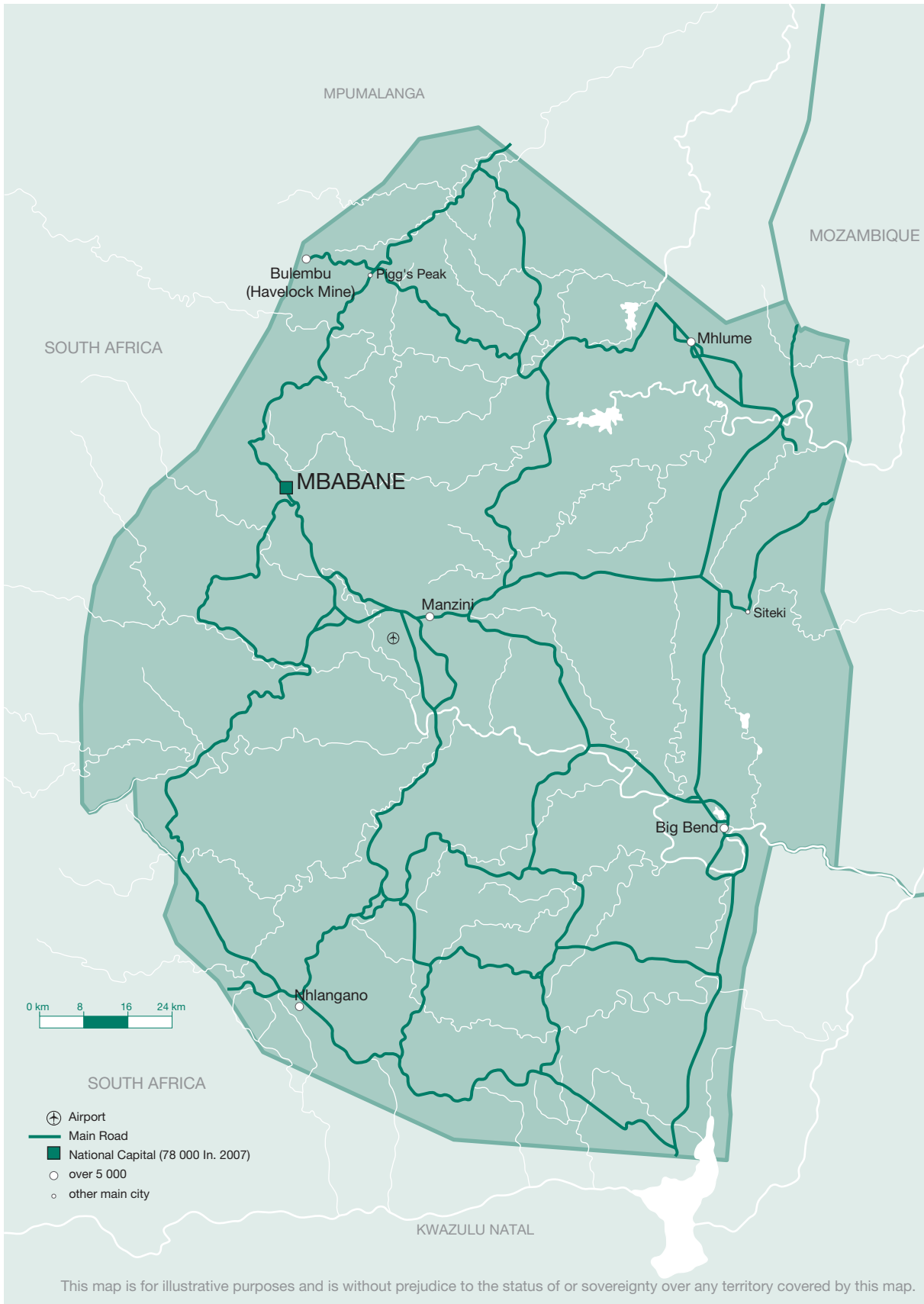


Swaziland

2011



www.africaneconomicoutlook.org



Swaziland

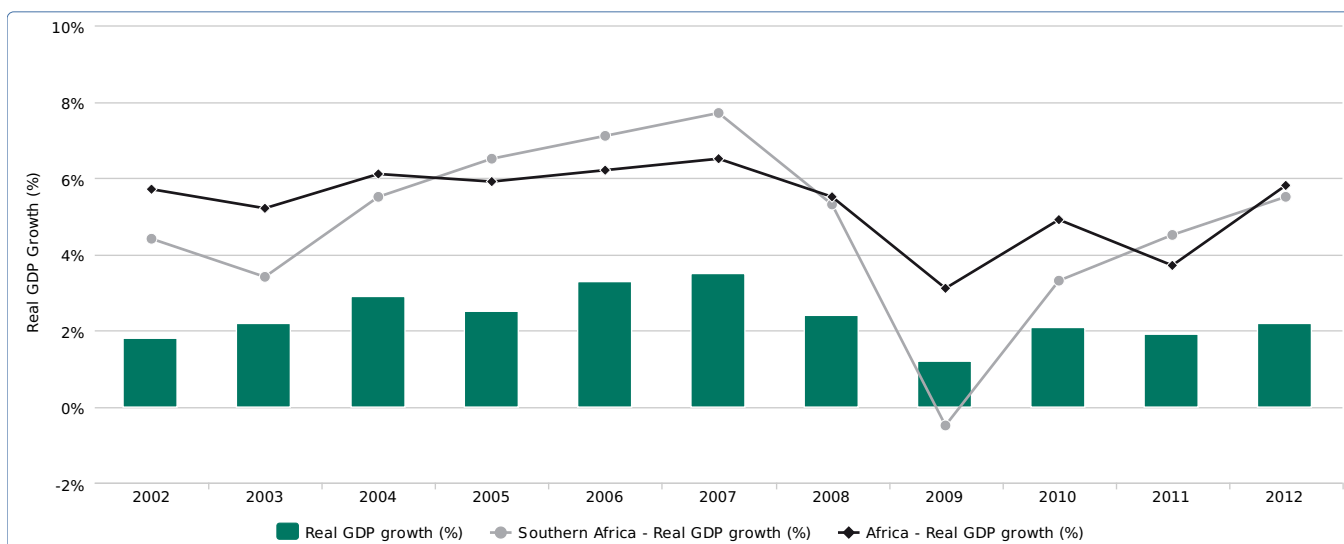
Overview

After averaging 2.9% during 2004-08, economic growth in Swaziland dropped significantly in 2009, mainly due to the impact of the global economic downturn on export-oriented sectors, in particular textiles and wood pulp. Other contributory factors were prolonged drought and low levels of foreign direct investment (FDI). In 2010, the economy moderately recovered with a rebound in global demand mainly for sugar and textiles. However, falling receipts from the Southern African Customs Union (SACU) coupled with lower internal revenues constrained the government's ability to implement counter-cyclical measures. In order to support economic activity in 2010, low interest rates were maintained in line with those of South Africa. However, the main focus of the Central Bank of Swaziland continued to be price stability. Inflation was 4.5% in 2010, down from 7.5% in 2009. This was mainly driven by lower prices for food and transport. Inflation is forecast at 7.7% in 2011, reflecting the lagged impact of increases in tariffs for water and electricity in 2010. The anticipated fuel and food crises are also expected to impact domestic price levels.

The economic outlook for 2011 appears bullish with unchanged international prices for sugar and wood pulp. However, supply for wood pulp is expected to be affected by the closure of the Sappi Company in 2010. The continued appreciation of the South African rand (ZAR) against the US dollar (USD) and other major currencies has reduced profitability in export-oriented sectors including mining, which might lead to a scaling down of operations and postponement of planned investments. In addition, the high cost of doing business and the high rate of HIV/AIDS prevalence will continue to subdue growth in 2011.

In order to deal with the fiscal challenges caused by the drop in Southern Africa Customs Union (SACU) revenues and burgeoning wage salary expenditures, the Government of Swaziland (GoS) has prepared a Fiscal Adjustment Roadmap (FAR) that runs from 2010/11 to 2014/15. This became the basis for negotiations with the International Monetary Fund (IMF) for an IMF Staff Monitored Program (SMP) since late October 2010. Once concluded, the SMP will unlock external donor support for the FAR and lay a solid foundation for sustainable economic growth. The SMP among other things advocates for quick implementation of the Value Added Tax (VAT) and reduction of the budget, particularly wages and salaries (16.4% of GDP in 2010/11) by 5% per annum beginning 2011/12 until 2013/2014. Revitalising the private sector through improving the business environment and using existing and emerging partnerships will be critical to a quick economic turnaround and for putting the economy onto a path of sustainable economic growth.

Figure 1: Real GDP growth (S)



Source: IMF and local authorities' data; estimates and projections based on authors' calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink <http://dx.doi.org/10.1787/888932404598>

Table 1: Macroeconomic indicators

	2009	2010	2011	2012
Real GDP growth	1.2	2.1	1.9	2.2
CPI inflation	7.5	4.5	7.7	10
Budget balance % GDP	-0.2	-6.7	-10.8	-13.6
Current account % GDP	-12	-16.6	-14.2	-12.5

Source: National authorities' data; estimates and predictions based on authors' calculations.

Figures for budget balance refer to fiscal year April (n)/ March (n+1).

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932406954>

Recent Economic Developments and Prospects

Table 2: GDP by sector (in percentage)

	2005	2008
Agriculture, forestry, fishing & hunting	8.6	7.7
Agriculture, livestock, fishery, forestry and logging	-	-
of which agriculture	-	-
of which food crops	-	-
Mining and quarrying	0.3	0.3
Mining, manufacturing and utilities	-	-
of which oil	-	-
Manufacturing	38	41.4
of which hydrocarbon	-	-
Electricity, gas and water	1	0.8
Electricity, water and sewerage	-	-
Construction	4.3	3
Wholesale and retail trade, hotels and restaurants	11.2	10.8
of which hotels and restaurants	-	-
Transport, storage and communication	6.5	7.3
Transport and storage, information and communication	-	-
Finance, real estate and business services	9.8	9.7
Financial intermediation, real estate services, business and other service activities	-	-
General government services	18.4	17.5
Public administration & defence; social security, education, health & social work	-	-
Public administration, education, health	-	-
Public administration, education, health & other social & personal services	-	-
Public administration, education, health & social work, community, social & personal services	-	-
Public administration, education, health & social work, community, social services	-	-
Other community, social & personal service activities	-	-
Other services	1.8	1.6
Gross domestic product at basic prices / factor cost	100	100

Source: AfDB Statistics Department; Ministry of Finance.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932407923>

Swaziland's GDP is consumption driven. In 2009, the share of consumption was estimated at above 100% of

GDP. While this is predominantly private consumption (over 88%), public consumption is equally sizeable (14%). In 2010, the volumes of public consumption increased by 8.4%, contributing 1.7% to economic growth. Wages and salaries constituted 54% of public consumption and are the main source of aggregate demand. However, the expected implementation of some of the reforms recommended by FAR in 2011 should cause public consumption growth to decline. This is coupled with an absolute decline in private consumption leading to a drop in real consumption. Gross investment contributed 2.4% to overall economic growth in 2010 and is expected to add another 2.7% in 2011. This will be underpinned by increases in capital expenditure (mainly health and education) financed by donor inflows. Despite this increase, the share of investment in GDP remains low. This reflects the risks posed by changing climatic conditions on pineapples but also difficulties in accessing credit, which constrains investment in the mining and quarrying sector.

Overall, in 2011, growth is projected to reach 1.9% driven by public investment in donor supported projects. Notable amongst these are donor inflows for budgetary support and investment in a multi-billion dollar water project supported by the Millennium Challenge Account (USD 362.2 million). Additionally, the global economic recovery is expected to increase demand for manufacturing and tourism. The agricultural sector is expected to benefit from improved access to water for irrigation from the lower Usuthu basin, thus contributing to growth.

However, water remains a constraining factor for economic growth. The country is perennially affected by drought and the bulk of water resources have been earmarked for the production of sugarcane, the country's main export. The availability of water is limited by the tripartite arrangement with Mozambique and South Africa concerning the management of water bodies (mainly rivers passing through Swaziland to neighbouring countries). None of these rivers originate in Swaziland.

Table 3: Demand composition

	Percentage of GDP (current price)		Percentage changes, volume			Contribution to real GDP growth		
	2002	2009	2010	2011	2012	2010	2011	2012
Gross capital formation	20.1	10.3	15	15	7.4	2.4	2.7	1.5
Public	6	5.4	15	15	5	1.3	1.4	0.5
Private	14.1	4.9	15	15	10	1.1	1.3	1
Consumption	85.4	101.9	2.4	-1.3	-2	2.8	-1.6	-2.3
Public	16.7	13.7	8.4	4.2	1.8	1.7	0.9	0.4
Private	68.7	88.2	1.2	-2.5	-2.9	1.2	-2.5	-2.7
External sector	-5.5	-12.1	-	-	-	-3.2	0.8	3
Exports	99.8	55.5	2.8	2.7	1.7	2.3	2.2	1.4
Imports	-105.3	-67.7	4.7	1.2	-1.4	-5.5	-1.4	1.6
Real GDP growth rate	-	-	-	-	-	2.1	1.9	2.2

Source: Data from Central Statistical Office & Ministry of Finance, Swaziland, Jan. 2010; estimates (e) and projections (p) based on authors calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932408892>

Fiscal Policy

Fiscal policy in 2010 continued to be influenced by monetary policy especially the need to maintain the peg between the domestic currency, the Lilangeni, and the South African rand. It was also guided by the need to maintain sufficient levels of currency reserves. The implementation of the 2010/11 national budget was impeded by a decline in total revenues from 34.2% of GDP in 2009 to an estimated 31.1% of GDP in 2010. This decline largely reflects the impact of the global economic recession on SACU receipts, which account for over 60% of total revenues. In 2010, the fiscal gap was exacerbated by across-the-board increases in wages and salaries for civil servants by 4.5% and increased entitlements for politicians. Wages and salaries constituted an estimated 16.4% of GDP in 2010 and are the key driver of the national budget. In view of these challenges, donor financing of the national budget was critical. Donor financing in the form of grants increased from 0.4% of GDP in 2009 to an estimated 0.6% in 2010. In terms of structure, the national budget was dominated by recurrent spending which reached more than three times the level of capital spending.

The global increase in fuel prices led to an increase in the budget provision for energy and fuel from 0.3% of the national budget in 2008/07 to 3.8% in 2009/10 before dropping to an estimated 2.1% in 2010/11. Owing to fiscal pressure, the government subsidies, which had reached 6.7% of GDP in 2009/10 dropped to 4.7% in 2010/11. For similar reasons, social protection (transfers to vulnerable groups including the aged and disabled), which had reached 7.5% of the national budget in 2009/10, dropped to an estimated 2.7% in 2010/11. The share of education and health in the national budget were respectively estimated at 18.9% and 7.8% in 2010/11.

In response to the challenges of the negative revenue shock and escalating expenditures, the authorities have developed a fiscal adjustment roadmap (FAR), which gained donor endorsement in October 2010. The FAR runs from 2010/11 to 2014/15 and proposes fiscal and structural measures to deal with the ailing economy. These include the establishment of the revenue authority and introduction of Value Added Tax (VAT) by 2011, replacing the narrower-based sales tax and measures to improve financial management. Based on the FAR, the IMF and the GoS have been engaged in negotiations since November 2010 over a staff monitored programme (SMP). The World Bank's Country Integrated Fiduciary Assessment, 2010 on page VII noted that "...although there has been improvement, most Public Financial Management (PFM) indicators continue to lag behind basic levels of good performance. There remain key risks in the PFM system that require urgent further mitigation." Improvements in PFM are among the measures included in the FAR.

Owing to a large financing gap, the government has had to mobilise extra resources through external borrowing and domestic financing. Consequently, Parliament has amended legislation to increase the domestic debt ceiling from SZL 1 billion to SZL 5 billion. During 2010/11, government bonds of varying maturities (3 years and 7 years) and in 2011, a 5-year bond were issued. The 7-year bond was mainly targeting pension funds. While the 3- and 5-year bonds were oversubscribed, the 7-year maturity bond was undersubscribed with its poor performance being attributed to a less attractive interest rate and perceived high risk exposure.

Table 4: Public finances (percentage of GDP)

	2002	2007	2008	2009	2010	2011	2012
Total revenue and grants	31.7	39.4	36.1	37.9	34.2	31.1	30
Tax revenue	28.8	37.7	33.8	35.9	32.4	29.1	28
Oil revenue	-	-	-	-	-	-	-
Grants	1.1	0.8	0.8	0.6	0.4	0.6	0.7
Other revenues	-	-	-	-	-	-	-
Total expenditure and net lending (a)	30.8	30.6	33.4	38.1	40.9	41.9	43.7
Current expenditure	23.2	23.8	24.7	28.8	32.3	32.5	33.4
Excluding interest	22.3	23	23.9	27.8	31.5	31.7	32.5
Wages and salaries	10.2	12.7	12.3	15.4	16.4	16.4	16.1
Goods and services	6.8	5.9	6.2	6.3	16.4	13.9	14.3
Interest	0.9	0.8	0.8	1	0.8	0.8	1
Capital expenditure	7.6	7.1	8.7	9.7	9.9	9.6	10.2
Primary balance	1.9	9.6	3.5	0.8	-5.9	-10	-12.7
Overall balance	1	8.8	2.7	-0.2	-6.7	-10.8	-13.6

a. Only major items are reported.

Source: Data from Central Statistical Office & Ministry of Finance, Swaziland, Jan. 2010; estimates (e) and projections (p) based on authors' calculations.

Fiscal year July (n-1)/June (n).

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932409861>

Monetary Policy

Swaziland is a member of the Common Monetary Area (CMA) in Southern Africa and has limited discretion in influencing monetary policy although it has full control over fiscal policy. The country still ensures that there is monetary stability and that the financial sector thrives through controlling interest rates. The Central Bank of Swaziland (CBS) has pursued an inflation target of 3 to 6% as a framework for price stability. During 2010, CBS pursued an expansionary policy stance, which was started in 2009 in response to the need to stimulate the economy and arrest the recessionary impact of the global economic recession. The discount rate was maintained at 5.5%, which was lower than the 6.5% repo rate pursued by the South African Reserve Bank (SARB). However, domestic credit growth was slower than anticipated, growing at an annual rate of 10.3% by end of November 2010. Despite the reform in the pension law, which required that 30% of asset holdings be returned to the country, credit extension remained low. The commercial banks have accumulated excess liquidity due to limited instruments for investing the funds within the country, availing instead of South Africa as alternative investment destination for some of these funds.

In 2011, the expansionary monetary policy stance pursued in 2010 is expected to continue. This will provide a credit stimulus to the economy while ensuring that inflation does not spiral out of control. Nonetheless inflation is expected to accelerate to 7.7% in 2011, reflecting the lagged impact of water and electricity tariff increases during the second half of 2010. The local currency is expected to appreciate moderately which will mitigate the impact of imported inflation. Additionally, the anticipated SMP, which the government is negotiating with the International Monetary Fund, is expected to deter inflation expectations.

External Position

In 2010, the external sector remained vulnerable, mainly dependent on global demand, which was depressed for some exports. The narrow export base and sluggish global recovery is likely to continue to impact on the external sector in 2011. Growth in the main exports, which comprise sugar, citrus fruits and minerals has remained sluggish. For instance, world consumption of sugar is expected to grow at a rate of 2%, somewhat below the long-term 10-year average of 2.6%. This lower global demand has been attributed to record high prices although in 2011, world availability of sugar is expected to surpass demand, which might depress export prices. Further, the euro zone, Swaziland's main export destination for sugar, has continued to open its market to Asian competitors and all these factors could slow down the country's exports in 2011. On a positive side, prospects for both cane and sugar are brighter with the completion of the Lower Usuthu Smallholder Irrigation Project (LUSIP) and the Komati Downstream Development Project. The development of 1 200 hectares in 2010 under LUSIP should greatly contribute to exports.

Poor response of the pulp industries to resumption in external demand remains a real impediment for Swaziland. There no explicit successor plans for the Sappi mill, which was closed in January 2010. The country has remained extremely open and exposed to external shocks as the share of total trade in its GDP demonstrates (averaging 170.1% for the 2005-08 period and 191.6% of GDP in 2009/10).¹ The current account deficit is expected to reduce by 2.2% of GDP in 2011.

Table 5: Current account (percentage of GDP)

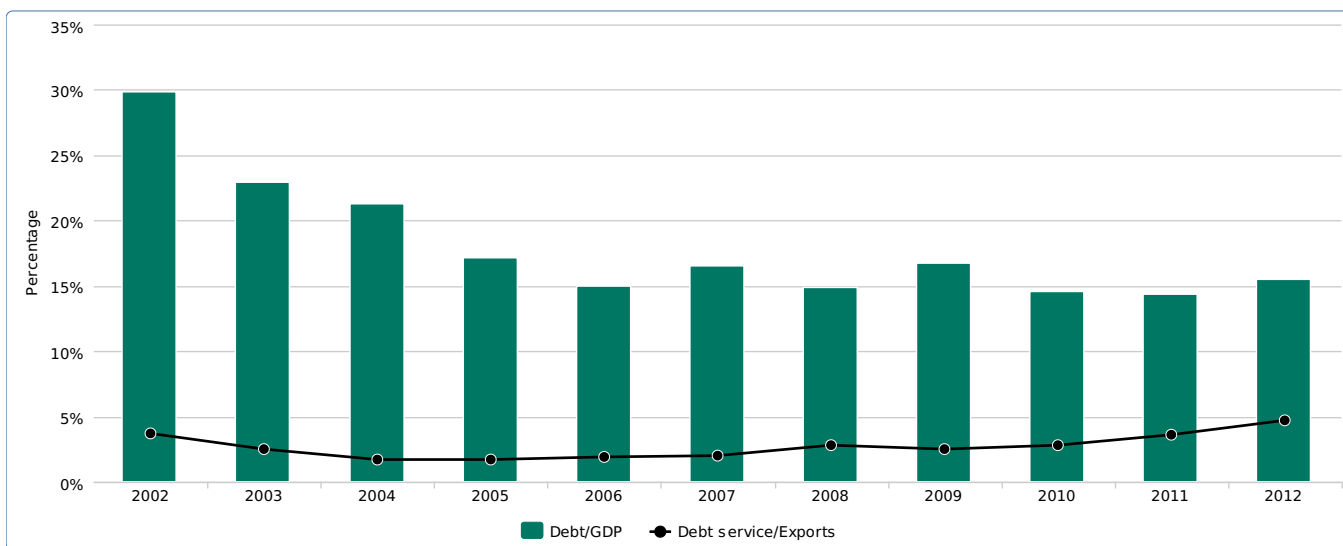
	2002	2007	2008	2009	2010	2011	2012
Trade balance	8.8	-3.3	-0.3	-4.2	-4.1	-4.8	-4.4
Exports of goods (f.o.b.)	90.9	57.1	52	49.8	43.5	40.2	39.9
Imports of goods (f.o.b.)	82.1	60.4	52.3	53.9	47.6	45	44.3
Services	-3.9	-8.6	-9.3	-10	-10.2	-8.5	-7.6
Factor income	0.3	1.3	-0.2	-3.9	-4.7	-2.2	-1.6
Current transfers	8	6	7	6.1	2.4	1.2	1.1
Current account balance	13.1	-4.6	-2.8	-12	-16.6	-14.2	-12.5

Source: Data from Central Statistical Office & Ministry of Finance, Swaziland, Jan. 2010; estimates (e) and projections (p) based on authors calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932410830>

Figure 2: Stock of total external debt (percentage of GDP) and debt service (percentage of exports of goods and services)



Source: IMF and local authorities' data; estimates and projections based on authors' calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932404598>

Structural Issues

Private Sector Development

The 2011 *Doing Business* report ranks Swaziland 118th out of 183 economies, three places lower than in 2010. The main areas of weakness relate to dealing with construction permits, enforcing contracts, protecting investors, registering property, starting a business and trading across borders. These areas are critical impediments to private sector development including attracting foreign direct investment (FDI) in the country. In order to improve the functioning of the private sector, structural constraints in the financial sector, in particular those threatening credit stability and borrower access to credit have to be removed. While the global financial crisis had very little effect on the Swazi financial sector, some vulnerability remains. These include inadequately regulated non-bank financial institutions. The proposed new regulatory system for the Savings and Credit Co-operatives (SACCOs) and for the non-bank financial institutions (NBFIs) is expected to strengthen the financial sector. Further, the strengthening of the capital market should boost the extension of credit to the private sector and government.

During the 2010/11 budget speech, the government made a number of commitments to address these critical constraints. It constituted a task force chaired by the Minister for Trade with performance indicators linked to improvements in the country's annual rating in the *Doing Business* report. There are planned reforms tailored towards improving the country's environment encapsulated in the FAR. These entail among others, trade facilitation through opening the country's border posts on a 24-hour basis.

There are initiatives spearheaded by Swaziland Investment Authority (SIPA) which include reviewing the legislature covering investment and auditing the implementation of the Investor Roadmap. Additionally, with the assistance of the United States Agency for International Development (USAID) Trade Hub, SIPA has prepared a draft investment policy which has been submitted to the government for consideration. In 2011, the African Development Bank (AfDB) is expected to provide funding for an economic diversification study aimed at identifying potential and constraints to broadening Swaziland's economic base and to increasing competitiveness. The outcome of this study is expected to greatly enhance Swaziland's drive to promote FDI and diversify its economy, which is critical for the country's growth.

The government is developing a Public Private Partnership framework which would effectively be implemented with a functional stock market. These initiatives, coupled with the Financial Services Regulatory Bill, should promote private sector investment in 2011. In the telecommunication sector, where MTN is currently the sole service provider albeit with private participation in mobile and internet services, the plan is to introduce competition. A telecommunications regulator should be introduced by 2010/11 and a fully operational energy regulator by December 2011.² These, it is envisaged, will facilitate the licensing of various power plants.

Other Recent Developments

The government has heightened its commitment to dealing with short and medium-term economic challenges using various measures. Since the 2009/10 fiscal year, it has embarked on mobilising resources by contacting multilateral donors for potential budget support. As a direct result of these efforts, it has received technical assistance and prepared the FAR. Of particular note is the establishment of the Swaziland Revenue Authority (SRA) which was officially launched in February 2011. Further, the November 2010 decision to lift the ceiling on public borrowing will allow increased domestic borrowing and will shelve international reserves from financing the domestic budget. In consequence, the Lilangeni-Rand parity will be protected. Although the country's debt stock is expected to increase as the government borrows to finance its fiscal deficits, Swaziland is expected to remain within sustainable debt levels as revealed by IMF/World Bank debt sustainability analysis (DSA). The country's gross public debt which was at 12.5% of GDP in 2009/10 is expected to rise but remain under the critical level of 40% in the medium term. However, this will only be possible if the country implements the FAR reform measures.

Public management reforms aimed at strengthening the country's controls and eliminating budget leakages are underway. In particular, these reforms include modernising the Ministry of Finance, strengthening the budgeting system, consolidating procurement reforms, expenditure reporting, internal and external auditing, and Parliamentary oversight. This is in addition to addressing the recommendations of the 2010 Country Integrated Fiduciary Assessment (CIFA) report.

Emerging Economic Partnerships

Swaziland is a member of Southern African Development Community (SADC), the Southern Africa Customs Union (SACU) and the Common Market for Eastern and Southern Africa (COMESA). It participated in the negotiations for a comprehensive Economic Partnership Agreement (EPA) with the European Commission through the SADC EPA group. Since 2009, the country has had an interim agreement with the EU after facing lower preferences under the General System of Preferences scheme.

As a member of SACU, Swaziland signed a Trade, Investment, and Development Cooperation Agreement with the United States in July 2008. Negotiations are ongoing to develop US-SACU co-operation into a free trade agreement. If they succeed, bilateral country negotiations with the US are expected in the same way as a bilateral agreement was reached with the US under the African Growth and Opportunity Act. Swaziland also participated in negotiations to establish a free trade area between member countries of the European Free Trade Association and SACU in 2008. A Preferential Trade Agreement with the Common Market of the South (MERCOSUR) was concluded in April 2009 and Swaziland became a member of the new Common Market for Eastern and Southern Africa (COMESA) Customs Union in June 2009. SACU has already been approached by India and South American countries for similar negotiations.

Political Context

Swaziland continues to experience pressure to fully democratise. Throughout 2010, many organised riots took place pointing to the need for further reform of the governance system. The country's governance indicators are mixed and the World Bank's Worldwide Governance Indicators 2010 show that of the 212 countries surveyed, the country falls below the 30 percentile rank in two out of the six dimensions of governance (voice and accountability, and government effectiveness) and is below the 50 percentile range in the four remaining dimensions. This unfavourably compares with the average governance ranking of above 40% for other SACU countries. Nonetheless, compared to 2004, progress has been made in all categories except political stability. The 2008/09 Ibrahim Index of African governance shows that Swaziland scored 50.8 out of 100, thus ranking 25th out of 53 African countries.

Social Context and Human Resource Development

The country experiences three critical social challenges: high prevalence of HIV, unemployment and poverty. The HIV prevalence rate for the 15-49 age group was estimated at 42% in 2008, representing an increase of 3% over 2007 (UNAIDS, 2010). The results are based on HIV sentinel surveillance in 2008. Government interventions to combat the spread of HIV/AIDS are articulated in the national strategy framework, the national male circumcision policy, national policy on children and national social development policy, all of which date from 2009. The above initiatives notwithstanding, the high HIV prevalence rate combined with high unemployment rates (40%) and poverty levels (63%) threaten to deter economic progress in the country. Other social challenges are food insecurity and low human development indicators. Food poverty stands at 30%, according to the 2009/10 Swaziland Household Income and Expenditure Survey (SHIES). This means that three in ten people do not have enough food to meet their energy and nutrient needs. Swaziland's Human Development Index stood at 0.498 in 2010, ranking the country at 121st out of 169 countries.³ While the country maintained the same ranking in 2009, its HDI showed some improvement (0.492, 2009).

In order to improve the Millennium Development Goal (MDG) indicators particularly that of education, the government continues to implement universal primary education which was introduced in 2008, initially focusing on grade I and grade II. This has culminated in increases in enrolment. The plan is to incrementally add another level annually. In 2010, the implementation of universal primary education was beset with various challenges, in particular, the construction of additional permanent classrooms to meet increased student numbers, recruitment of additional teachers and provision of accommodation for them. In view of the limited adjustment timeframe, the government had to construct mobile classrooms and hire contract teachers. In 2011, the government would have completed construction of permanent infrastructure for classrooms, offices and teachers' accommodation in order to accommodate the increased enrolment; which has already spiked.

Notes

1. World Trade Indicators 2009/10.
2. The energy regulator is physically in place but has yet to develop regulations and licensing procedures.
3. UNDP, Human Development Index 2010.