Swaziland: Selected Economic and Financial Indicators, 2002-2006

	2002	2003	2004	2005	2006 Est.
Domestic economy					
Real GDP	2.9	2.9	2.1	2.3	2.1
Consumer price inflation (period average)	11.7	7.4	3.4	4.8	5.1
	(In millions of U.S. dollars, unless otherwise indicated)				
External economy					
Exports, f.o.b.	1,032	1,387	1,741	1,825	1,877
Imports, f.o.b.	-941	-1,283	-1,601	-1,752	-1,810
Current account balance [1]	58	124	74	42	19
(In percent of GDP)	4.8	6.5	3.1	1.6	0.7
Gross official international reserves	260	265	262	231	378
(In months of imports of goods and nonfactor services)	2.7	2.1	1.6	1.3	2.0
Debt service (in percent of exports of goods and nonfactor services)	1.4	1.1	1.3	1.1	1.1
Financial variables	(In percent of GDP, unless otherwise indicated)				
Total government revenue and grants [2]	26.3	26.7	30.8	32.5	35.6
Total government expenditure and net lending [2]	30.8	29.4	35.4	34.0	35.1
Overall government balance (incl. grants) [2]	-4.5	-2.8	-4.6	-1.5	0.5
Change in broad money (in percent)	13.1	14.1	10.4	5.9	15.3
Interest rates (in percent) [3]	9.5	4.2	4.1	3.5	7.4

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 Gakunu, Executive Director for the Kingdom of Swaziland and Bhadala T. Mamba, Advisor to Executive Director
January 31, 2007

Introduction

Swaziland's economic performance has been lackluster in recent years as a result of a confluence of exogenous shocks and other challenges that include: high international oil prices; recurring droughts; the decline in international price of sugar, a key export; and the end of the multi-fiber arrangement and loss of preferential trade access for textiles, another key export. There is the ongoing appreciation of the Rand/Lilangeni exchange rate for which Swaziland has little control and the consequential diversion of foreign direct investments to more competitive destinations within the region. These developments and the stagnating economic growth, which has averaged only 2 percent since 2000, aggravated youth unemployment and poverty. The incidence of HIV/AIDS has been rising and is now rated the highest in the world. With these daunting challenges, the classification of Swaziland as a middle income country adds another layer of complication, depriving the country of concessional resources to fight HIV/AIDS and reduce poverty thereby making the already challenging fiscal situation even more difficult.

Facing these problems, the authorities have embarked on a reform process aimed at resuscitating economic growth to the robust levels being experienced by other countries in the region. They are fully aware that there is no room for complacency and the process of reform implementation requires resoluteness on their part. The 2006/07 budget is cast with a view to addressing the main priorities, which include poverty alleviation, fight against HIV/AIDS, employment creation, tackling the food security problem, ensuring sound public expenditure management and revenue diversification. In this regard, the authorities appreciate the continued Fund engagement and thank the staff mission for the constructive dialogue during the last streamlined Article IV discussion. They thank the IMF Executive Board and management for the advice proffered over the years and their continued support in the many challenges they face.

Recent Economic Developments

The slowdown in economic activity has been aggravated by the coming to an end of preferential access to markets for Swazi exports, especially the all important sugar exports. This situation has also been worsened by the expiry of the multi-fiber agreement in the textile sector and the subsequent decline in the international price of sugar, which has had far reaching implications beyond the sugar industry. The sugar industry directly and indirectly supports a bulk of the social services in communities surrounding the sugar estates, covering a substantial part of the eastern part of the country. Furthermore, during the review period, the country's exchange rate strengthened, further undermining manufacturing sector exports,

which also include the textile, forestry and the sugar industries, resulting in the loss of over 10,000 jobs. This has called upon the government to devise an effective strategy to counteract the effect of the reduction of prices, including developing mitigating measures for the job losses and seeking diversification of exports and markets.

Swaziland's investment climate has been largely undermined by perceptions of governance in the last few years and the 2007 World Bank, Doing Business report, shows that though the country may have slipped in rankings, there were more positive reforms than being perceived. These include the restoration of the rule of law and adoption of a constitution, the commitment to fight corruption by passing a new anti-corruption bill, and strengthening the Anti-Corruption Commission. To demonstrate its commitment towards getting rid of the scourge, the Government is taking action to deal with individuals and institutions that have been associated with any corrupt practices. To improve the investment climate, the Swaziland Investment Promotion Agency (SIPA) has been strengthened as a one shop center and an eminent group of advisors called the Business Advisory Panel (BEAP) has been formed, comprising of locals and foreigners to advise government on how to improve the country's attractiveness as an investment destination.

Fiscal Developments

Swaziland has limited scope for influencing the economy through monetary policy given its membership to the CMA. The authorities, therefore, recognize the importance of pursuing a prudent fiscal policy and structural reforms as the only avenues at their disposal to restore macroeconomic stability and engender sustained economic growth. The 2006/07 budget has been anchored on fiscal sustainability, which is key to macroeconomic stability requiring strict measures in the allocation of limited financial resources. During the 2006/07 fiscal year, there has been increased outlays towards social sectors, but this has not been enough to address the scale of the challenges facing the economy. The government of Swaziland has no access to concessional resources to deal with these challenges despite the rising incidence of HIV/AIDS pandemic, worsening social indicators and deepening poverty. Nonetheless, the budget has re-established expenditure controls and fiscal sustainability through the introduction of a computerized commitment system, improvement of the procurement system and support to the reform of public enterprises. These reforms are not expected to yield immediate results and their adoption and implementation will only show results in the years to come.

Meanwhile, the country has very limited fiscal space to deal with institutional reforms aimed at reducing expenditure in certain areas while at the same time increasing expenditures in the social sectors like health and education aimed at increasing investments in human capital. In this respect the introduction of universal primary education will be gradually phased-in. The authorities, faced with the limited resource envelope, have also had to prioritize between the on-going development program and related recurrent requirements. The budget was crafted

taking into consideration the recommendations of the country's cooperating partners. It targeted a fiscal deficit of around 2% of GDP and ensures a balanced budget in the medium term. This situation was made possible by the improved but still unpredictable revenue inflows from the SACU pool. The authorities are looking at various avenues of broadening the tax base and reducing the over-reliance on SACU receipts. They are seeking technical assistance from the Fund and the international community to introduce the VAT and establish the Revenue authority by 2007/08 to improve revenue collection. They have committed themselves to replenish the country's international reserves using the higher than expected SACU receipts.

Civil service reform

The authorities are committed to implementing public expenditure management systems aimed at bringing down the wage bill, starting with the voluntary retirement program, elimination of arrears and reduction of overall recurrent expenditure. They acknowledge the constraints relating to implementation of the proposed civil service reforms, and have continued to engage all stakeholders and cooperating partners on the best way forward with minimal disruptions in an already difficult economic and social environment. The authorities face a dilemma of right-sizing the civil service in a shrinking economic environment with unemployment already at high levels. The authorities had initially offered a voluntary separation package for civil servants who were over 55 years of age but the response has been very disappointing. This has forced the Government to go back to the drawing board and devise a new strategy. Of particular concern however, is developing the appropriate safety nets to mitigate against the effects of the envisaged civil service rightsizing. They remain committed to civil service reform while seeking social safety nets to cushion and accommodate the very vulnerable groups.

Fighting the HIV/AIDS pandemic

The results of the recent 2006 10th HIV Sentinel Surveillance survey that establishes trends of the epidemic among pregnant women, estimate incidence of HIV prevalence in the adult population to have significantly decreased to 39.2% from 42.6 percent as a result of a wide range of intervention strategies by the National Emergency Response Council on HIV/AIDS (NERCHA). Though this may indicate some measure of success, the authorities believe the figure remains at an alarmingly high level and more still needs to be done and seek support of the international community to fight the pandemic. The government, working with NERCHA, is also developing complementary policies and measures in the fight against the HIV/AIDS pandemic, such as the National Multi-Sectoral HIV and AIDS Policy, National Policy on Children, including OVCs, Gender Policy and Land Policy.

The authorities recognize the increasing challenges in the medium to long term, towards meeting the health needs of its youthful population. In an effort to revitalize the health sector,

the authorities have embarked on a comprehensive review of the health sector budget to incorporate these new challenges and begin a process of zero-based budgeting. This effort is supported by the World Health Organization (WHO), and includes developing a strategic plan for the whole health sector, undertaking a service mapping exercise for the sector, strengthening the sector's legislative framework, addressing the brain drain issue, strengthening health management systems and designing a human resource development policy. The authorities seek international support to implement this ambitious health sector reform program to train, build and equip health institutions and practitioners to effectively deal with the emergence of new diseases and challenges in an already disease-burdened country.

Monetary and Exchange Rate Developments

The overall financial sector continued to grow as more institutions broadened their services and products. The authorities in their efforts to revamp the sector, embarked on a process to reform the Financial Services Regulatory Authority through a Bill which seeks to modernize financial sector, creating new structures and institutions and instilling competition and efficiency in the sector. The Central Bank has initiated a process to implement a Real Time Gross Settlement (RTGS) System for the monitoring of payments and settlements. The authorities remain committed to strengthening and maintaining a healthy financial sector as indicated in previous Article IV reports and the staff's concluding statement. Their efforts to modernize the financial system are supported by the Fund in a number of areas including improving reserve management, dealing with anti-money laundering and supervision of all financial institutions amongst other areas. Several pieces of legislation have been tabled to parliament in the review period to support these efforts. The authorities acknowledge the challenges facing the sector and have been reviewing the legal and structural reforms aimed at deepening the financial sector and enhancing its stability so as to further conform to regional and international norms and standards. In this vein they have requested further assistance from the International Financial Institutions to continue with these reforms and dealing with other challenges like the supervision of the non-bank financial institutions.

The authorities continue to foster cooperation and monetary integration at the regional level. They remain fully committed to the ideals of the Common Monetary Area as a means to anchor price stability and promote economic growth in the country. They recognize the need to strengthen their obligation to the exchange rate peg through steady accumulation of international reserves. The Central Bank, supported by the government, has continued to focus on promoting financial sector soundness and exchange rate stability by increasing the country's international reserve position. The government has continued to recapitalize the Central Bank by committing to inject E400 million during the 2006/07 fiscal year. This will improve the Bank's balance sheet and boost the country's international reserves, which have since risen to cover 2.4 months of imports by November 2006 compared to only a month of import coverage at the beginning of 2006.

Structural Issues

The authorities acknowledge the need to dramatically review the investment climate and efforts are underway to implement the recommendations of studies already undertaken. They will commission more studies about Swaziland's unique challenges with a view to improve the country's competitiveness and reclaim some markets lost to the more competitive producers. The expiry of the multi-fiber agreement and its replacement with the agreement on textile and clothing, has undermined smaller and less competitive economies like Swaziland, thereby reducing their market share. This development has resulted in a massive restructuring exercise by most firms leading to lay offs and other firms closing shop. They believe the continued harmonious industrial climate, the country's good infrastructure, preferential access and proximity to markets, and a relatively well-educated labor force, augurs well for future investment inflows, though more work needs to be done.

The process to transform the economy will be anchored on implementation of a number of structural reforms, sound macroeconomic management, improve competitiveness and develop and implement a new set of investment incentives that are budget neutral. This effort will be bolstered by the attraction of foreign investors while developing an indigenous entrepreneurial class of Small and Medium Sized Entrepreneurs (SMEs). The government is committed to supporting this effort through clearing domestic arrears and expediting payment to private sector suppliers of goods and services.

The authorities recognize the challenges facing the economy arising from the constraints to economies of scale and geographic location, and have embraced regional economic integration efforts as the main driving force for growth and development. The country, together with its SACU counterparts, continue to pursue an aggressive bilateral trade negotiations agenda to achieve this goal. The authorities are watching the WTO multilateral trade negotiations with anxiety and are cognizant of the impact of the outcome of the Doha Development Agenda on a small export dependant developing country like Swaziland.

The authorities are committed to the fight against poverty and are in the process of devising a comprehensive strategy to deal with this issue. This is particularly so, given the threat posed by the HIV/AIDS pandemic, which is now a major obstacle to economic and social progress. The authorities have since developed a Poverty Reduction Strategy and Action Plan (PRSAP), which will be the country's development framework for poverty reduction. The PRSAP guides government and all stakeholders on the programs and projects to be implemented in order to effectively reduce poverty by half by 2015 and eradicate it by 2022, in line with the Millennium Development Goals (MDGs). As mentioned above, the 2006/07 budget has increased outlays towards achieving this goal through significant increases in the education and health sectors.