local officials and central GOL officials working at the local levels. As GTZ is the key partner and the Bank does not have ongoing support in the area of decentralization, the prior actions identified for PRCS-2 no longer cover support in this area.

56. Lesotho has been a relative latecomer to public sector reform and is trying to catch up quickly. As a result, the remaining PRSC agenda is daunting. In other countries, similar agendas have required considerable coordination, technical assistance (TA), time, and commitment. The challenge for Lesotho will be the speedy delivery of results that improve governance through a more efficient and effective public sector to make Lesotho more competitive in the region. More efficient public spending is even more relevant today when the availability of public resources is decreasing as SACU revenues shrink. In moving forward, the Bank and other donors should take into account GOL's capacity limitations and strive to keep the program designs simple.

V. Bank Performance

57. Actual lending has followed the CAS program, with the exception of the proposed GEF operation, which could not be delivered for reasons noted. Appendix tables A1 and A2 provide information on the projects that were active at the beginning of the CAS and the projects that were approved during the CAS. Table A5 compares planned with actual lending. As of May 1, 2010, 6 IDA operations and 1 GPOBA[48] grant (in the amount of US$6 million) were active in the Lesotho portfolio. The PRSC I has been closed and the PRSC II was approved by Board on March 30, 2010. Total lending commitments are approximately $100.7 million, of which as of May 1, 2010. The bulk of the disbursements in FY06–07 had come from operations under implementation at the beginning of the CAS (table A3). In FY09 new operations approved during the CAS implementation took off and outperformed the old ones on the disbursement front. The disbursement ratio in FY09 reached 38.6 percent, which was above the Sub-Saharan Africa average. Nevertheless, the bulk of the results came from the operations active at the beginning of the CAS period since half of the portfolio is young.

58. Likewise, delivery of the AAA program is roughly on target. Two studies were dropped: Justice and Law Reform, and a Transport Sector Study.[49] The analytical work on poverty (shared growth) and vulnerability was direly needed and is now available to inform the preparation of the coming 2010 Country Assistance Strategy. The work on creating shared growth by reducing inequality and vulnerability analyzes a broad range of relevant topics and provides recommendations based on the international experience. An Investment Climate Review (ICR) and a Country Economic Memorandum (CEM) in the form of the

[48] The Global Partnership on Output-Based Aid grant in support of Lesotho Queen Elizabeth II Hospital PPP project aimed at improved access and quality of medical services in Lesotho.
[49] Table A6.

Policy Notes (with a focus on trade, regional integration, fiscal challenges, and agriculture) were delivered during the CAS period and buttress the increasing emphasis on growth.

59. The current portfolio of six projects shows mixed performance. There is one problem project—the Water Sector Improvement Project Phase 1 (WSIP I). In addition, the rating of the Private Sector Competitiveness and Economic Diversification Project recently was downgraded, for reasons stated in para. 22 above. Thus, the commitment at risk amounts to $14.1 million and constitutes 18.6 percent of the portfolio. The index of proactivity stands at 100 percent, which means that the response of the country team to emerging problems is timely and effective. At the same time, the latest weakening of portfolio performance calls for increased staff and management attention to the portfolio quality and implementation support.

60. The last formal Country Portfolio Review (CPR) took place in June 2008. Its recommendations provided a comprehensive and strategic overview of portfolio performance and the portfolio's alignment with CAS objectives. The CPR also pointed out persisting implementation issues (implementation delays, project management difficulties, institutional issues, FM) that may not have been reflected in the project ratings but which could affect projects' performances. The CPR Note highlighted the necessity to ensure good alignment among portfolio, CAS, and other DP programs. The CPR Note also urged that the government and other DPs agree on a modus operandi for systematic, coordinated and integrated portfolio/program and CAS implementation monitoring. However, the same Portfolio Review Note warns against complacency and calls for closer and timelier tracking of the program and its impact on development outcomes. The review note recommends that the team informally track performance on a continua; basis; and formally track it with the authorities and other development partners periodically.[50] More proactive tracking helps to (a) promptly address delivery delays and (b) fine-tune the results framework to improve the program's alignment with the development outcomes.

61. Reviews of projects already completed show mixed results. Four projects were completed during the CAS period and reviewed internally by the teams. The country teams rated two of them (HIV/AIDS and Highland Water) as satisfactory on both outcomes and Bank performance. The team rated the Education Sector Development Program (EDSP II) as satisfactory on outcomes and moderately satisfactory on Bank performance. The team rated the Utilities Sector Reform Project moderately satisfactory on both counts. The team rated Maloti Drakensberg GEF moderately satisfactory on outcomes and moderately unsatisfactory on Bank performance. Health Sector Reform Project II was closed in FY10 and not has been rated yet.

62. Lesotho's current performance is in line with the average of Sub-Saharan Africa countries. However, the evidence points to shortcomings in, among others, institutional development impact and performance at entry. The evidence here refers to the project reviews undertaken by the Bank's Independent Evaluation Office (IEG). The most recent moderately unsatisfactory rating for EDSP II on outcomes and mixed portfolio performance calls for the teams to pay more attention to (a) project design, that is, to make an upfront shift in quality design and (b) institutional sustainability, given cases of backsliding after projects

[50] The last formal Country Portfolio Review dates from 2005.

are completed. IEG also reviewed the Utilities Sector Reform Project and rated it Moderately Satisfactory on outcomes and implementation performance.

63. The Bank has been working closely with development partners on multiple fronts. The Bank's role in partnering with other donors differs from sector to sector. In HIV/AIDS, the Bank is helping to build the GOL's capacity to effectively use available resources from Global Fund, Millennium Challenge Corporation (MCC), and PEPFAR. In water, it is helping to mobilize and leverage sizable resources from MCC, the European Investment Bank (EIB), Arab Bank for Economic Development in Africa (BADEA), OPEC Fund for International Development (OFID), Kuwait Fund, Saudi Fund, and Republic of South Africa to continue investment in infrastructure and increase coverage. In the education sector, the Bank works closely with FTI, Irish Aid, and Japan International Cooperation Association (JICA). As the CAS foresaw, overall, the Bank has succeeded in leveraging development partners' aid inflows. The Development Partners Consultative Forum (DPCF) proved to be an effective way to achieve the stated goals, and the Bank plays an important role in coordinating and harmonizing aid. However, the leadership of the authorities, particularly the Ministry of Finance and Development Planning, is essential to enhance the donors' coordination.

VI. Looking Forward: Lessons and Recommendations

64. The Bank program has contributed significant results in the areas in which it has been involved longer, including water, electricity, and education. In these areas, the Bank has made a sustained effort and focused on institution building. The new areas of Bank engagement, mainly competitiveness and strengthening the capacity of the state, are very relevant, but the program has yet to deliver solid results. AAA work is well aligned with country needs and priorities: shared growth, effective management of public funds, and decentralization. However, this work has not always been timely in terms of project preparation and the country stills lacks updated information on poverty incidence. Portfolio performance is mixed, with 1 problem project and 2 projects out of 5 having been downgraded in their performance ratings.

65. The paradox is that in spite of the broadly positive economic performance during the CAS period, the development challenges remain roughly the same as when the CAS was designed. HIV/AIDS incidence remains high as do poverty and economic inequality, despite a rate of economic growth higher than expected. The likelihood of reaching the MDG targets is mixed across the targets. Competitiveness continues facing the same challenges and risks, and Lesotho is missing a refined strategic vision of how best to profit from the regional and global opportunities. At the same time, the global economic crisis brought new challenges of sharply declining SACU revenues with a potential threat to the country's macro and fiscal stability.

66. At the heart of this paradox is the fact that Lesotho's political difficulties until the end of the 1990s meant delays in starting reforms in critical areas, such as public sector governance and competitiveness, in which other countries have been working for a longer time. As a consequence, Lesotho faces a catch-up problem, which in turn leads to the design of ambitious agendas that test the country's limited capacities. Therefore, the main lessons and recommendations center around two actions. The first is to build capacity. The second

is to prioritize and streamline the reform agenda to avoid over-ambitious undertakings that create fatigue and a feeling of failure, as was the case in the CAS under review. Third, it also should be kept in mind that no Progress Report was prepared. Hence, there was no mid-term opportunity to bring greater realism to the results framework.

VII. Develop a Credible Capacity Building Strategy

67. Bank country teams and the GOL share the consensus that lack of capacity is a major constraint to program effectiveness and to the advance of reform initiatives. The present Completion Report finds that the evidence supports this consensus. Moreover, since results are interconnected across themes, delays in one area, such as decentralization, slow progress in others, such as service delivery.

68. The emphasis on capacity is not new. The FY06–09 CAS called on partners to think how best to break (release) the capacity constraints. The avenues tried included improving capacity within projects. This approach has worked well in repeat operations and when the emphasis includes putting in place the incentives to sustain institutional designs. The accomplishments in the water sector are an example.

69. Another approach was to use IDA funds to break capacity constraints and facilitate access to international funds and their implementation. This approach has worked in HIV/AIDS by helping to mobilize and use external funds. However, the AIDS efforts initiated at mid-stream have yet to make an impact on development outcomes. The lesson that emerges is that it takes time to establish a *modus operandi* of how to break the capacity constraints to deliver results on the ground. The challenge is to shorten the learning lag.

70. In tackling capacity constraints, it is important to bear in mind that capacity is a catch word that covers a variety of concerns. Examples include the lack of trained personnel, such as physicians; weak program design; weak incentives and institutions; and commitment from the authorities. Hence, any approach must take account of the specifics at the sector and the project levels. For instance, it is necessary to understand the drivers of brain drain, the factors that delay adopting new legislation, and the reasons behind slow implementation of the reforms. Doing so enables the design of effective tailor-made capacity building interventions as a prerequisite for successful implementation of the Bank program.

VIII. Rethink and Sharpen the Growth (Competitiveness) Strategy

71. Rethinking the current competitiveness strategy beyond its emphasis on improving the business environment and putting in place the required infrastructure should acquire a focus on shared growth—one of Lesotho's greatest challenges. The lesson is that shared growth is not likely to happen by itself. It needs a determined focus. The previous CAS raised the issue but did not articulate a strategy due to lack of supporting analytical underpinning. Recent reviews provide some ground upon which to begin to think about shared growth. However, an updated understanding of poverty incidence is needed, because the most recent information is seven years old (April 2003).[51]

[51] The precise title of the study is "Lesotho: Sharing Growth by Reducing Inequality and Vulnerability: A Poverty, Gender, and Social Assessment" (May 30, 2008). Its wide range of themes include, most notably,

72. A shared growth strategy should include attention to:

- Agriculture and rural development, for which a roadmap beyond the last CAS is needed.
- Encouragement of local entrepreneurship, including focus on the development of adequate skills and increasing the relevance of tertiary education.
- Thinking through the role of the state, which absorbs 70 percent of GDP. The state's expenditures leave very limited space for private economic activity, leading to very weak internal constituencies to promote economic activity. One possibility that other countries have used is to create strong pro-growth advocates—whether government agencies or NGOs—within the state itself.
- Sustained efforts are needed to increase public sector effectiveness, catch up with improving public expenditure practices, and get a handle on decentralization. These moves not only would improve service delivery but also would prepare for a possible decline in the resources available to Lesotho from regional agreements.

IX. Think Regionally

73. One lesson from the past is that Lesotho's success in utilizing the opportunities offered by the 2000 African Growth and Opportunity Act (AGOA) turned the country's attention to international markets, possibly at the expense of thinking regionally. Therefore, some rebalancing is needed to counter the continued risks in the global economy. That rebalancing may come in the form of strategies that exploit the considerable positional advantages that Lesotho has in the region given its wage levels, access to markets, and past experience of profiting from opportunity, as in the case of water. Thinking regionally will mean making sure that institutional mechanisms work. An example would be enhancing customs cooperation between Lesotho and South Africa. Thinking regionally also means learning from other countries in the region that have developed more competitive business environments.

X. Improve the Effectiveness of the Bank's Interventions

74. The limited resources that the Bank provides to Lesotho call for thinking creatively about effectiveness. Besides a continuous focus on addressing capacity constraints and the simplification of objectives, the Bank will aid the effectiveness of its interventions by taking a proactive advocacy position in critical areas such as shared growth to help build ownership. In Lesotho, as elsewhere, the central government's ownership, through the commitment and allocation of political priority and economic resources, is a fundamental driver of success in delivering results. Ownership, however, is not automatic even when the authorities have made public statements on desired outcomes. Through AAA, dissemination, and TA, the Bank can do much more to sharpen clarity of objectives and intended results. In this regard, the Bank can help in providing space for the internal dialogue (Basotho-Basotho), which is now quite limited and for which the Bank could help develop a culture of dialogue and coordination.

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agriculture and rural development, delivery of public services, and an in-depth review of the status of HIV/AIDS.

75. In turn, the Bank can strengthen its position as a strategic partner to Lesotho by supporting the authorities in addressing the immediate challenges that the country will face in the coming years. First, regional rearrangements will lead to a loss of public revenue, calling for a major restructuring of the public function. Second, the country is facing a weakening of its international privileges and must look for alternative ways to participate in the global and the regional economies. Third, the political balance may suffer under drastic internal readjustments.

76. The Bank also can encourage the GOL to take a more active leadership role in donor coordination. Today the country works with donors mainly at the sector level in water, education, AIDS, PFM reform, and PSD. However, the coordination is largely donor driven. Lesotho needs to be in the driver's seat through more determined leadership by the Ministry of Finance and Development Planning.

77. Last, continued progress should help prepare Lesotho to move from IDA funds to access World Bank funds on IBRD terms, especially for enclave projects. Lesotho already has taken this step for the Highlands Water project.

Appendixes

Table A1. Projects under Implementation at Beginning of 2005 CAS

Project name	Dates			ICR rating (outcomes/Bank performance)	IEG ratting (outcomes/Bank performance)	If not closed, expected closing date	Comments
	Board approval	Board effectiveness	Actual closing				
HIV/AIDS CB and TA	07/06/04	01/31/05	12/31/08	Satisfactory/ Satisfactory	Not yet rated		
Water Sector Improvement APL	10/26/04	03/07/05		Not yet rated	Not yet rated	06/30/2010	
Highlands Water	06/04/98	06/09/99	12/31/06	Satisfactory/ Satisfactory	Moderately satisfactory/ Satisfactory		
ESDP 2 Phase 2 APL	07/17/03	09/15/03	12/31/08	Satisfactory/ Moderately satisfactory	Moderately unsatisfactory/ Moderately Satisfactory		
Utilities Sec. Reform	03/29/01	05/17/01	12/31/07	Moderately Satisfactory/ Moderately satisfactory	Not yet rated		
Maloti-Drakensberg (GEF)	09/13/01	07/06/02	12/31/09	Moderately Satisfactory/ Moderately Unsatisfactory	Not yet rated		

Table A2. Projects Approved during Implementation

Projects foreseen originally in the CAS by fiscal year	Project name	Dates			Notes if needed
		Board approval	Effectiveness	Closing	
FY06	Lesotho Health Sector Reform	10/13/05	02/23/06	03/31/09	Closing extended till 30/09/09
FY07	Lesotho Integrated Transport Project	10/19/06	02/19/07	30/06/11	
	Private Sector Competitiveness	03/21/07	10/05/07	06/30/12	
FY08	PRSC I	05/22/08	08/20/08		
FY09	Water Sector Improvement Project II	05/18/09	09/18/09	06/30/15	
FY09	PRSC II	03/30/10	TBD		
FY09	Technical Assistance Project for HIV/AIDS	08/27/09	19/01/10	01/31/15	

Table A3. Disbursement by Year Differentiating between Projects in Place at Beginning of CAS and Projects Approved during CAS Period *(US$ m)*

Projects	2004	2005	2006	2007	2008	2009
Under implementation at the beginning of CAS period	7.48	14.96	10.85	16.50	7.01	28.3
Approved during CAS period	0.00	0.00	0.60	2.80	2.75	42.2
Total disbursement	7.48	14.96	11.45	19.30	9.76	38.6

Table A4. Total Disbursements by Each CAS Pillar *(US$)*

Objectives	Disbursements 2004–10
Strategic Objective 1: Fighting HIV/AIDS Pandemic - HIV/AIDS CB and TA	4.1
Strategic Objective 2: Sustainable Pro-Poor Growth and Job Creation - PRSC I - Private Sector Competitiveness and Economic Diversification - LT Integrated Transport Project - Highlands Water - Water Sector Improvement APL - Maloti-Drakensberg Transfrontier Conservation and Development Project	45.6
Strategic Objective 3: Improve Human Development Outcomes - Health Sector Reform - ESDP 2 Phase2 APL	27.5
Strategic Objective 4: Decentralization, Service Delivery, and Monitoring and Evaluation - Utilities Sector Reform	29.6
Total	106.8

Table A5. Planned IDA/IBRD Lending Program and Actual Deliveries, FY06-09

FY	CAS plan		CAS actual deliveries	
	Project	**US $(M)**	**Status**	**US$m**
2006	Health Sector Reform Project Phase II	IDA allocation 15.6 million (o/w 7 million grant)	Approved	6.5
2007	Private Sector Competitiveness Project	IDA allocation 31.3 million for FY07-08 (o/w 13.9 million grant) + appr. 4 million from GEF	Approved	8.1
	Integrated Transport Project		Approved	23.5
2008	Poverty Reduction Support Credit I		Approved	15.9
	Community-based Environment and Natural Resource Management (GEF) Project		No GEF project	
2009	Poverty Reduction Support Credit II	IDA allocation of 46.9 million for FY09-10 (o/w 21 million grant)	to be signed during Spring Meetings 2010	25.0[52]
	Technical Assistance Project for HIV/AIDS		Approved	5.0
	Education APL/Swap		The project has been closed; ICR submitted.	

[52] Includes US$10 million of additional IDA allocated through Crisis Response Window.

Table A6. Planned AAA and Actual Deliveries

Year	CAS plan	CASCR
	Product	Completion and date delivered to client
2006	Public Expenditure Management and Financial Accountability Review (PEMFAR)	Delivered FY06
	Justice and Law Reform	Dropped
2007	Poverty Assessment (including gender and social assessment)	Delivered FY09
	Decentralization and demand-driven service delivery	Delivered FY07
	Country Procurement Assessment Report (CPAR)	Delivered FY08
	Incidence and Impact of HIV/AIDS	Delivered FY07
2008	Transport Sector Study	Dropped
	Health Sector Review	Delivered in FY09
	Investment Climate Assessment (repeat of 2004 ICA)	Ongoing – extended until FY10
2009	Country Economic Memorandum: Trade, Regional Integration, and Employment	Delivered in FY10
	Impact Evaluation of Education Interventions for Orphans	Did not take off

Table A7. Reporting on Results

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
1.1 Increase capacity and effectiveness of GOL, private sector, and NGOs to manage national and local HIV/AIDS programs. ***Indicators:*** - At least 50% of projects financed by Global Fund for AIDS, TB and Malaria (GFATM) are judged by the NAC to be implemented satisfactorily by July 2008. - At least 55% of health facilities provide services for prevention of mother-to-child transmission (MCTC) by July 2008. - 26 VCT sites function appropriately with required test kits, counselors, and following national protocols. - Analytic and advisory work on HIV/AIDS is widely disseminated and nationally debated. It influences policies and programs, thus contributing to behavioral changes and reducing the pandemic.	**Achieved :** As of December 31, 2008, 94 percent (US$32.25 million) of the Round 2 GFATM Grants had been disbursed. Ninety-three (93) percent, i.e., 14 of 15 total financed subprojects were rated satisfactory during implementation. **Partially achieved**: No data available on changes in number of health facilities providing services for prevention of MCTC. As of Dec 2007, 31% of pregnant women had received pre-test counseling and accepted to be tested under Prevention of MCTC program. **Achieved**: 102 sites with functional VCT centers as of end-December 2007. 50% of centers equipped with test kits, counselors etc. **Achieved:** NAC together with MOHSW produced and disseminated annual and bi-annual reports as well as Joint annual review reports and M&E quarterly reports for 2008-2009 on all key HIV/AIDS indicators. (ICR for HIV/AIDS project)	HIV/AIDS Capacity Building and Technical Assistance Project (FY05). Second Education Sector Development Project Phase II (FY04). Health Sector Reform Project Phase II (FY06). Integrated Transport Project (FY07) Private Sector Competitiveness Project (FY07). Poverty Reduction Support Credit (FY08). ***Partners:*** Clinton Foundation, Development Cooperation Ireland (DCI), GFATM, UNAIDS, UNDP, UNICEF, USAID, WHO.	Some progress in arresting the spread of HIV/AIDS infection, but limited given magnitude of epidemic. Since 2005, no significant change in adult HIV prevalence has been detected. Surveillance data in 2007 showed no major difference in HIV prevalence among women attending antenatal clinics. However, HIV prevalence among youth (ages 15–24) appeared to trend down from 11.0% in 2005 to 8.9% in 2007. However, female youth continue to be more susceptible to infection at 14.9% vs. 5.9% for male youth. Bank's current strategy to help country implement its program and use available resources to fights HIV/AIDS effectively seems sound. Strategy should be continued with emphasis on monitoring impact through AAA to adjust use of external funds in response to impact evaluation. In doing this, it is important to set realistic goals.

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
2.1 Reduce constraints and associated costs to private sector development to enhance domestic and foreign investment. ***Indicators:*** - Days required to start up a business reduced from 92 days in 2005 to fewer than 38 by Dec 2007. - Days required to obtain industrial and trade licenses reduced from 35–50 days to fewer than 7 by Dec 2007. - Simplified procedures to issue visas, work and residents' permits, etc. by Dec 2007.	**Partially achieved – work in progress:** Days required to start up business reduced from 92 days in 2005 to 40 by November 2009. **Partially achieved:** Days required to obtain industrial and trade licenses remain 35-50 days. Delay in adopting and implementing the new Licensing Bill is affecting this indicator. The One Stop Business Facilitation Center (OBFC), previously called One Stop Shop (OSS) established by MTICM to manage issuing export permits, import permits, business registration and licenses, and work permits. Average time taken to process import permits has dropped to 1.9 days from 4 days. Time taken to process export visas has dropped from 2–3 days to 5–6 hours. **Partially Achieved:** There is a simplified procedure to issue work (3 days first application and 1 day renewal) and residency permits (1 day) under the OBFC. However, only textile manufacturers are eligible for this procedure. The rest should apply to the ministries and it tales 1 month for	Private Sector Competitiveness Project (FY06). Poverty Reduction Support Credit (FY08). ***Partners***: DfID, EU, IFC, MCC, UNDP, USAID.	Progress in creating business environment conducive for private sector development is slow mainly due to delays in improving the legal framework for doing business. Policy reforms have been triggered by PRSC and supported through PSC Project. However, for the reforms to be effective there is a need for a champion of change. A new Private Sector Development Department has been established at the Ministry of Finance and Development Planning with DfID support, which is expected to play a coordinating and facilitating role in pursuing reforms agenda. It is expected that the Bank's support would yield visible results and impact on business environment once the basic laws – Companies Bill and Licensing Bill would be adopted. Adoption of new Companies Act will reduce time to register a business even further to less than 40 days. However, delay in adopting and implementing the new Companies Bill is affecting this indicator. A draft Companies Bill has been approved by Attorney General for submission to Cabinet and is targeted for adoption in 2010. PSC Project has supported development of a Strategic Plan for OBFC and is expected to support implementation of OBFC strategic plan after DfID support ended in 2009. **Implementation of these laws would have a major impact on doing business indicators.** Work under PSC Project also has helped identify constraints such as lack of built factory space for growth of manufacturing sector. Through PSC Project, dialogue has been initiated with GOL to provide support for Lesotho National Development Corporation (LNDC) to develop and manage industrial facilities and possibly restructure

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
- Transparent concessioning procedures for tourism investment opportunities.	work permits and 2-3 months for residency permits. **Achieved:** The Ministry of Tourism has adopted a Concessions Manual, which sets out transparent procedures for concessioning tourism sites. GoL already has successfully signed concession agreements on 3 sites based on the concessions manual.		LNDC.
- Lesotho's share of trade to SACU increases.	**Not achieved:** Lesotho's share of exports to SACU has remained relatively constant at approximately 20-30%, as well as imports from SACU at approximately 80%.	Policy Notes on FDI, Agriculture	The Bank provided analytical support and policy advice on removing constraints in facilitating business relations and trade with South Africa and other SACU members. It is too early to capture impact.
- Harmonization of taxes and introduction of single border posts within SACU.	**Partially achieved:** Lesotho's taxes are largely harmonized within SACU. As a member of SACU, Lesotho applies common customs tariffs and excise duties with Botswana, Namibia, Swaziland and South Africa. The simple average MFN CET decreased from 11.4% in 2002 to 8.1% in 2009 and over half of SACU's tariff lines are now duty free. Works to simplify cross-border trade and customs clearance costs and time at the border with South Africa are underway. The one-stop border posts with South Africa, are still work in progress which will soon be supported by a World Bank Trust Fund grant under the Trade Facilitation Facility.	Trade Facilitation Facility	In 2009 the Bank mobilized financing through the Trade Facilitation Facility managed by the International Trade Department to support collaboration between the Lesotho Revenue Authority and the South African Revenue Service. It is aimed at facilitating trade and investment between two countries through simplified customs clearance procedures and unifying services. It is too early to capture impact.
- Improvement in SACU revenue-sharing formula	**Not achieved and not relevant:**		This result is beyond Bank's activities and support program.

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
	No improvements in SACU revenue-sharing formula. No supporting Bank interventions.		
2.2 Improve access to services and infrastructures to rural households, local communities, and rural enterprises to foster growth in rural sector. ***Indicators:*** - Electrification rate increased from 11% in 2005 to 20% in 2009. - Number of customers with less than 18-hour water supply reduced from 94,000 in 2005 to 76,000 in 2008. - WASA achieves performance targets as mandated in the performance agreement by June 2008. - Number of fixed and mobile	**Partially achieved:** Electrification rate reached 18% at end of 2009. **Achieved:** WSIP project (Phase I) achieved all expected outcomes and surpassed expectations. Number of customers with less than 18-hour water supply fell from 94,000 in 2005 to 2,700 in 2009. WASA successfully completed 2005–08 performance agreement with GOL and signed a second phase agreement for 2008–11. An independent audit of the Phase II agreement concluded that WASA achieved "excellent" ratings on 19 of the 24 indicators. **Achieved:**	Utilities Sector Reform Project (FY01). Water Sector Improvement Project APL (FY05). ***Partners:*** DfID, EU, IFC, MCC, UNDP.	Progress has been made in extending electrification rate. However, national target of 35% by 2015 seems out of reach, especially given concerns about sustainability gains. A lesson learned is that outright privatization may no longer be an appropriate policy for an electric utility in Lesotho with a strong resistance to privatization (similar to many other African countries). Investor appetite is unlikely. To the contrary, domestic political resistance is likely to emerge in response to expected tariff increases and reluctance by private investors to expand connections into "unprofitable" locations. Nevertheless, it is important that the managers of public companies be accountable for their performance. Progress toward improving quality of water delivery has been significant. Experience has yielded three important lessons: • *Targeted incentives and innovative management tools can provide success.* Under WSIP, WASA has been a success story because the design provided incentives. They include payments for utility and relative autonomy as well as accountability through an independent performance audit function, a requirement to publish results, and a dual oversight of the agreement by both Ministry of Finance and Development Planning and Ministry of Natural Resources. • *Capacity building with more autonomy continues to be necessary:* COW and PPSU have improved their confidence during the CAS period and have developed

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
subscribers rise from 287,000 in 2005 to 480,000 by 2009.	Number of fixed and mobile subscribers increased to 530,000 by 2009.		leadership skills for the sector. It is now clear that autonomy is needed for institutions to work and that a separation between regulatory and management responsibilities is needed. • *Donor coordination:* Given the small amount of IDA available and uncertainty of graduating to IBRD status, donor coordination, especially with more nontraditional donors, needs to be given a very high profile.
- Average travel time to social services and markets for beneficiary populations in targeted areas along the South Eastern Corridor is reduced by 25%. - Improved rural infrastructure (including increase in area under irrigation, rural roads, water supply and electrification improved to be determined by service delivery survey).	**Achieved:** Average travel time to social and economic services in targeted area (Senqu-Senqunyane) reduced from 5 hours (1 hour drive and 4 hours walk) to 1 hour (or 80%). **Partially Achieved:** There were several surveys but not a single one to capture improvements in service delivery across the sectors. In the area of electrification and energy supply there were several surveys to measure impact of implementation of the National Electrification plan; to understand better willingness to pay in rural areas. The WB Utility Sector Reform Project (within pilots on rural electrification) achieved an outcome of 700 connections in 10 villages in 4 locations). No interventions in rural water supply. Under the ITP 10 km of rural link roads	Integrated Transport Project (FY07). Private Sector Competitiveness Project (FY06). Poverty Reduction Support Credit (FY08). Economic and Sector Work on Decentralization and Demand-Driven Service Delivery.	It is too early to assess impact of ITP on long-term development outcomes since project is in the middle of its implementation. The new CAS should build on the key achievements in the transport and road sector and provide additional financing for the expected impact to materialize. Performance indicators of the project that go beyond the CAS lifetime should be captured in the next CAS.

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
	constructed and 14 km of rural roads rehabilitated. The percentage of villages within 2km of motorable roads in Senqu-Senqunyane area increased from 2.5% to 17.5% between 2006 and 2009[53].		
- Increase adoption of conservation agriculture technology by 20% of farmers by June 2009 (as indicated by farmer survey). - Increase the number of communities adopting improved range management techniques by 20% by June 2009 (as indicated by farmer survey).	**Too early to measure. Project is under preparation.** **Not achieved.** Data is not available.	Policy Note on Agriculture	Agriculture continues to be a major development concern. The support to agriculture is at an early stage and was done mainly through the AAA and policy dialogue. Policy Note on agriculture and agribusiness prepared upon the government's request informed the discussion with the Cabinet on July 20, 2009. Next CPS should focus on the issues of agriculture as a source of growth and income.
2.3. Increase capacity of local communities and local authorities to enhance sustainable use of environmental assets. ***Indicators:*** - Community-based planning principles adopted to facilitate management of their natural	**Partially achieved:** Achieved in the target areas covered by GEF project. However, stalled decentralization process has so far prevented the completed	Maloti Drakensberg Transfrontier Project (GEF, FY02).	Pilot experiences under MDTP are expected to serve as models to other areas and to become an integral part of community and local government planning processes. Project activities are likely to result in sustainable conservation of protected areas, impact economic development around conservation areas, and enhance community participation in planning processes. MDTP experience can be used to cover entire country by

[53] The original target was for 30,000 people living in Senqu-Senqunyane river area to have access to motorable road. Financed by ITP, the government has developed GIS system, however, the GIS only contains information on the spread of villages not individuals, so the rural access index could only be evaluated by number/percentage of villages. Without the project, only 2 out 78 villages were within 2 km to a motorable road, with the project, 14 of 78 will be within the range.

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
resources. - Environmental regulations enforced by Districts and Municipal councils. - Proportion of projects and investments subjected to EIA increase by 20% by 2009	integration of these areas into the community planning and budget process. **Partially achieved** An Environment Bill (2007) is under consideration, and would establish a National Environment Council and Department of Environment, with Assistant Environment Officers to be appointed at the District level. It is envisaged that the establishment of the National Environmental Council will strengthen the institutional framework and enhance NES' role in monitoring and enforcement of environmental legislation in the country. **Achieved -** All projects and investments (100%) are subject to EIA. In this context EIA does not refer to a full EIA study, but the one where environmental impact has been assessed and category of project determined according to WB Environmental Assessment Policy – OP 4.01.		strengthening local governments. Through the Local Government Act, in 2004 Lesotho moved into decentralization, which included agriculture and natural resource management as one of 9 key sectors where authority and management was devolved to local elected councils. However, roles and responsibilities within the decentralized system still not clearly defined. Thus, the whole process of decentralization has been stalled.
3.1 Improve health systems management and efficiency to provide essential health services: ***Indicators:*** - Reduction in average waiting period from 4.5 hours to 2 hours at health facilities by 2009.	**Partially achieved:** Average waiting period reduced to 3 hours and 20 minutes in 2009 (Source: 2009 Annual Joint Review (AJR) Report page 15) **Partially achieved:**	Health Sector Reform Project Phase II (FY06).	Major achievements include improved capacity for service delivery at district level; high immunization rates; improved access to antenatal care and PMTCT; increased HIV testing coverage and TB detection rates; and improved M&E and fiduciary capacity. The GOL health sector reform program made noticeable progress. However, concerns remain. Lesotho is off track to reach MDGs: high maternal mortality rate, high child

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
- Increase in health center client satisfaction from 40% to 80% by 2009. - Increase in percentage of the population residing within 5km walking distance from a health facility (baseline is 79.5%). - Increase in TB cure rate from 52% to 60% by 2008. - Improvement in Life Index of beneficiary population in S-E Corridor based on proxy basket measuring core welfare (index composition and baseline being developed). - Increase percentage of DHMTs that are properly staffed and with office accommodation from 30% to 90% by June 2009	The client satisfaction in services provided in most hospitals in Lesotho increased and was on average 76% in 2009 (Source: 2009 AJR Report, page 15)) **Not achieved:** The proportion of the population living within two hours walking distance from a fixed facility' and several other service targets remained unchanged at 79.5% **Achieved:** For 2008/09 the average TB cure rate reached 66.5% as per data provided by AJR report. **Not Achieved. No data available.** **Partially achieved** Percentage of DHMT that are properly staffed increased and ranges from 40% to 80%. Percentage of DHMTs with office accommodation also increased up to 63% (in 3 districts) and even 100% (in 3 districts). It is 22% in one district. It is difficult to establish averages for the country due to missing data. (Source:2009 AJR Report)	Integrated Transport Project (FY07). Poverty Reduction Support Credit (FY08). Health Sector Reform Project II (FY05) ***Partners:*** AfDB, CARE, DCI, EU, GFATM, UNAIDS, UNDP, UNICEF, and USAID.	mortality rate, and world's third highest HIV adult prevalence are the main reasons for concern. Long-term human resource issues and weak capacity continue to affect service delivery. There is a severe scarcity of health professionals—a long-term strategy is needed. Local governments are at forefront of service delivery but remain institutionally weak.
3.2 Increase access and performance in primary and	**Partially achieved:** Pupil:teacher ratio in 2008: 36:1	Second Education Sector Development	The overall picture is mixed. Primary completion and secondary access are increasing. Primary enrollment grew

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
secondary education ***Indicators:*** - Pupil:classroom ratio declines from 1:65 in 2003 to 1:55 by 2009, and pupils per qualified teacher from 1:69 in 2003 to 1:60 by 2009. - Geographic disparities between schools reduced to less than 5% by 2009. - National Performance Level (NPL) in numeracy at grade 6 increased from 49% in 2003 to 55% by Dec 2007. - National Performance Level in Sesotho literacy at grade 6 increased from 58% in 2003 to 65% by Dec 2007. - National Performance Level in English literacy at grade 6 increased from 45% in 2003 to 50% by Dec 2007. - Share of total education	Pupil: qualified teacher ratio in 2008: 61:1 Primary net enrollment ratio was the same in 2004 and 2006: 83%. Lower secondary coverage (Form A-C) is 51% in 2006 (latest available), compared to 48% in 2004. **Not achieved:** No data available **Achieved:** NPL in numeracy at grade 6 was 58% in 2006 (latest available). **Achieved:** NPL in Sesotho literacy at grade 6 was 69% in 2006 (latest available). **Not achieved:** NPL in English literacy at grade 6 was 39% in 2006 (latest available). **Achieved:** Share of total education recurrent budget	Project Phase II (FY04). Integrated Transport Project (FY07). Poverty Reduction Support Credit (FY08).	with introduction of free public education (FPE), but has stabilized at approximately 425,000, a GER of 127.[54] Extra-large cohorts enrolled immediately after announcement of FPE are passing out of primary education. Subsequent cohorts are smaller but have better survival rates. Despite this healthy trend, at least 60% of pupils repeat at least 1 grade; the overall repetition rate is 21%. Quality seems to have suffered in some areas in expansion, but recent interventions to improve qualified teacher supply, provide in-service training, and provide textbooks have had little chance to be reflected in available data. Building capacity in GOL remains a challenge, which can be aided by efforts of improved donors coordination and enhanced policy dialogue. However, there are very few active donors in sector. For the Bank to maintain a strong presence in sector policy dialogue is important, at least until MoET capacity and systems develop. Emphasis needs to be given to the quality of education and reform in post-basic education.

[54] Primary enrollment in registered schools was 424,855 in 2006, with little variation in the previous 2 years.

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
recurrent budget devoted to primary and secondary education increased from 57% in 2004 to 65% in 2007 - Primary net enrollment ratio increased from 83% in 2004 to 90% by 2007 -	devoted to primary and secondary education reached 64% in 2008/09. **Not Achieved:** Primary net enrollment ratio remained stagnant at 83% between 2004 and 2006		
4.1. Improve capacity for management of public resources at central and decentralized local GOL levels ***Indicators:*** - MTEF introduced in at least 10 ministries by 2009. - Revised Procurement and Financial Management Acts and Regulations adopted by the Government by 2008 and Bank provides budgetary support. - District Development Fund operational by 2007. - GOL transfers financial resources from budget directly to	**Achieved:** All Ministries used a MTEF and produced Budget Framework Papers for 2009/10 and in 2010/11. **Not achieved:** Draft PFMA Bill has been developed by the government. It is with the Attorney General and will be presented to Parliament. **Not achieved and not relevant.** No supporting Bank interventions. **Not achieved and not relevant.** No supporting Bank interventions.	Poverty Reduction Support Credit (FY08). Public Expenditure and Financial Accountability Review (FY06). IDF grant to enhance capacity of monitoring and evaluation in ministry of Finance and Development Planning. Country Procurement Assessment (FY08). Decentralization and demand-driven service delivery (including	An assessment of PFM based on the PFM Performance Measurement Framework (PMF) has been recently conducted jointly by the GOL and its key DPs and a draft report has been prepared. The assessment notes that although a longstanding weakness in budget execution, the internal control and financial reporting, some progress is clearly being made. A multi-year perspective in fiscal planning, expenditure policy and budgeting has been deepened with the adoption of MTEF. However, there is need for a greater sense of urgency particularly with regard to the legislative requirements of the PFM reform. There have been delays in the submission of the Public Financial Management and Accountability (PFMA) Bill, which is required to support legally the new business process. The decentralization reform program has a focus on improving decentralized service delivery and decision making with the aim of reducing poverty. The National Decentralization Action Plan (NDAP) has been prepared and endorsed by Cabinet. However, the key bottleneck is a weak local capacity to implement the reform.

Expected result under CAS (1)	Actual outcome (2)	Supporting WBG program (3)	Progress toward long-term development objectives (4): Lessons learned
Local Government Assemblies.		intergovernmental fiscal decentralization) (FY07).	
- Timely poverty data made available within National Monitoring and Evaluation System.	**Partially Achieved:** The National Monitoring and Evaluation System has been set up to improve the collection, dissemination and use of data across Lesotho in the Department of Development Planning in MFDP. One of the first activities has been to compile an extensive database of all development data produced in Lesotho. In parallel, the Bureau of Statistics (BOS) undertook a concerted effort to document and disseminate existing household survey data via their website.	Poverty Assessment (FY09). ***Partners:*** DCI, DfID, EU, MCC, UNDP.	Strengthening Statistics and the National Monitoring and Evaluation System requires special attention as a tool of making informed policy decisions.
- National Statistical Council fully operational and functioning.	**Partially Achieved:** The BOS has taken important steps towards the development of a National Strategy for Development of Statistics (NSDS) based on Paris 21 Principles. It has completed the inception report on the design of NSDS, conducted stakeholder consultations and completed situation analysis in key line ministries.		
- Government approves and put in place a harmonized mechanism for monitoring the PRS by June 2008	**Achieved:** Joint government-donor PAF has been developed and annually reviewed		

Annex 3: CONSULTATION ON LESOTHO CAS, 2010 – 2014.

1. As part of the preparation of the CAS, 2010-14, a series of consultations were organized over a period of eighteen months with key stakeholders. The first of these took place on September 29-30, 2008 and involved representatives from the GOL, donors, civil society and the private sector, and the World Bank. This meeting served to define key objectives that the GOL wished to pursue over the medium term and constraints to their achievement. The GOL identified two priorities in the area of poverty reduction: improved social protection and the promotion of shared and sustainable growth. Much of the discussion focused on the latter objective.

2. At the session, there was agreement that the promotion of shared and sustainable growth required actions in several areas. The first of these was a more efficient public sector framework which would focus on facilitating and encouraging the private sector. In this area, several domains of public intervention were identified: improved business climate, enhanced access to finance, addressing the HIV/AIDs pandemic, alignment of the education system with economic needs, better infrastructure, and improved land management. Another key area for the promotion of shared and sustainable growth was private sector development through the promotion of labor-intensive sectors. In this area, specific sectoral constraints were identified and concrete actions proposed for addressing these constraints. The third area identified as central to the promotion of shared and sustainable growth was regional integration. Here, as well, specific actions were identified to allow Lesotho to take fuller advantage of its regional context.

3. A broad theme that was discussed during the September 2008 meeting was the need to improve implementation of policies and strategies. Much of the discussion here focussed on capacity weaknesses and the actions that could be taken to enhance local capacity. Specific solutions were proposed for capacity problems in the public and private sectors as well as in civil society organizations. The need to improve public sector institutions received considerable attention. There was also recognition of the need for better communication among key stakeholders; e.g., between the GOL and civil society, between donors and the Government, and within the private sector.

4. Finally, the meeting generated specific suggestions for the World Bank CAS, notably the need to be more explicit about how results are to be achieved and the need to improve the approach to capacity building in Bank activities.

5. At the September 2008 meeting, Finance Minister Thahane suggested that before moving on with the CAS preparation the Bank should prepare a series of policy notes which can help Lesotho increase its productive capacity in response to the possible decline in SACU revenue, address constraints to growth, and explore prospects for new growth sectors such as agriculture and tourism. These policy notes were subsequently prepared and discussed with the Minister and the Lesotho delegation during the Spring Meetings in 2009 and then with the whole Cabinet on July 20, 2009. The GOL has acknowledged that the policy notes provided the analytical underpinning for the development of the Government's growth strategy and the GOL's budget for 2010/11

6. More recently, the World Bank (WB) and Government of Lesotho (GOL) organized a multi-stakeholder forum on Lesotho's country assistance strategy (CAS), on March 18-19, 2010. The participants of this development dialogue platform comprised GOL officials, academics, private sector representatives, international and local NGOs, faith based organisations (FBOs) and youth organisations.

7. In the opening session of the forum, Minister Thahane expressed the GOL's appreciation for the well established development partnership with World Bank that is based on openness, frankness and honesty. In the 2009-10 periods, Lesotho is dealing with a multi-faceted crisis given the adverse impact of an external economic crisis and deepening poverty and inequality and the imperatives of fiscal adjustment and public service efficiencyTo address these interrelated challenges, the GOL needs to have clear policies and strategies. Given the GOL's limited resources, its role is to create an enabling framework for private sector led growth, level the playing field, provide a minimum infrastructure platform and develop a skilled and healthy human resource base. Meanwhile GOL still needs to enhance its service delivery to poor and vulnerable citizens and combat HIV/AIDS effectively.

8. Ms. Lebona, Director–MOFDP, then outlined Lesotho's long term and medium term development challenges that are based on a clear appreciation of threats and constraints as well as opportunities facing the Country. In summary, GOL's current priorities are;

- A shared growth strategy which is broad based and addresses inequalities.
- Expanding the production base by improving the investment climate for the private sector and enabling the doing of business
- Human development that also protects the poor, vulnerable and youth.
- Effective public service delivery at the central and local levels
- Effective strategies to combat HIV/ADS.

9. The Government Secretary, Mr. Sekhamane presented the background, rationale and major components of GOL's service delivery agenda (SDA) to be implemented by the Public Service at the central, sectoral and local levels. SDA is a radical approach to achieve the MDGs and is an appropriate response to the multi-faceted crisis facing Lesotho in 2010 – 2014. The key SDA principles are; ethos of efficient service to citizens, accountability, monitoring and evaluation, listening to the people and addressing their needs. Accordingly, the Prime Minister and GOL's cabinet are fully committed to the overall goals of the SDA campaign. While appreciating the SDA, Participants wanted the full involvement of Non-State Actors (NSAs), Faith Based Organizations (FBOs) and Traditional Authorities/Chiefs in the implementation of the SDA.

10. The World Bank representative presented the key themes of the envisioned CAS for 2010-14: fiscal adjustment and public sector efficiency; human development and improved service delivery; and economic diversification and improved competitiveness. These themes were endorsed as appropriate by the forum participants.

11. The key messages, issues and questions that emerged in plenary discussions were the following. While Lesotho's long term Vision 2020 goals are appreciated, these 2010 consultations provide an opportunity for a mid-term review of Vision 2020 goals. Lesotho needs to derive lessons from implementing the 8 priorities of the poverty reduction strategy (PRS) since 2004/05. Lesotho must manage brain drain through effective human resource retention strategies while taking full advantage of its location within RSA, SACU and SADC region. Lesotho faces a crisis of worsening poverty, high unemployment, deteriorating human development indicators, inequalities and chronic vulnerability and environmental degradation. To achieve shared growth in this context, serious choices and strategic options have to be pursued, such as investment climate reform to enable private sector and FDI led growth, supporting growth of SMMES, commercializing agriculture, reducing economic and social costs of rural to urban mobility, adjusting the size of the public sector equitably to ensure effective service delivery to poor, rural and marginalized communities. Generally, there is need to do much more with much less resources.

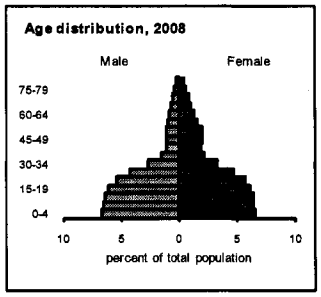
Annex 4: DONOR ACTIVITIES MATRIX BREAKDOWN BY CAS 2010 – 2014 AREAS OF ENGAGEMENT

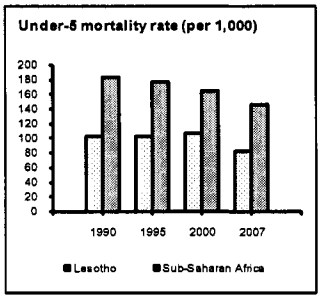
Development partner	Area of Engagement 1: Fiscal adjustment and Public Sector Efficiency	Area of Engagement 2: Advance human development and improved service delivery	Area of Engagement 3: Economic Diversification and improved Competitiveness
African Development Bank (AfDB)	• Poverty Reduction Support Programme (Budget Support)		
Department for International Development (DFID) (UK)	• Macroeconomic Framework • Public Financial Management (PFM) • Capacity Building & Institutional Support	• Agriculture • HIV & AIDS • Social Protection	• Trade
European Commission (EC)	• General Budget Support	• Human Development • Support to orphaned and vulnerable children	• ITP • Water and Sanitation
PEPFAR		• HIV & AIDS	
Global Fund (GF)		• HIV & AIDS and TB	
GTZ	• Capacity Building & Inst. Support	• Governance	• Agriculture
Irish Aid	• Public Financial Management (PFM) • Capacity Building & Inst. Support	• FTI Catalytic Fund • Health • Governance • HIV & AIDS	
IFAD			• Agriculture
Government of Japan		• Education	
RSA			• Metolong Dam (water sector)
Kuwait Fund		• Health	• Metolong Dam (water sector) • Road Transport
Saudi Fund			• Metolong Dam (water sector)
OPEC			• Metolong Dam (water sector)
IDA/IFC*	• PRSC • CEM – Policy Notes • Investment Climate Assessment • ROSC – Accounting & Auditing • PER • TA Statistics • TA in PFM	• HIV/AIDS TA project • FTI Catalytic Fund • HSRP • Governance & Capacity Assessment Study • Poverty Assessment	• PSC project • ITP • WSIP II • PPP referral* hospital construction
UN		• Democratic governance • HIV/AIDS	• Energy & Environment

		• Poverty & Food Security • Support to orphaned & vulnerable children	
USA – MCC		• Health	• Metolong Dam (water sector) • Private Sector Development

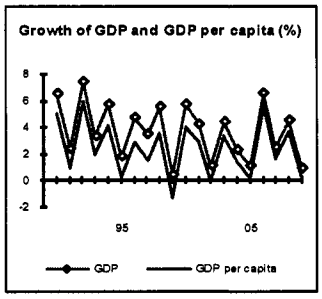
Annex A2 – Lesotho at a glance

Key Development Indicators	Lesotho	Sub-Saharan Africa	Lower middle income
(2009)			
Population, mid-year (millions)	2.1	818	3,702
Surface area (thousand sq. km)	*30*	24,242	32,309
Population growth (%)	0.9	2.5	1.2
Urban population (% of total population)	*25*	36	41
GNI (Atlas method, US$ billions)	2.1	885	7,692
GNI per capita (Atlas method, US$)	1,020	1,082	2,078
GNI per capita (PPP, international $)	*2,000*	1,991	4,592
GDP growth (%)	0.9	5.0	7.6
GDP per capita growth (%)	0.0	2.5	6.3
(most recent estimate, 2003–2009)			
Poverty headcount ratio at $1.25 a day (PPP, %)	43	51	..
Poverty headcount ratio at $2.00 a day (PPP, %)	62	73	..
Life expectancy at birth (years)	43	52	68
Infant mortality (per 1,000 live births)	68	89	46
Child malnutrition (% of children under 5)	17	27	26
Adult literacy, male (% of ages 15 and older)	..	71	88
Adult literacy, female (% of ages 15 and older)	..	54	77
Gross primary enrollment, male (% of age group)	115	103	112
Gross primary enrollment, female (% of age group)	114	93	106
Access to an improved water source (% of population)	78	58	86
Access to improved sanitation facilities (% of population)	36	31	52





Net Aid Flows	1980	1990	2000	2009 [a]
(US$ millions)				
Net ODA and official aid	93	139	37	130
Top 3 donors (in 2007):				
United States	18	14	1	19
Ireland	4	3	9	19
European Commission	5	14	10	17
Aid (% of GNI)	13.4	15.4	3.8	6.5
Aid per capita (US$)	72	87	19	64
Long-Term Economic Trends				
Consumer prices (annual % change)	15.7	11.6	6.1	7.2
GDP implicit deflator (annual % change)	41.5	11.6	2.4	3.4
Exchange rate (annual average, local per US$)	0.8	2.6	6.9	8.7
Terms of trade index (2000 = 100)	..	72	100	157



					1980–90	1990–2000	2000–09
					(average annual growth %)		
Population, mid-year (millions)	1.3	1.6	1.9	2.1	2.1	1.6	1.0
GDP (US$ millions)	431	541	746	1,579	4.4	4.0	3.1
		(% of GDP)					
Agriculture	22.4	24.9	12.3	8.4	0.0	2.8	-2.4
Industry	24.2	34.4	31.6	34.1	8.9	5.5	3.6
Manufacturing	7.7	14.6	14.0	17.0	9.4	7.9	5.7
Services	53.4	40.7	56.1	57.5	2.5	4.5	3.7
Household final consumption expenditure	142.1	123.3	83.3	76.9	-0.1	1.8	11.5
General gov't final consumption expenditure	10.0	25.8	41.7	50.4	15.2	8.1	6.4
Gross capital formation	37.0	56.1	44.2	33.2	9.3	0.2	-0.5
Exports of goods and services	21.0	18.1	34.2	51.2	4.0	10.3	10.0
Imports of goods and services	110.1	123.2	103.4	111.7	2.4	2.7	12.2
Gross savings	71.8	39.6	23.6	32.9			

Note: Figures in italics are for years other than those specified. 2009 data are preliminary. Group data are through 2008. .. indicates data are not available.
a. Aid data are for 2007.

Development Economics, Development Data Group (DECDG) and AFTP1

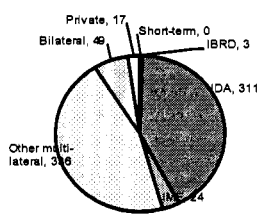
Lesotho

Balance of Payments and Trade	2000	2009
(US$ millions)		
Total merchandise exports (fob)	212	739
Total merchandise imports (cif)	769	1,759
Net trade in goods and services	-516	-955
Current account balance	-153	-5
as a % of GDP	-20.5	-0.3
Workers' remittances and compensation of employees (receipts)	252	379
Reserves, including gold	459	1,131

Central Government Finance (In Calendar Years)		
(% of GDP)		
Current revenue (excl. grants)	49.2	63.4
Tax revenue	37.3	57.4
Current expenditure	46.5	52.8
Overall surplus/deficit	-8.6	-7.9
Highest marginal tax rate (%)		
Individual	..	..
Corporate	..	..

External Debt and Resource Flows		
(US$ millions)		
Total debt outstanding and disbursed	672	740
Total debt service	62	34
Debt relief (HIPC, MDRI)	–	–
Total debt (% of GDP)	90.1	46.9
Total debt service (% of exports)	11.2	4.2
Foreign direct investment (net inflows)	118	*82*
Portfolio equity (net inflows)	..	*0*

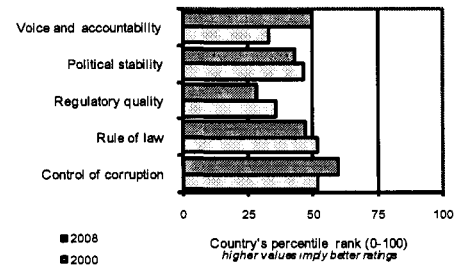
Composition of total external debt, 2009



US$ millions

Private Sector Development	2000	2008
Time required to start a business (days)	–	40
Cost to start a business (% of GNI per capita)	–	37.8
Time required to register property (days)	–	101
Ranked as a major constraint to business (% of managers surveyed who agreed)	**2000**	**2008**
Access to/cost of financing	..	*54.1*
Crime	..	*45.9*
Stock market capitalization (% of GDP)	..	..
Bank capital to asset ratio (%)	..	*14.6*

Governance Indicators, 2000 and 2008



Source: Kaufmann-Kraay-Mastruzzi, World Bank

Technology and Infrastructure	2000	2008
Paved roads (% of total)	18.3	..
Fixed line and mobile phone subscribers (per 100 people)	2	*21*
High technology exports (% of manufactured exports)	0.3	*0.0*

Environment		
Agricultural land (% of land area)	77	*77*
Forest area (% of land area)	0.2	*0.3*
Nationally protected areas (% of land area)	..	*0.2*
Freshwater resources per capita (cu. meters)	*2,707*	*2,607*
Freshwater withdrawal (billion cubic meters)	0.1	..
CO2 emissions per capita (mt)	..	..
GDP per unit of energy use (2005 PPP $ per kg of oil equivalent)	..	..
Energy use per capita (kg of oil equivalent)	..	..

World Bank Group portfolio	2000	2008
(US$ millions)		
IBRD		
Total debt outstanding and disbursed	59	3
Disbursements	10	0
Principal repayments	4	1
Interest payments	3	0
IDA		
Total debt outstanding and disbursed	183	303
Disbursements	8	17
Total debt service	4	9
IFC *(fiscal year)*		
Total disbursed and outstanding portfolio	0	0
of which IFC own account	0	0
Disbursements for IFC own account	0	0
Portfolio sales, prepayments and repayments for IFC own account	0	0
MIGA		
Gross exposure	24	*0*
New guarantees	0	*0*

Note: Figures in italics are for years other than those specified. 2009 data are preliminary. 4/21/10
.. indicates data are not available. – indicates observation is not applicable.

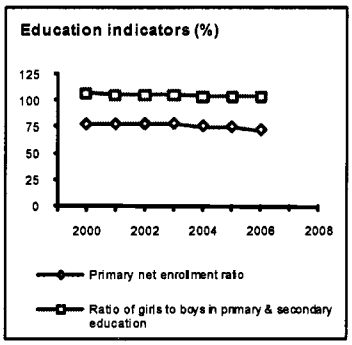
Development Economics, Development Data Group (DECDG) and AFTP1

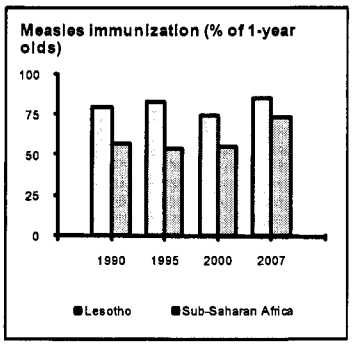
Millennium Development Goals

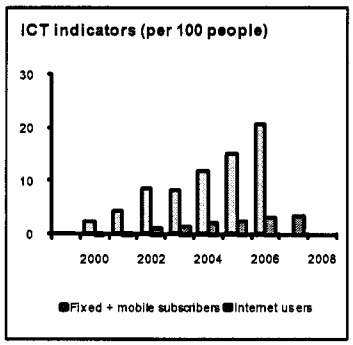
Lesotho

With selected targets to achieve between 1990 and 2015
(estimate closest to date shown, +/- 2 years)

	Lesotho			
Goal 1: halve the rates for extreme poverty and malnutrition	**1990**	**1995**	**2000**	**2008**
Poverty headcount ratio at $ 1.25 a day (PPP, % of population)	..	47.6	..	*43.4*
Poverty headcount ratio at national poverty line (% of population)	..	*49.2*	*68.0*	..
Share of income or consumption to the poorest quintile (%)	..	1.5	..	*3.0*
Prevalence of malnutrition (% of children under 5)	..	..	15.0	*16.6*
Goal 2: ensure that children are able to complete primary schooling				
Primary school enrollment (net, %)	*72*	..	78	*72*
Primary completion rate (% of relevant age group)	58	..	60	*78*
Secondary school enrollment (gross, %)	25	30	30	*37*
Youth literacy rate (% of people ages 15-24)	..	..	..	..
Goal 3: eliminate gender disparity in education and empower women				
Ratio of girls to boys in primary and secondary education (%)	*123*	..	107	*104*
Women employed in the nonagricultural sector (% of nonagricultural employment)	..	*52*	*51*	..
Proportion of seats held by women in national parliament (%)	..	5	4	25
Goal 4: reduce under-5 mortality by two-thirds				
Under-5 mortality rate (per 1,000)	102	102	107	*84*
Infant mortality rate (per 1,000 live births)	81	81	84	*68*
Measles immunization (proportion of one-year olds immunized, %)	80	83	74	*85*
Goal 5: reduce maternal mortality by three-fourths				
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	*960*
Births attended by skilled health staff (% of total)	..	*50*	60	*55*
Contraceptive prevalence (% of women ages 15-49)	*23*	..	30	*37*
Goal 6: halt and begin to reverse the spread of HIV/AIDS and other major diseases				
Prevalence of HIV (% of population ages 15-49)	0.8	14.2	23.9	*23.2*
Incidence of tuberculosis (per 100,000 people)	184	323	553	*637*
Tuberculosis cases detected under DOTS (%)	..	63	78	*16*
Goal 7: halve the proportion of people without sustainable access to basic needs				
Access to an improved water source (% of population)	..	77	77	*78*
Access to improved sanitation facilities (% of population)	..	33	34	*36*
Forest area (% of total land area)	0.2	0.2	0.2	*0.3*
Nationally protected areas (% of total land area)	..	..	..	*0.2*
CO2 emissions (metric tons per capita)	..	..	..	..
GDP per unit of energy use (constant 2005 PPP $ per kg of oil equivalent)	..	..	..	..
Goal 8: develop a global partnership for development				
Telephone mainlines (per 100 people)	0.8	1.0	1.2	*2.7*
Mobile phone subscribers (per 100 people)	0.0	0.0	1.1	28.8
Internet users (per 100 people)	0.0	*0.0*	0.2	3.6
Personal computers (per 100 people)	..	..	*0.1*	*0.3*







Note: Figures in italics are for years other than those specified. .. indicates data are not available. 4/21/10

Development Economics, Development Data Group (DECDG).

Lesotho
Annex B2 – Selected Indicators* of Bank Portfolio Performance and Management
As of April 5, 2010

Indicator	2007	2008	2009	2010
Portfolio Assessment				
Number of Projects Under Implementation [a]	8	8	6	6
Average Implementation Period (years) [b]	3.0	3.2	3.5	2.2
Percent of Problem Projects by Number [a, c]	12.5	0.0	0.0	16.7
Percent of Problem Projects by Amount [a, c]	12.4	0.0	0.0	14.0
Percent of Projects at Risk by Number [a, d]	12.5	0.0	0.0	16.7
Percent of Projects at Risk by Amount [a, d]	12.4	0.0	0.0	14.0
Disbursement Ratio (%) [e]	32.2	18.9	39.7	19.4
Portfolio Management				
CPPR during the year (yes/no)	no	yes	no	no
Supervision Resources (total US$) **	1300.0	736.0	797.0	391.0
Average Supervision (US$/project) **	162.5	92.0	99.6	55.9

Memorandum Item	Since FY80	Last Five FYs
Proj Eval by OED by Number	29	3
Proj Eval by OED by Amt (US$ millions)	375.5	72.8
% of OED Projects Rated U or HU by Number	34.5	33.3
% of OED Projects Rated U or HU by Amt	23.7	31.0

a. As shown in the Annual Report on Portfolio Performance (except for current FY).

b. Average age of projects in the Bank's country portfolio.

c. Percent of projects rated U or HU on development objectives (DO) and/or implementation progress (IP).

d. As defined under the Portfolio Improvement Program.

e. Ratio of disbursements during the year to the undisbursed balance of the Bank's portfolio at the beginning of the year: Investment projects only.

* All indicators are for projects active in the Portfolio, with the exception of Disbursement Ratio, which includes all active projects as well as projects which exited during the fiscal year.

Lesotho
Annex B3 - IBRD / IDA Program Summary
As of April 5, 2010

Proposed IBRD/IDA Base-Case Lending Program [a]

Fiscal Year	*Proj. ID*	*US$(M)*	*Strategic Rewards b (H/M/L)*	*Implementation b Risks (H/M/L)*
2010	HIV/AIDS TAL	5.0	H	M
	PRSC II	25.0	H	H
	Integrated Transport Additional Financing	15.0	M	M
2011	PRSC III	15.0	H	H
	Agriculture/Rural Development	10.0	M	M
2012	PRSC IV	15.0	H	H
	Water Sector APL 2	5.0	H	M
	Human Development	5.0	H	M
	TOTAL	**95.0**		

/a This table presents the proposed lending program for FY10-12

/b For each project, the strategic rewards and implementation risks are indicated according to expectation: high (H), moderate (M), or low (L)

Lesotho
Annex B3 – IFC and MIGA Program - FY2006-2009

	2006	2007	2008	2009*
Commitments (US$m)				
Gross	0	0	0	0
Net**	0	0	0	0
Net Commitments by Sector (%)	0	0	0	0
Net Commitments by Investment Instrument (%)	0	0	0	0
MIGA facilitated investments into Lesotho Gross Exposure (US$ mil)	0	0	0	0
MIGA facilitated investments financed by investors by Basotho Investors	0	0	0	0
MIGA Gross Exposure (US$ mil)	0	0	0	0

* As of February 28, 2010
** IFC's Own Account only

Lesotho
Annex B4 – Summary of Nonlending Services
As of April 5, 2010

Product	*Completion FY*	*Cost (US$000)*	*Audience* [a]	*Objective* [b]
Recent completions				
Decentralization & Demand Driven Service Deliv	FY07	100	G, D, B	KG, PS
HIV/AIDS Incidence Analysis	FY07	32	G, D, B	KG, PS
IF Follow-up	FY08		G, D, B	KG, PS
CPAR	FY08	60	G, D, B	KG, PS
Poverty Gender Social Assessment	FY09	50	G, D, B	KG, PS
Health Sector Review & PER	FY10	170	G, D, B	KG, PS
Underway				
Country Economic Memorandum/Policy Notes	FY10	200	G, D, B	KG, PS
Country Assistance Strategy	FY10	200	G, D, B	KG, PD
ICA Policy Notes	FY10	50	G, B, P	KG, PD, PS
Accounting and Auditing ROSC	FY10	70	G, B, B	KG, PD
PPP Industrial Space Development	FY10	50	G, B, P	KG, PB
PPIAF Reg Model Power and Water Sector	FY10	287	G, D, P	KG, PS
Health Sector Review	FY10		G, D, P	KG, PD
Planned				
PER	FY11		G, D, P	KG, PD, PS
Post Basic Education Study	FY11		G, D, P	KG, PD
Governance and Cap. Assessment	FY11		G, D, B	KG, PS

a. Government, donor, Bank, public dissemination.
b. Knowledge generation, public debate, problem-solving.

Annex B6: Key Economic Indicators

Indicator	Actual			Estimate			Projected		
	2005	2006	2007	2008	2009	2010	2011	2012	2013
National accounts (as % of GDP)									
Gross domestic product[a]	100	100	100	100	100	100	100	100	100
Agriculture	9	10	8	8	8	8	8	8	7
Industry	35	37	39	38	34	35	36	38	39
Services	56	54	53	54	58	57	56	54	54
Total Consumption	130	125	125	124	127	127	117	118	112
Gross domestic fixed investment	24	25	28	30	33	40	44	42	38
Government investment	8	8	10	13	16	22	26	24	19
Private investment	16	17	18	17	18	18	18	18	19
Exports (GNFS)[b]	53	54	56	59	51	51	50	48	50
Imports (GNFS)	107	103	109	113	112	117	110	109	100
Gross domestic savings	-30	-25	-25	-24	-27	-27	-17	-18	-12
Gross national savings[c]	16	29	42	40	33	16	21	23	30
Memorandum items									
Gross domestic product (US$ million at current prices)	1315	1417	1577	1594	1579	1677	1782	1894	2010
GNI per capita (US$, Atlas method)	760	900	960	1050	1020	1010	1050	1100	1150
Real annual growth rates (%, calculated from 95 prices)									
Gross domestic product at market prices	1.1	6.5	2.4	4.5	0.9	3.7	3.5	3.9	2.1
Gross Domestic Income	0.6	9.7	7.7	11.5	-1.7	4.0	6.1	5.0	4.6
Real annual per capita growth rates (%, calculated from 95 prices)									
Gross domestic product at market prices	0.1	5.5	1.5	3.6	0.0	2.9	2.6	3.0	1.2
Total consumption	3.1	3.4	8.4	7.6	2.2	5.8	-3.0	4.0	-4.0
Private consumption	2.0	1.7	10.0	1.1	2.2	11.1	-2.2	5.4	-4.5
Balance of Payments (US$ millions)									
Exports (GNFS)[b]	703	759	880	936	809	849	892	918	1002
Merchandise FOB	651	699	804	870	739	771	813	837	919
Imports (GNFS)[b]	1411	1462	1713	1796	1764	1966	1967	2060	2006
Merchandise FOB	1307	1367	1603	1687	1656	1848	1847	1934	1879
Resource balance	-708	-703	-833	-860	-955	-1117	-1075	-1142	-1004
Net current transfers	300	389	628	511	521	308	212	334	370
Current account balance	-104	66	221	152	-5	-392	-413	-355	-158
Net private foreign direct investment	93	112	130	109	81	64	66	80	82
Long-term loans (net)	38	-111	-43	-67	26	-52	-97	44	9
Official	-11	1	13	16	8	56	78	94	45
Private	49	-112	-56	-83	17	-108	-175	-50	-37
Other capital (net, incl. errors & ommissions)	1	70	-25	-40	108	189	257	247	145
Change in reserves[d]	-29	-138	-282	-154	-210	190	187	-16	-78
Memorandum items									
Resource balance (% of GDP)	-53.8	-49.6	-52.8	-54.0	-60.5	-66.6	-60.3	-60.3	-50.0
Real annual growth rates (YR95 prices)									
Merchandise exports (FOB)	-8.1	2.0	3.7	0.0	-18.5	1.6	-5.5	-7.6	0.6
Merchandise imports (CIF)	-0.4	3.3	11.9	7.8	-1.1	9.6	-2.7	1.5	-6.2

(Continued)

Lesotho - Key Economic Indicators (Continued)

Indicator	Actual			Estimate			Projected		
Indicator	2005	2006	2007	2008	2009	2010	2011	2012	2013
Public finance (as % of GDP at market prices)[e]									
Current revenues	51.1	60.9	62.1	66.2	66.3	49.0	50.1	57.0	52.8
Current expenditures	**39.5**	38.8	40.3	47.9	51.5	44.4	41.5	40.4	38.6
Current account surplus (+) or deficit (-)	11.6	22.0	21.8	18.3	14.8	4.6	8.6	16.6	14.2
Capital expenditure	7.6	6.9	11.1	13.8	16.1	24.0	26.9	23.6	16.9
Overall balance (including grants)[f]	**4.1**	15.2	8.7	1.6	-2.7	-19.3	-18.3	-7.0	-2.7
Foreign financing	-3.0	-2.5	0.2	1.3	0.2	3.9	4.0	4.0	1.1
Monetary indicators									
M2/GDP	31.0	36.6	36.7	37.0	42.9	44.4	46.1	47.8	49.7
Growth of M2 (%)	9.1	35.4	16.4	19.7	20.8	14.0	14.4	13.6	13.2
Private sector credit growth / total credit growth (%)	656.8	-25.4	-19.2	-81.8	102.0	11.2	25.0	59.0	65.5
Price indices(YR95 =100)									
Merchandise export price index	176.2	185.6	205.8	222.6	232.3	238.6	266.2	296.6	323.5
Merchandise import price index	**98.5**	98.8	103.4	100.6	99.9	101.6	104.5	107.9	112.0
Merchandise terms of trade index	178.9	187.9	199.0	221.3	232.6	234.8	254.7	274.9	289.0
Real interest rates [g]	7.2	6.9	7.8	9.8	10.8	11.8	12.8		
Consumer price index (% change)	3.4	6.1	8.0	10.7	7.2	6.3	6.0	5.7	5.0
GDP deflator (% change)	6.3	7.6	13.3	13.4	3.4	6.2	6.3	5.5	6.6

Sources: LDB and in turn from Lesotho authorities, IMF and WB staff estimates and projections.

a. GDP at factor cost
b. "GNFS" denotes "goods and nonfactor services."
c. Includes net unrequited transfers excluding official capital grants.
d. Includes use of IMF resources.
e. Data is in fiscal years which begin in April and refers to consolidated central government.
f. Includes unidentified expenditure.
g. The average effective rate on three-month treasury bills.

Annex B7- Key Exposure Indicators

Indicator	Actual			Estimated			Projected		
	2005	2006	2007	2008	2009	2010	2011	2012	2013
Total debt outstanding and disbursed (TDO) (US$m)a	718	773	925	738	740	810	975	1140	1249
Net disbursements (US$m)a	-44	-8	4	0	5	53	75	91	46
Total debt service (TDS) (US$m)a	79	46	98	47	35	36	40	45	46
Debt and debt service indicators (%)									
TDO/XGSb	66.3	65.0	65.9	50.3	58.1	61.9	70.3	80.3	81.6
TDO/GDP	54.6	54.6	58.7	46.3	46.9	48.3	54.7	60.2	62.1
TDS/XGS	7.3	3.8	7.0	3.2	2.7	2.7	2.9	3.2	3.0
Concessional/TDO	76.0	71.9	64.4	83.8	85.1	79.0	65.4	55.1	49.1
IBRD exposure indicators (%)									
IBRD DS/public DS	5.2	9.3	4.2	2.7	2.1	2.0	1.7	1.6	0.7
Preferred creditor DS/public DS (%)c	32.1	56.0	30.8	75.3	79.0	78.8	71.5	65.0	58.6
IBRD DS/XGS	0.4	0.4	0.3	0.1	0.1	0.1	0.1	0.1	0.0
IBRD TDO (US$m)d	13	9	4	3	3	0	0	0	0
Of which present value of guarantees (US$m)	0	0	0	0	0	0	0	0	0
Share of IBRD portfolio (%)	0	0	0	0	0	0	0	0	0
IDA TDO (US$m)d	258	275	293	303	311	325	323	324	332
IFC (US$m)									
Loans	0	0	0	0	0	0	0	0	0
Equity and quasi-equity c	0	0	0	0	0	0	0	0	0
MIGA									
MIGA guarantees (US$m)	0	0	0	0	0	0*	0	0	0

Sources: LDB and in turn from Lesotho authorities, IMF and WB staff estimates and projections.

a. Includes public and publicly guaranteed debt, private nonguaranteed, use of IMF credits and net short-term capital.

b. "XGS" denotes exports of goods and services, including workers' remittances.

c. Preferred creditors are defined as IBRD, IDA, the regional multilateral development banks, the IMF, and the Bank for International Settlements.

d. Includes present value of guarantees.

e. Includes equity and quasi-equity types of both loan and equity instruments

* as of March 30, 2010

Lesotho
Annex B8 : (IFC) - Committed and Outsanding Investment Portfolio

As of April 5, 2010
(In USD Millions)

		Committed					Outstanding				
FY Approval	Company	Loan	Equity	**Quasi Equity	*GT/RM	Participant	Loan	Equity	**Quasi Equity	*GT/RM	Participant
none											

Lesotho
Annex B8 – Operations Portfolio (IBRD/IDA and Grants)

As of April 21, 2010

Closed Projects	
IBRD/IDA *	
Total Disbursed (Active)!	31.44
of which has been repaid	0.00
Total Disbursed (Closed)	103.74
of which has been repaid	101.38
Total Disbursed (Active + Closed)	135.17
of which has been repaid	101.38
Total Undisbursed (Active)	72.17
Total Undisbursed (Closed)	0.00
Total Undisbursed (Active + Closed)	72.17

Active Projects

Project ID	Project Name	Last PSR Supervision Rating: Development Objectives	Last PSR Supervision Rating: Implementation Progress	Fiscal Year	Original Amount in US$ Millions: IBRD	IDA	GRANT	Cancel.	Undisb.	Difference Between Expected and Actual Disbursements[a/]: Orig.	Frm Rev'd
P112817	LS-PRSC II			2010		25			24.62		
P107375	LS-HIV & AIDS TAL (FY10)	S	S	2010		5			4.99	0.33	
P075566	LS-Integr Transp SIL (FY07)	S	S	2007		23.5			6.99	5.90	
P088544	LS-Priv Sec Competitiveness	MS	MS	2007		8.1			5.76	2.36	
P056418	LS-Water Sec Improvements APL	MS	MU	2005		14.1			3.72	3.06	
P108143	LS-Water Sec Improvements APL	S	S	2009		25			26.09	1.95	
Overall Re: t						**100.7**			**72.17**	**13.61**	

MAP SECTION

IBRD 33434

LESOTHO

SELECTED CITIES AND TOWNS
DISTRICT CAPITALS
NATIONAL CAPITAL
RIVERS
MAIN ROADS
RAILROADS
DISTRICT BOUNDARIES
INTERNATIONAL BOUNDARIES

SOUTH AFRICA
SOUTH AFRICA
27°E
28°E
29°E
29°S
30°S
Caledon
Orange
Mohokare
Libono
Mont-aux-Sources (3,282 m)
Butha-Buthe
BUTHA-BUTHE
Leribe
Maputsoe
LERIBE
Pitseng
Peka
Mapoteng
Teyateyaneng
BEREA
MASERU
Machache (2,885 m)
Mazenwood
Roma
MASERU
Ranko
Matsieng
Thaba Putsoa (3,095 m)
Semonkong
MAFETENG
Mafeteng
Tsoloane
MOHALE'S HOEK
Mohale's Hoek
Mekaling
Mount Moorosi
QUTHING
Quthing
Sinxondo
Sekake
QACHA'S NEK
Qacha's Nek
Sehlabathebe
Mashai
Mantsonyane
Thaba-Tseka
THABA-TSEKA
MOKHOTLONG
Mokoeng
Mokhotlong
Maluti Mtns.
Thaba-Phafane (3,250m)
Seqoqo (3,394 m)
Njesuthi (3,446 m)
Makheka (3,461 m)
Thabana Ntlenyana 3,482 m)
Drakensberg Mtns.
To Fouriesburg
To Senekal
To Clocolan
To Ladybrand
To Dewetsdorp
To Zastron
To Zastron
To Sterkspruit
To Matatiele
To Matatiele
To Himeville
0 10 20 30 40 50 Kilometers
0 10 20 30 Miles

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