

Swaziland: Selected Economic and Financial Indicators, 2001–05

	2001	2002	2003	2004	2005 Est.
Domestic economy	(Annual percentage change)				
Real GDP	1.6	2.9	2.4	2.1	1.8
Consumer price inflation (period average)	7.5	11.7	7.4	3.4	4.8
External economy	(In millions of U.S. dollars, unless otherwise indicated)				
Exports, f.o.b.	1,043	1,032	1,485	1,878	1,889
Imports, f.o.b.	-1,125	-941	-1,442	-1,910	-1,994
Current account balance 1/ (In percent of GDP)	-57 -4.5	58 4.8	36 1.9	40 1.6	-44 -1.6
Gross official international reserves (In months of imports of goods and nonfactor services)	267 2.4	260 2.7	265 1.9	262 1.3	232 1.1
Debt service (in percent of exports of goods and nonfactor services)	1.3	1.4	1.1	1.1	1.2
Financial variables	(In percent of GDP, unless otherwise indicated)				
Total government revenue and grants 2/	27.6	26.3	26.3	29.3	30.7
Total government expenditure and net lending 2/	30.6	30.8	29.0	33.6	35.0
Overall government balance (incl. grants) 2/	-3.1	-4.5	-2.7	-4.3	-4.3
Change in broad money (in percent)	10.7	13.1	14.1	10.4	10.5
Interest rates (in percent) 3/	6.3	9.5	4.2	4.1	3.5

Sources: Swazi authorities; and IMF staff estimates.

1/ Including transfers.

2/ Fiscal years (April 1-March 31).

3/ For 12-month time deposits.

**Statement by Peter J. Ngumbullu, Executive Director for The Kingdom of Swaziland
and Bhadala T. Mamba, Advisor to Executive Director
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Introduction

1. I would like to extend appreciation of the Swazi authorities to the Fund staff and management for the candid and constructive discussion and advice during the Article IV consultation Mission. The Mission held widespread discussions with various stakeholders in the economy and presented its findings to the authorities who are thankful for the opportunity to exchange views during these meetings and are mindful and equally concerned about the many challenges facing the country. They have always valued the Board and Fund advice on these issues and are in broad agreement with staff's analysis and policy recommendations contained in the staff paper. The authorities also appreciate the excellent and timely technical assistance provided by the Fund on a number of areas. They value the productive and enlightening presentation made by staff to senior government officials at a seminar held during the mission, which focused on Growth and Fiscal Consolidation over the Medium-term and the Common Monetary Area and Improving External Competitiveness.

2. Swaziland has had to deal with a convergence of a multi-pronged set of challenges driven by persistent and unabating humanitarian crisis, arising from food shortages resulting from continued erratic weather patterns, worsening HIV/AIDS pandemic, increasing incidence of poverty and negative changes in international trade arrangements affecting the country's major exports, particularly sugar and textiles. While marginal improvements in food production were realized during the 2005 crop season, the World Food Program (WFP) still estimates that 227,000 people will need food aid by the end of the 2006 crop season. The country's poverty incidence has risen from 66 to 69 percent according to a recent Household and Income and Expenditure Survey. Furthermore, over and above shocks to the important textile and sugar sectors, the country's fiscal performance has also been precarious, resulting in increased expenditures, creating an unsustainable fiscal trend and decline in the country's foreign reserve holdings to historically low levels. The overall balance of payments position since 2000 has become negative, as a result of increased net capital outflows. The authorities are aware of the persistent decline in economic performance and are committed to deal with the deteriorating socio-economic situation and take measures to address the existing structural fiscal imbalances and reform the public expenditure management system, improve the investment climate, enhance restructuring and privatization of public sector enterprises and restore macroeconomic stability through serious implementation of the reform agenda.

Recent Economic Developments

3. The Swazi economy is largely driven by the agriculture and manufacturing sectors. Although contribution of agriculture to GDP has declined over the years, it remains a

crucial supporter of the manufacturing sector, which is agro-based. The agricultural sector, however, remains vulnerable to exogenous factors like the prevalence of natural disasters such as drought and is highly dependent on climatic and international market developments, including exchange rate movements, the world business cycle, in particular, increases in oil prices, as well as changes in international prices of major exports. There has been recently rapid growth of the services sector alongside the expanding manufacturing sector, which is attributable to the continued growth in government activities in trade, banking, finance and transport. The delayed rains during the 2005/06 season and drought, having spanned a number of years, has dealt a harsh blow to the efforts of rural farmers. This delay is likely to prolong the already bad food security situation in the country.

4. The country is also facing challenges in the international trading environment, which are adversely affecting the economy. The textile sector experienced major shocks with an estimated 15,000 jobs lost in 2005 and a number of firms that were exporting to the USA under the American Growth and Opportunities Act (AGOA) closed their operations and left the country. The sugar industry also faced similar shocks following the renegotiation of the country's preferential access to the EU, which resulted in laying-off several hundreds of workers in this sector. These developments further worsened the dire unemployment situation in a country with a youthful demographic structure, requiring fundamental and comprehensive structural changes to be crafted and implemented through collaborative efforts and cooperation between the private sector, the country's development partners and the government. The sluggish economic growth recorded in recent years has not been able to match the population growth rate of 2.9 percent, indicating that the real per capita income has been on a declining trend.

Fiscal Developments

5. The authorities are in the process of finalizing the 2006/07 budget, which will focus broadly on the following priority areas:
 - revitalization of the economy and pursuing sound macro-economic management;
 - poverty reduction and decisive action on the HIV/AIDS pandemic; and
 - reverse the humanitarian crisis by dealing with the food security problem.
6. In addition, the Government in presenting this year's Medium Term Budget Policy Statement (MTBPS), adopted an inclusive approach to generate comments and inputs into the budgetary process from the general public, civil society and politicians. The authorities realize that there are limited avenues to deal with the deteriorating economic situation other than steadfastly adopting a tight fiscal stance, persistently implementing a broad structural reform agenda aimed at improving business environment and competitiveness. The government has clearly outlined these intentions in the recent Medium Term Budget Policy Statement, which aims at achieving a 2 percent budget deficit in 2006/07. This framework also envisages

achievement of a balanced budget in 2008/09, through implementation of the following reforms:

- Civil Service reforms aimed at offering an early voluntary retirement for those civil servants who are 55 years and above in 2006. Furthermore, freezing civil service vacancies, and releasing about E250 million for other priority expenditures, stop creating new posts in the civil service and offer no cost of living adjustments for the remaining civil servants;
 - Cutting capital expenditure by E200 million; and
 - Lowering the budget ceiling through cuts in recurrent expenditures and expenditure on goods and services of at least 5 percent.
7. While implementing this strategy, the authorities have committed themselves to continue to address, through the budget, some of the social challenges facing the country. They intend to increase expenditure on priority social sectors including health and education in dealing with the increasing poverty, worsening HIV/AIDS pandemic and providing services for the growing number of orphan and vulnerable children (OVC). The authorities plan on improving health care service delivery as well as capacity building of this sector by designing appropriate and properly developed projects and programmes. They expect that this will result in an increase in the share of budget to the health sector by about 2 percent.
8. The budgetary tight situation is going to be temporarily propped-up by a slight increase on revenue receipts from internal revenues and an additional E1.1 billion expected from SACU receipts for 2006/07. Though this SACU windfall will augment the authorities' revenue collection efforts, such flows are not expected in the near future and hence their commitment to an austere fiscal strategy. To further consolidate these efforts, they also plan on establishing a Revenue Authority in the coming financial year and also introduce a broad-based VAT in the medium term.

Economic Resuscitation Plans and Medium-term outlook

9. The authorities recognize that, substantial and sustainable poverty reduction can only be achieved in the context of a growing economy requiring improved environment for conducive private sector investment that will create employment and further achieve diversification. Therefore, expectations on future growth will be anchored on focusing on key areas or pillars of the economy through pursuing fiscal and structural reforms, and supporting the key agricultural and manufacturing sectors, embracing good governance principles premised on transparent and accountable systems, and promoting human capital development.
10. The government is committed to fostering and facilitating a conducive environment for a private sector-driven economic recovery to take place. It plans to ensure these efforts succeed, coupled with efficiency in the use of public resources, and better service delivery. Paramount to this effort is the deregulation and commercialization of some industries especially communication, insurance, water and electricity sectors,

which are expected to provide the much needed impetus for a comprehensive economic recovery.

11. The government held a Job Creation Summit in July 2005, where significant amount of money, totaling about E1.6 billion, was pledged for job creating activities and the authorities are making the necessary preparations to ensure that these pledges and investments support capacity building of the SMEs and the informal sector, particularly in the area of business management as well as providing credit as start-up capital. It is expected that this initiative will contribute significantly to employment creation. The government's medium-term strategy is to continue with the ongoing initiatives towards employment generation such as Lower Usuthu, Maguga project, the Millennium Projects, rollout of the SMEs policy and improve efforts at attracting FDI, amongst others.
12. The authorities remain committed to regional integration efforts and have been participating in a number of SACU-led international trade negotiations, which aim at creating new markets for the country's trade arrangements with the USA, EU and MERCUSOR, among others. They are also committed to developing new export-oriented industries and reduce relying predominantly on the traditional sugar and textile manufacturing sectors.

Monetary, Exchange Rate, and Financial Sector Developments

13. Swaziland is currently involved in a broad-based financial sector reform exercise involving legislative reforms and modernization of the financial sector. Several pieces of legislation aimed at improving financial sector development were passed in parliament in the last year, including amendments to the Financial Institutions Act and the Insurance Act. Additional legislation is expected to be passed in 2006, including the Anti-Money Laundering Act (AML/CFT), Securities Bill, Financial Services Regulatory Authority, and the National Clearing and Settlement Systems Bills.
14. The authorities believe that the decision to maintain the peg of the local currency to the South African rand has provided stability and helped usher financial discipline. While the recent appreciation of the rand against major international currencies undermined the country's competitiveness, they believe that the CMA arrangement has helped in keeping inflation low.

Structural Reforms

15. The authorities' formulation exercise of the constitution, which will usher the country into a new governance dispensation that would lead to political and legal reforms conducive to attracting investments into the country, is in its final stages of completion. Improvement of the business climate and reduction of the role of government in the mainstream of the economy is seen as key to the success of the proposed reforms.

16. The National HIV/AIDS coordinating unit (NERCHA) continues to deliver commendable service in augmenting government activities in this critical area. The unit has established several structures and working committees to deal with the HIV/AIDS pandemic. Unfortunately, the HIV/AIDS prevalence continues to rise and worsening the poverty situation. The government with the support of other donors and the Global Aids Fund has made commendable progress in fighting the scourge and in dealing with the sick by rolling out an anti-retroviral program, as well as dealing with the rising orphan population and embarking on civic education campaign and also strengthened home-based care. The successful roll-out of the anti-retroviral drugs achieved the set target of 13,000 people receiving drugs by the end of 2005. The fight against the HIV/AIDS pandemic has been hampered by rising turnover in the nursing profession with most of them leaving the country to go and work abroad. The pandemic has reached crisis proportions and needs further concerted effort by the authorities and the international community.

17. In response to the declining social indicators the authorities are planning on introducing a national program for Universal Primary Education to ensure basic education for all. This Program is being phased and has started with provision of free text books for primary schools and will be followed up by subsidized education for the first four grades of primary schooling in the coming year so that every child can attend school. This process is undertaken in collaboration with the Ministry of Health and Social Welfare, with particular focus on dealing with the rising number of OVCs.

Conclusion

18. The Swazi authorities remain committed to fundamental structural reforms in both the public and private sectors; and are prepared to review all existing systems and structures to enable implementation of a comprehensive recovery package aimed at reversing the economic malaise. They aim at fully taking advantage of all sectors in which the country has a natural comparative advantage, such as sugar, pulp, and minerals, and improve labour productivity and competitiveness.

19. Income distribution in Swaziland is very skewed and as more people fall into the poverty trap, there is a further worsening of the social indicators. Consequently, the authorities believe that it is important to review the current classification of the country as a middle income country so that it can benefit from concessional resources given the deterioration in the country's socio-economic situation. The international community and the IFIs need to assist and cooperate with the authorities to address the existing unique circumstances and challenges being faced, especially on HIV/AIDS and achieving the MDGs by 2015.

20. The HIV/AIDS pandemic, given its multi-pronged consequences, is the single-most significant threat to achieving sustainable macroeconomic stability due to its devastating effect on the most productive human resource base of the country, with a