October 2008
IMF Country Report No. 356

The Kingdom of Swaziland: 2008 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the Article IV consultation with the Kingdom of Swaziland, the following documents have been released and are included in this package:

- The staff report for the 2008 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on August 5, 2008 with the officials of the Kingdom of Swaziland on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on October 1, 2008. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its October 17, 2008 discussion of the staff report that concluded the Article IV consultation.

- A statement by the Executive Director for the Kingdom of Swaziland.

The document listed below has been or will be separately released.

Selected Issues and Statistical Appendix Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

KINGDOM OF SWAZILAND

Staff Report for the 2008 Article IV Consultation

Prepared by the Staff Representatives for the

2008 Consultation with the Kingdom of Swaziland

Approved by Anne-Marie Gulde-Wolf and Anthony R. Boote

October 1, 2008

Date: July 23–August 5, 2008.

Team: Ms. Soonthornsima (head), Messrs. Torrez, Fontaine, Davoodi (all AFR), and Bartholomew (MCM), Ms. Gesami (OED), and Mr. Van Houtte (World Bank) also participated.

Staff met with senior government officials including Prime Minister Dlamini, the Cabinet, Finance Minister Sithole and Central Bank Governor Dlamini. Staff also conducted an outreach seminar for public officials, representatives of the private sector, labor unions, media and donors.

Swaziland has accepted the obligations of Article VIII, Sections 2–4; it maintains two exchange restrictions arising from limits on the provision of foreign exchange for advance payments for imports: (i) an overall limit of E 250,000, and (ii) a 33.33 percent limit for the import of certain capital goods. The Swazi lilangeni is pegged at par with the South African rand, which is also legal tender.

Statistical quality is adequate for surveillance, but there is scope for improvement especially in national accounts and balance of payments data.

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ABBREVIATIONS AND ACRONYMS

CBS	Central Bank of Swaziland
CMA	Common Monetary Area
CPI	Consumer price index
DSA	Debt sustainability analysis
EFTA	European Free Trade Association
ES	External sustainability approach
EU	European Union Commission
FDI	Foreign direct investment
FSRA	Financial Services and Regulatory Authority
GDP	Gross domestic product
GNI	Gross national income
MCM	IMF Monetary and Capital Markets Department
MDGs	Millennium Development Goals
MOAC	Ministry of Agriculture and Co-operatives
MTEF	Medium-Term Expenditure Framework
NBFI	Nonbank financial institutions
NERCHA	National Emergency Response Council on HIV/AIDS
NFA	Net foreign assets
NIIP	Net International Investment Position
PPP	Purchasing power parity
REER	Real effective exchange rate
PRSAP	Poverty Reduction Strategy and Action Program
RA	Revenue Authority
SACU	Southern African Customs Union
SADC	Southern African Development Community
SARB	South African Reserve Bank.
SCCO	Saving and Credit Cooperatives
TICA	Trade and Investment Cooperation Agreement

EXECUTIVE SUMMARY

- **High rates of economic growth remain elusive and downside risks have increased.** Growth recovered moderately in 2007, but inflation escalated into double digits, initially owing to high food and fuel prices. High Southern African Customs Union (SACU) revenue contributed to the second consecutive budget surplus, an improved current account, and a build-up of international reserves. The authorities anticipate higher growth rates than the staff but agreed that the growth was still too low. The global economic slowdown and the high food and fuel prices increase downside risks.

- **Growth could be bolstered by fiscal and structural reforms** to improve the investment climate, address financial sector vulnerabilities, and control the HIV/AIDS epidemic. The authorities generally agreed with the reforms recommended but noted that capacity constraints limit the pace of their implementation.

- **Fiscal adjustment is needed to mitigate the risks of high dependence on SACU revenue, given their likely eventual decline, and to safeguard macroeconomic stability.** High SACU revenues currently provide an opportunity for orderly fiscal and structural reforms that could increase fiscal savings and GDP growth. Staff recommended efforts toward an improvement in the quality of expenditure, domestic revenue measures, streamlining expenditures, and public finance management. The authorities indicated that enormous social needs and political constraints, including the program of the government elected in September, could limit fiscal consolidation.

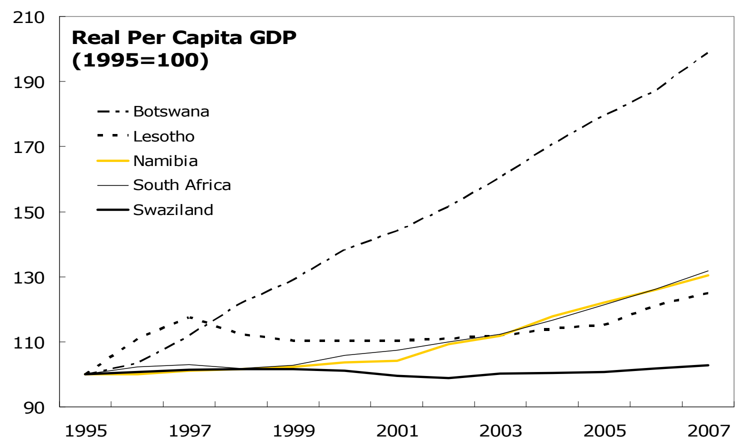
- **The level of the exchange rate seems broadly adequate, but competitiveness remains a concern.** Efforts should focus on structural reforms, such as enhancing the investment climate and governance. As a member of the Common Monetary Area (CMA), the authorities have limited independence in monetary policy and should keep the policy interest rate as close as possible to South Africa's to help control inflation while mitigating capital outflows.

- **To alleviate the impact of high food and fuel prices while being fiscally responsible, the authorities should focus assistance on the most vulnerable within the population and use the existing distribution channels to deliver such assistance.** Staff recommended liberalization of food imports, prompt pass-through of exogenous price increases, and better coordination among stakeholders.

- **To safeguard financial stability, prompt actions are required to tighten supervision of saving and credit cooperatives and address pyramid schemes.** Beginning with the privatization of the government-owned bank is a welcome step. The requirement that insurance and retirement funds invest domestically should be reconsidered, with a view to gradual phase-out, because it could reduce returns and undermine deepening of the financial sector. Several financial bills should be enacted as soon as possible.

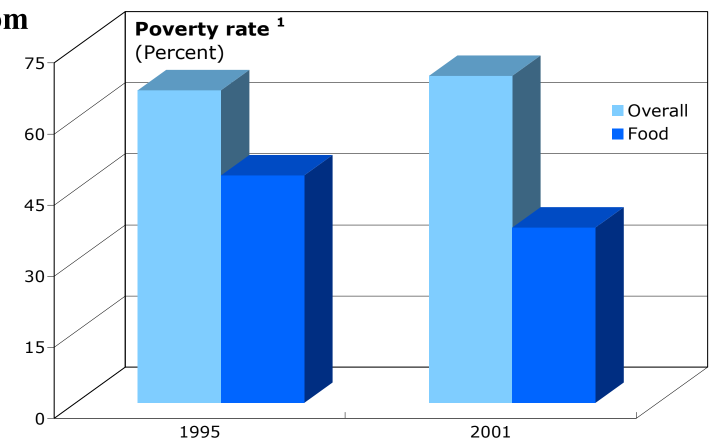
I. Background

1. **High and sustained economic growth remains elusive.** Real GDP growth is lower than the 5 percent government target for effectively reducing poverty. Growth prospects are clouded by low investments, slow pace of economic reforms, and deterioration of preferential treatment for Swaziland's main exports, sugar and textiles. The recent global shocks—surges of commodity prices and inflation, slowdown of economic growth, and continuing financial rebalancing—further increases risks to the Swazi economy. Years of persistently low growth have pushed up poverty and unemployment, a situation worsened by the prevalence of HIV/AIDS, labor force absenteeism, and low productivity. Since 1997 the epidemic has also limited annual population growth to about 0.4 percent.[1]



Source: World Economic Outlook.

2. **High and rising revenues from the Southern African Customs Union (SACU) have allowed Swaziland to expand public expenditure and accumulate international reserves.** The authorities have increased fiscal savings during the last two years; international reserves now cover more than three months of imports of goods and services after years of less than adequate coverage. Yet despite escalated public expenditure, the country's social challenges remain daunting.



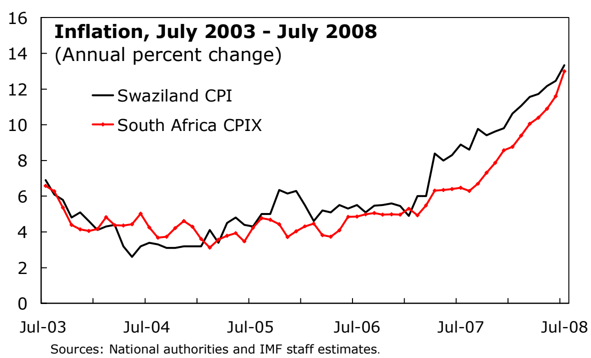
[1] The food poverty represents the fraction of people who cannot afford buying food in order to maintain a minimum daily intake of 2,100 calories.

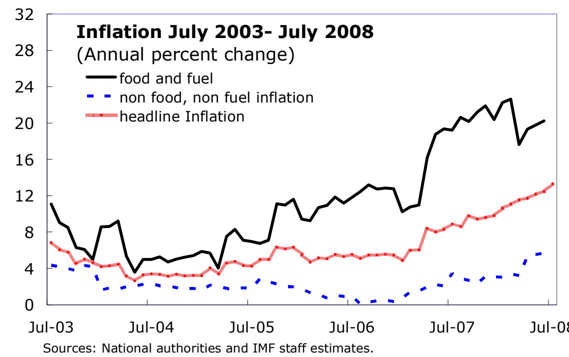
3. **The first parliamentary election under the new constitution took place on September 19 using** the traditional *tinkhundla* system—a grass roots system of local government and chiefdoms (Swaziland is a constitutional monarchy). A new Cabinet is expected to be sworn in during October 2008.

[1] The 2007 census showed the population had increased to 1,018 million from 980 million in 1997.

II. Recent Economic Developments and Outlook

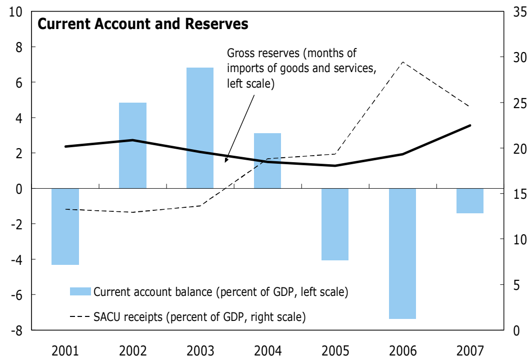
4. **As Swaziland recovered from the 2006 drought, real GDP growth in 2007 rose to 3.5 percent, and inflation escalated.** Growth was also driven by increases in output in services and manufacturing. Inflation reached 9.8 percent at the end of 2007 as food and fuel prices rose. By the end of July 2008, inflation was at 13.4 percent. The authorities have responded to the recent surges of food, fuel and transportation prices mainly through a delayed pass-through of price increases.[2] In 2008 average inflation is expected to be about 13 percent based on second-round effects from double-digit wage settlements, and despite recent declines in global fuel prices. Interest rates generally have risen in line with those of South Africa but the authorities decided in June 2008 not to match a 50 basis point increase by the South African Reserve Bank (SARB).



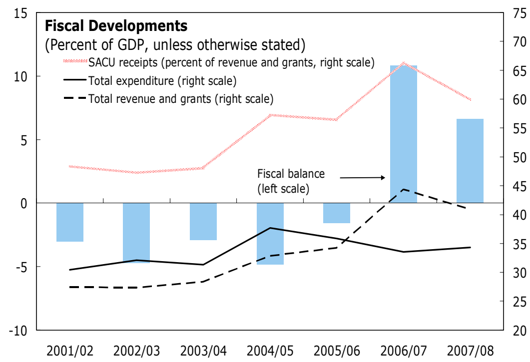


5. **In 2007/08 high SACU transfers contributed to the second consecutive budget surplus (6.4 percent of GDP), an improved current account, and an accumulation of international reserves.** The recent depreciation of the nominal exchange rate along with the South African rand, to which it is pegged, is possibly having a positive impact on the export sector. External debt in 2007 declined to 16.7 percent of GDP, and international reserves reached the equivalent of 3.5 months of imports.

[2] Between June 2007 and June 2008 the price of maize increased by 38 percent, bread by 58 percent, milk by 11 percent, and rice by 100 percent. Bus fares increased by 60 percent in August. Despite relying mainly on imports from South Africa, electricity prices have been increased only with delays and at a more gradual pace than in South Africa. Swazi electricity prices increased in July, after the South African price increase announced in April.



Sources: National authorities and IMF staff estimates.



Sources: National authorities and IMF staff estimates.

6. **Since the last consultation the authorities have consolidated international reserves at the central bank (CBS) and enhanced supervision of the financial sector, but have done little to tighten expenditures and reform the civil service.** The 2008/09 budget forecasts increased expenditure by 7 percent of GDP to 40.3 percent and the wage bill to rise to 16.7 percent of GDP. Under the 2007 Revenue Authority (RA) Act, the authorities have established the RA and are recruiting staff. With insurance sector liberalization, four new companies started up in 2008. The authorities have begun the process of privatizing the government owned Swazi Bank and of supervising saving and credit cooperatives (SCCOs.)

7. **With current policies, medium-term prospects are not encouraging and subject to substantial risks that could undermine macroeconomic stability.** Growth could be further hampered by uncertainties about the viability and timing of investment projects, low competitiveness scores, an investment climate that keeps the cost of doing business high, and the prevalence of HIV/AIDS. Staff therefore expects a growth slowdown to less than 3 percent annually, although the authorities, anticipating investment projects, expect growth rates of at least 3 percent. The current account deficit is expected to widen as tariff protection in the SACU market is eliminated, and preferential prices for sugar in the EU market are reduced.[3] Furthermore, recent global financial market developments may have an adverse impact on the country's financial sector should South African banks, which dominate the sector, suffer significant losses. The outlook is further clouded by a fiscal stance that is overly dependent on SACU revenue, high inflation, and a vulnerable financial sector.

[3] Sugar prices to the EU will fall by 17.3 percent in 2008 and by a further 19 percent in 2009.

III. Policy Discussions

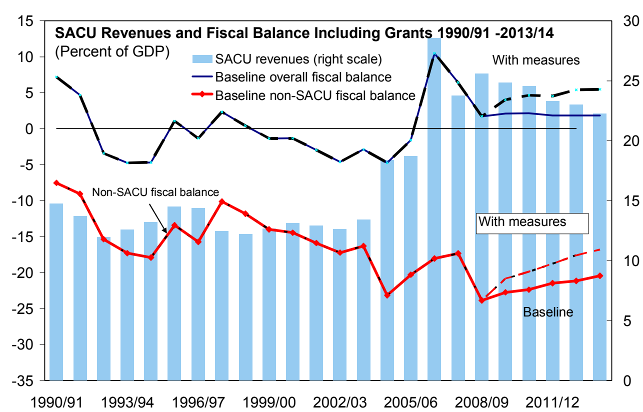
Box 1. Summary of the 2007 Consultation Discussions

Directors expressed concern about the slow pace of economic growth that lags behind most of other lower middle income countries, emphasized the need to ensure fiscal sustainability and safeguard priority spending to address urgent social needs (HIV/AIDS and unemployment). The Fund encouraged the authorities to use the buoyant SACU revenues to accelerate fiscal and structural reforms aimed at securing macroeconomic stability and addressing impediments to higher growth and poverty reduction. It commended the authorities' efforts in rebuilding international reserves, strengthening banking supervision, and the passage of key financial legislation. Finally, directors recommended the timely implementation of the Poverty Reduction Strategy and Action Program and in line with the medium-term fiscal expenditure framework.

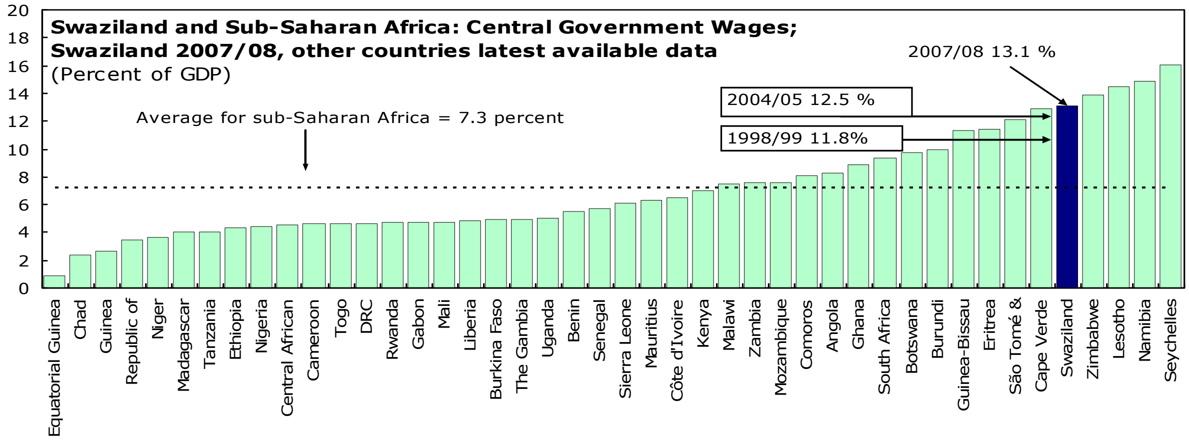
A. Fiscal Sustainability and Reforms

8. **Swaziland's fiscal stance is highly dependent on SACU revenues but these are not likely to be sustained,** based on: (i) a call by South Africa to revisit the revenue-sharing formula; (ii) a slowdown in South Africa's economic growth; (iii) a reduction in common external tariff rates due to trade liberalization; and (iv) possible transformation of the Southern African Development Community (SADC) into a customs union, which would imply lower shares for SACU members.

9. **In anticipation of SACU revenue declines in the long term, fiscal policy is not tight enough to make room for the savings needed** to smooth expenditure and prevent abrupt fiscal adjustment that could undermine macroeconomic stability**.** Furthermore, a tighter fiscal policy in the near term is also advisable from a cyclical perspective given the current high inflation that is anticipated to remain in 2009. Hence**,** the fiscal expansion of the 2008/09 budget and its medium-term fiscal outlook should be corrected, with adjustments equivalent to 4 percent of GDP over the medium term to secure savings (see below).



Sources: National authorities and IMF staff estimates and projections.



10. **To help put in context recent fiscal surpluses owing to temporary surges of SACU revenue, the non-SACU fiscal balance is used to estimate the deficit and level of adjustment needed for fiscal sustainability.** [4] Based on "normal" SACU revenue of 13 percent of GDP (the average for 1996/97–2004/05), staff targeted a sustainable non-SACU deficit of 16.8 percent of GDP. However, the authorities project a non-SACU deficit of 26.8 percent of GDP in the 2008/09 budget. Staff estimates that without reform, the fiscal imbalance would worsen, with non-SACU deficits of about 22 percent over the medium term.

11. **To achieve sustainable fiscal balances, staff proposed a phased implementation of revenue and expenditure reforms while providing for more spending on high-priority sectors.** Measures to immediately improve tax administration and introduce the VAT in the next few years should increase revenue by about 2 percent of GDP by 2013/14.[5] Civil service reform could bring the wage bill back to 12 percent of GDP, about the level in 2004/05—though the sub-Saharan African average is 7.3 percent to GDP. Expenditure reform should therefore combine consolidation, reorientation, and quality improvements to reduce spending by about 2 percent of GDP and allow fiscal space to facilitate economic growth and reduce poverty. On civil service reform, the performance management system, developed with the Botswana National Productivity Board, needs to be implemented promptly; it should involve redeployment toward prioritized sectors such as health care while promoting increased productivity, transparency, and accountability.[6] Though they concurred with the staff

[4] The non-SACU fiscal balance is defined as the overall fiscal balance excluding SACU revenues (see the 2007 Selected Issues Paper). A sustainable non-SACU fiscal balance allows for maintaining international reserves at about three months of imports, sufficient to support confidence in the currency peg and a low debt burden.

[5] In 2007 the revenue administration consultant estimated that only 20 percent of collectible tax is collected.

[6] Human resource allocations should better reflect priority sectors. For example, in 2007/08, only 7 percent of the wage bill was for the health sector; education received 37 percent and protection services 27 percent.

analysis, the authorities admitted that social pressures and a cumbersome bureaucracy had delayed implementation.

Swaziland: Medium Term Fiscal Scenario Without and With Measures [1]/
(Percent of GDP)

	2007/08	2008/09 Budget	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14
Baseline								
Non-SACU fiscal balance w/o measures	**-17.3**	**-26.9**	**-23.9**	**-22.7**	**-22.4**	**-21.5**	**-21.2**	**-20.4**
Revenues w/o SACU	16.0	13.6	13.4	13.8	14.0	14.0	14.2	14.6
Expenditures	33.3	40.5	37.2	36.5	36.4	35.5	35.4	35.0
Wages and salaries	13.1	16.7	13.8	13.8	13.7	13.6	13.5	13.2
Goods and services	6.4	6.5	6.4	6.4	6.4	6.4	6.5	6.5
Subsidies and transfers	4.3	7.0	7.1	5.7	5.7	4.8	4.8	4.7
Capital Expenditure	8.2	9.5	9.2	10.0	10.0	10.0	10.0	10.0
Interest payments	1.0	0.9	0.9	0.8	0.7	0.7	0.6	0.6
Adjusted scenario								
Non-SACU fiscal balance with measures				**-20.8**	**-19.9**	**-18.8**	**-17.6**	**-16.8**
Revenue w/o SACU				14.7	15.1	15.3	16.2	16.5
Expenditures				35.6	35.1	34.1	33.8	33.3
Of Which:								
Wages and salaries				13.3	13.0	12.8	12.6	12.2
Goods and services				6.4	6.4	6.4	6.4	6.3
Subsidies and transfers				5.3	5.1	4.2	4.0	3.8
Capital Expenditure				10.2	10.3	10.4	10.7	10.9
Memorandum items:								
SACU receipts [2]/	23.8	25.6	25.6	24.9	24.5	23.3	23.0	22.3
Overall balance without measures	6.4	-1.3	1.7	2.1	2.2	1.8	1.8	1.8
Overall balance with measures				4.0	4.7	4.5	5.4	5.5

[1]/ The fiscal year runs from April 1 to March 31.
[2]/ The buoyant SACU revenues through 2013/14 are consistent with the forecast of the South African staff team.

12. **Improvement in public expenditure management and assurance that spending is of high quality is crucial to successful fiscal adjustment.** Poor coordination of budget execution across government agencies has resulted in under-spending for some, arrears for others, and frequent supplementary budgets. To better manage public expenditure, the authorities highlighted continuing improvement of the procurement system and reform of the Public Finance Management Act. Staff underscored the need to assess expenditure and budget allocation on the basis of the social rate of return and government priorities in health, education, and agriculture, consistent with the Poverty Reduction Strategy and Action Program (PRSAP).

13. **Staff proposed an alternative scenario based on fiscal and structural reforms, preferably starting in 2008/09, that could generate GDP growth of about 4 percent over the medium term.** With reforms, the saving-investment balance should improve and foreign investment and donor financing be attracted, thus helping to raise GDP growth. Improved fiscal surpluses will help sustain reserves at more than 3.5 months of imports of goods and

services[7] while reducing the debt-to-GDP ratio to about 8 percent by 2012. While agreeing with staff on the risk to SACU revenues and the need for fiscal adjustments, the authorities identified political constraints and enormous social needs as formidable challenges to fiscal consolidation. Nonetheless, the authorities plan to save this year's unbudgeted SACU windfall.[8]

Swaziland: Medium-Term Scenario, 2008-2013
(Percent of GDP, unless noted otherwise)

	2007	2008	2009	2010	2011	2012	2013
Main macroeconomic variables [1]							
Without measures							
Real GDP growth	3.5	2.6	2.5	2.5	2.5	2.5	2.5
Inflation	8.2	12.7	8.9	6.0	5.9	5.5	5.3
Investment/GDP	16.2	17.4	17.7	17.2	16.8	16.8	16.3
GDP per capita at constant prices	3.1	2.1	2.1	2.1	2.1	2.1	2.1
Current account balance	-1.4	-5.3	-2.0	-2.6	-3.2	-3.1	-2.6
Gross official reserves (months of imports of goods and nonfactor services)	3.6	3.2	2.9	2.8	2.6	2.6	2.7
Government debt	18.8	15.9	14.4	13.5	12.7	12.0	11.5
Total Revenues and grants	39.7	39.0	38.7	38.5	37.3	37.2	36.9
Total Expenditure and Net Lending	33.3	37.2	36.5	36.4	35.5	35.4	35.0
Fiscal balance, including grants	6.4	1.7	2.1	2.2	1.8	1.8	1.8
Reform policies scenario [2]							
Real GDP growth		2.6	3.4	3.8	4.1	4.6	4.6
Investment/GDP		17.4	18.4	18.6	18.9	19.3	19.5
GDP per capita at constant prices		2.1	3.0	3.4	3.7	4.2	4.2
Current account balance		-5.3	-0.3	-0.1	0.5	1.3	1.3
Gross official reserves (months of imports of goods and nonfactor services)		3.2	3.4	3.6	3.7	3.9	4.0
Government debt		15.9	10.6	9.0	8.0	7.6	5.1
Total Revenues and grants		39.0	39.6	39.6	38.6	39.2	38.8
Total Expenditure and Net Lending		37.2	35.5	35.0	34.1	33.8	33.3
Fiscal balance, including grants		1.7	4.0	4.7	4.5	5.4	5.5

[1] Fiscal year runs from April 1 to March 31.

2 Assuming that fiscal policy and structural reforms including reducing the cost of doing business; improving the quality of public institutions; addressing the lack of transparency and poor administrative coordination; increasing labor market flexibility; simplifying business licensing; and improving infrastructure) will result in fiscal and current account surpluses.

B. External Stability and Exchange Rate Policy

14. **Sufficient international reserves are critical to safeguard external stability and confidence in the currency peg with South Africa,** which has served the country well. Staff supported the authorities' policy to have reserves of at least three months of import cover. The authorities believe that this level is appropriate in relation to the domestic monetary base (reflecting the free circulation of the rand) and external debt, while preserving confidence in the peg and serving as a cushion against adverse external shocks.

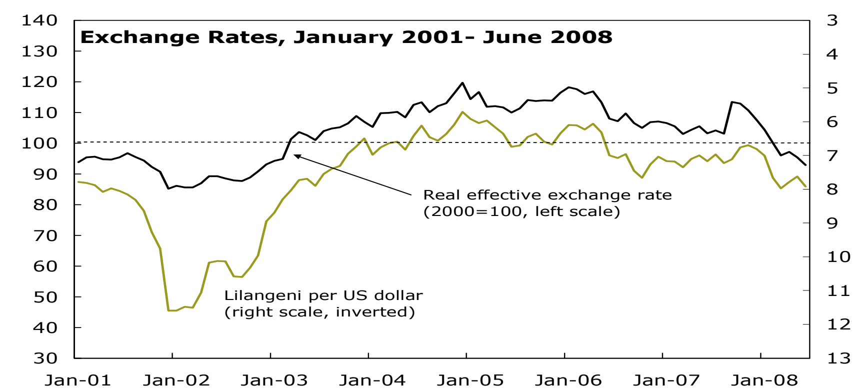
[7] Neighboring countries have higher import coverage: Botswana, more than 26 months; Lesotho, about seven months; and South Africa 3.7 months. Only Namibia has lower import coverage at 2.8 months.

[8] The difference between the estimated and actual value of the revenue-sharing pool in any given year.

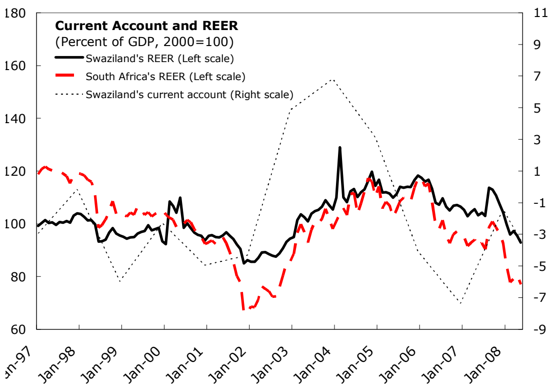
15. **Debt sustainability analysis (DSA) shows that Swaziland has very low debt Tables 7 and 8).** Since 2002 despite the most recent depreciation, total public sector debt has declined, reflecting in part limited new borrowing and an exchange rate appreciation between 2003 and 2006. As a lower-medium-income country, Swaziland has limited access to concessionary loans; any large increases in external debt would carry high interest costs.

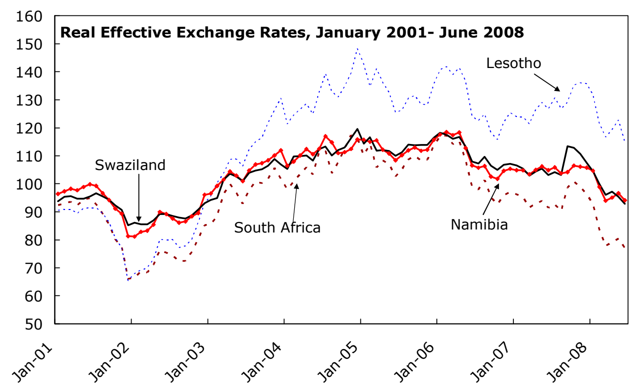
16. **The level of the exchange rate seems broadly adequate and the exchange rate regime is appropriate.** The assessment of the exchange rate level is based on two methodologies. The purchasing power parity methodology, adjusted for productivity differentials, indicates no misalignment as of 2008. The external sustainability approach indicates that stabilizing the current account at the net foreign asset (NFA) position as of 2007 would imply a somewhat stronger current account than projected, which could imply some overvaluation of the real exchange rate. Yet there are no other clear signs of an overvaluation and the depreciation of the real exchange rate since 2006 has boosted Swaziland's exports. As to the exchange rate regime, staff and the authorities agreed that the currency peg under the CMA should be maintained because it facilitates capital and current transactions with the country's most important economic partner, South Africa.

17. **In the CMA, movements in the real effective exchange rate are largely exogenously determined, and more effort is needed to improve structural competitiveness.** With the Swaziland's inflation rate also closely tracking South Africa's—and responsibility for macroeconomic stability resting squarely with fiscal policy—competitiveness should be pursued through structural reforms that improve the investment climate and compensate for eroding trade preferences. Staff acknowledged that—despite the depreciation in 2008 of the rand—Swaziland's lackluster export performance was, to a large part, due to lower preferential prices for sugar exports to the EU. Loss of preferences in the textiles sector is aggravated by escalating wage and other operational costs, labor strikes, and prospects for that sector do not look encouraging.



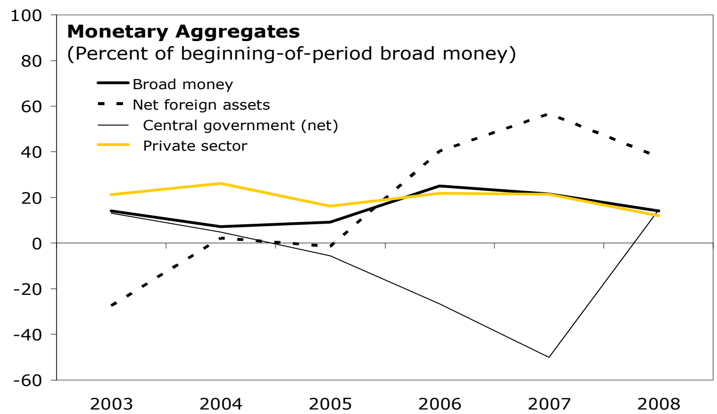
Sources: International Financial Statistics and Information Notice System.





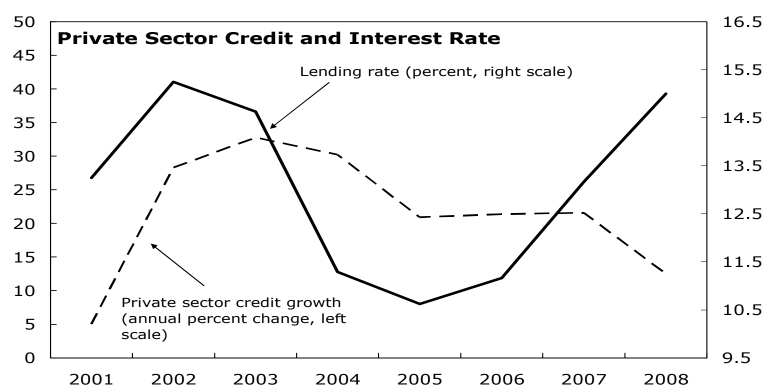
C. Monetary and Financial Sector Policies

18. **The CBS has limited independent monetary policy as a CMA member, and financial institutions tend to follow their rates in South Africa rather than the CBS policy rate.** Nevertheless, for the first time in recent memory, the CBS in June this year did not match a 50 basis point increase in the SARB repo rate. A lower policy rate does not necessarily lead to lower effective interest rates in Swaziland and by having a different policy rate from the SARB rate; the CBS could risk public misinterpretation about its commitment to combat inflation. The CBS is closely monitoring the impact of its June interest rate decision and capital outflows.



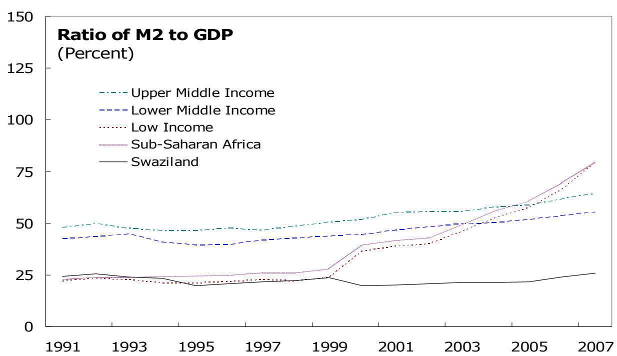
Sources: National authorities, and IMF staff estimates and projections.

19. **Authorities and staff agreed that continuing supply shocks and rising inflation expectations heighten the importance of clearly communicated justification of policy** to help contain the rise in inflation expectations, particularly given the July government wage settlement of 10.5 percent. Efforts could be made to educate the public about the nature of the current shocks, the importance of anchoring second-round inflation effects, and the long-run trade-off between inflation and growth.

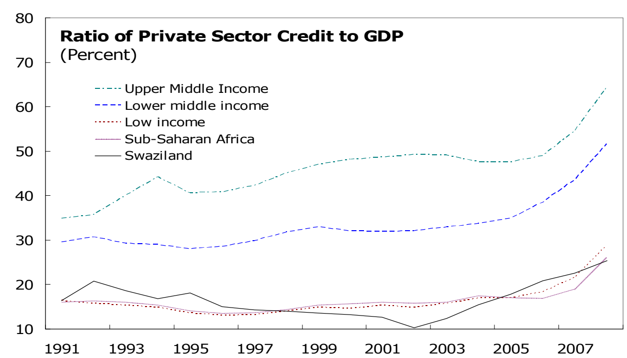


Sources: International Financial Statistics and IMF staff estimates.

20. **The financial sector faces some vulnerabilities from weaknesses in one bank and emerging vulnerabilities from the fast growth of insufficiently regulated SCCOs and the emergence of pyramid schemes.** In 2008 the number of nonbank financial institutions (NBFIs) has grown significantly as they attempt to take advantage of the liquidity surge from the requirement that all insurance and retirement funds must increase their holdings of domestic assets from 10 to 30 percent of total assets through 2009. The emergence of pyramid schemes, offering inordinately high rates of return, could also pose significant risks to the financial sector if left unchecked because they face constant rollover risks and are very likely to fail. Staff reiterated the urgency of prompt enactment and full implementation of the Financial Services Regulatory Authority (FSRA), Security, Payment System and Clearance bills to under gird the soundness of the financial sector, prevent regulatory arbitrage, and facilitate deepening of the sector. The authorities welcomed the financial sector strategy note prepared by staff emphasizing the need for deepening.



Sources: International Financial Statistics and World Economic Outlook.



Source: International Financial Statistics and World Economic Outlook.

21. **The authorities have approved privatization of Swazi Bank and are monitoring bank lending to the sugar industry.** On Swazi Bank, an advisory committee concurred with the staff view that any privatization strategy should be preceded by separation of its development and commercial activities. As prospects for the sugar sector weaken, staff urged the authorities to closely monitor loans to the industry and further scrutinize the risk management practices of banks. It is imperative that revised loan provisioning requirements be issued and enforced.

22. **To better supervise and regulate SCCOs, the Ministry of Agriculture and Cooperatives (MACO) and the CBS have begun a technical collaboration plan.** The plan sets prudential standards for SCCOs and provides for training of MACO staff to better monitor financial soundness, enforce compliance, and compile information relevant to monitoring SCCOs. MACO should move quickly to preserve the assets of some insolvent SCCOs to ensure public confidence in that sector.

23. **The recent emergence of pyramid schemes has increased the threat they pose to the stability of the financial system.** These entities as yet are relatively small. The authorities have warned the public of the risks and have taken legal action against some

operators. Staff urges further efforts, such as formalizing coordinated efforts among financial sector regulators, improving internal processes for dealing with fraudulent financial operations, and passing legislation prohibiting such operations.

24. **Concerning the insurance and retirement sector, a recently announced domestic investment requirement should be reconsidered.** Staff noted that, in the absence of deep markets, the requirement—at least 10 percent by 2007 and 30 percent by 2009 of investable funds will need to be held in Swazi assets—could lead to severe distortions, discourage investment flows to Swaziland and undermine efforts to develop the financial sector in the country. It argued that implementation experience to date showed that some insurance and retirement funds are merely displacing commercial bank lending and some are rerouted off-shore without financing new capital formation in Swaziland. Hence, staff recommended that the requirement should be gradually phased out.

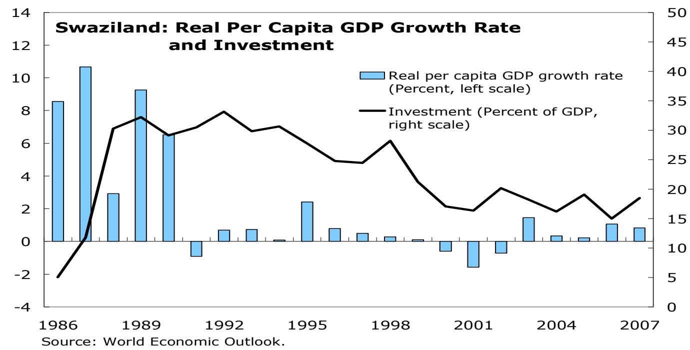
D. Response to the Fuel and Food Price Increases

25. **The recent surges of food and fuel prices have significantly affected the poor and created special challenges for the authorities.** Staff discussed policy options for dealing with surging prices, focusing on fiscal viability, minimization of market distortions, and effective and timely delivery to target groups. Staff recommended liberalization of food imports (e.g., maize) and providing assistance through already extensive food distribution programs. The policy of delaying the price pass-through should be abolished to depoliticize price adjustments and eliminate market distortion. Because Swaziland faces frequent food shortages, the authorities need to implement long-term solutions that are consistent with their sectoral policy while remaining fiscally sustainable. The National Disaster Management Agency needs to improve coordination of stakeholders on the food security issue. The authorities agreed that targeted assistance to the most vulnerable groups is appropriate, but are concerned about increasing public outcry for more interventionist programs, mostly general subsidies for commodities, and for agricultural inputs and finance.

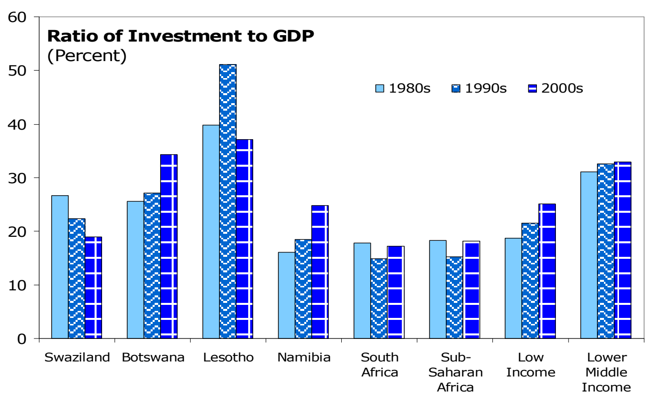
26. **In September, in response to the surges of food and fuel prices, the "food price crisis" committee proposed several measures to the Cabinet, but it remains unclear when implementation will take place.** These measures are consistent with the Comprehensive Agricultural Strategy and the National Program for Food Security. Short-term measures include improvements to the food distribution provided by the World Food Program and other donors, provision of cash transfers, and removal of levies on dairy and wheat products. Other recommendations included subsidies to boost maize production and implementation of the agricultural strategy.

E. Growth, Poverty Reduction, and Competitiveness

27. **Poverty and lackluster economic growth are major risks to the social and economic stability of Swaziland.** Growth prospects are seriously constrained by a low investment-to-GDP ratio, a poor investment climate, recurrent droughts, the HIV/AIDS epidemic, and the high cost of doing business. Failure to implement other structural and land reforms further reduces growth prospects. The PRSAP approved last year could be the basis for strategies and policies to reduce poverty, but it needs a clearer implementation strategy and measures of tangible progress.

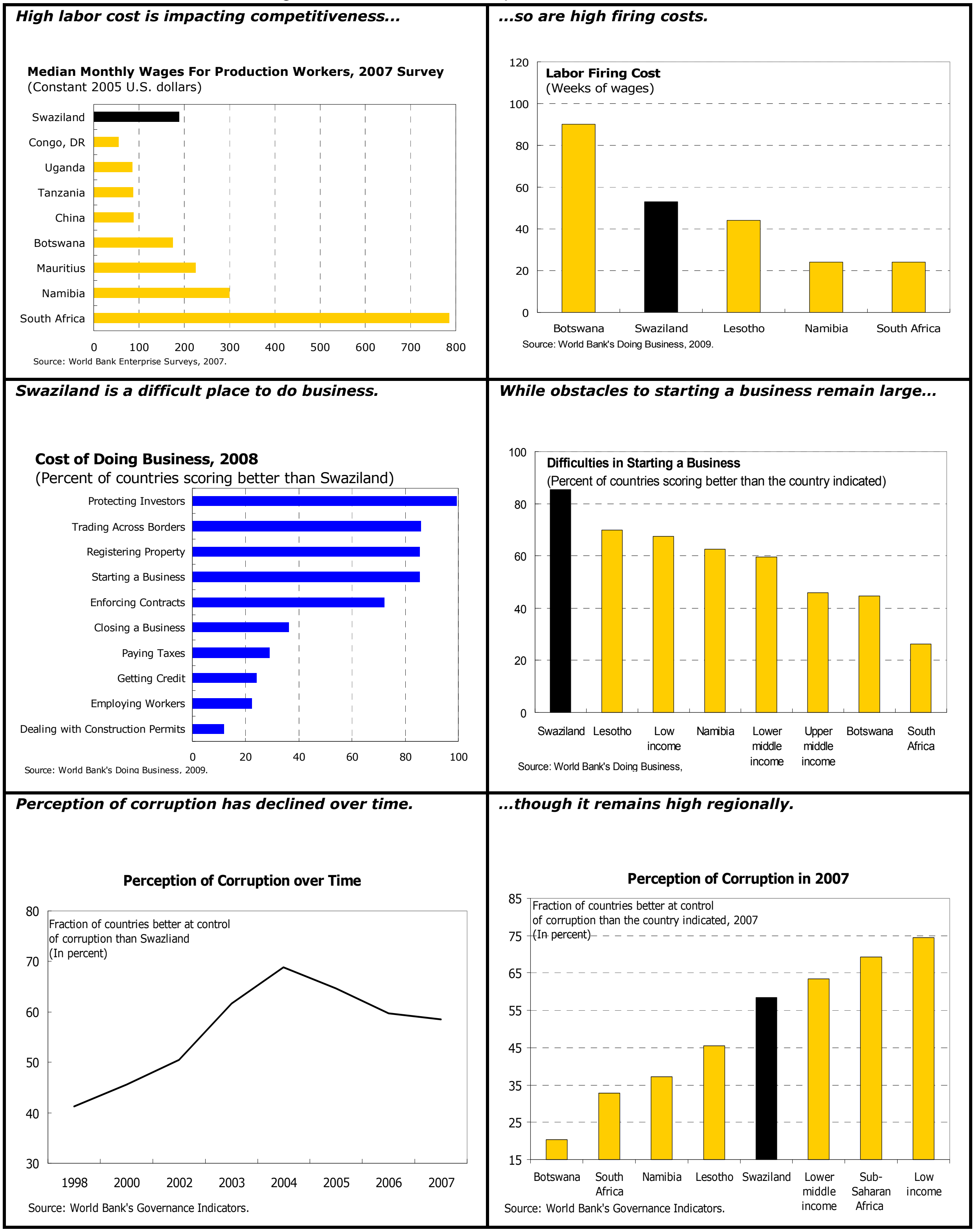


28. **To increase its growth prospects, Swaziland needs to increase investment and deepen its financial sector (see the SIP).** Since 2002 total investment has been stagnant at about 18 percent of GDP—not enough to promote growth and employment. Foreign direct investment (FDI) continues to decline. Swaziland needs to channel domestic resources to viable investment projects, with special attention to small and medium enterprises and public and Private Partnerships (PPPs). The authorities agreed with staff's view that the approach to PPPs should be cautious given the country's limited institutional capacity, inadequate legal framework, and the need to mitigate fiscal risks. Deepening the financial sector should help improve resource allocation.



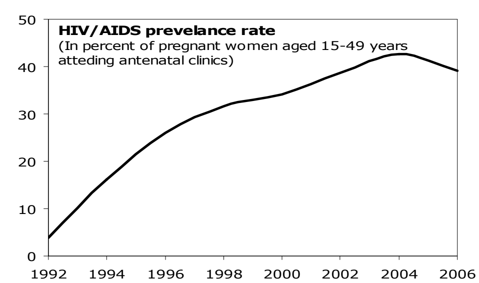
29. **Private-sector-led growth is severely constrained by concerns about Swaziland's competitiveness and governance issues (Figure 1).** To address these issues, staff recommended that the authorities implement the recommendations of the Swaziland Investor Roadmap Study (2005) and the Investment Climate Assessment (2008) prepared by the World Bank. The authorities welcomed the World Bank's Interim Strategy Note to help them address competitiveness, governance, and HIV/AIDS issues. They also noted that enactment of the Companies and Competition Bills in 2008 provides a legal framework for businesses to flourish, and expected the one-stop shop at the Swaziland Investment Promotion Agency to help reduce the cost of doing business. An anticorruption commissioner was appointed in 2008 and work has started on bringing corruption cases before the court. However, serious constraints within the court system could hinder the work.

Figure 1. Swaziland: Competitiveness Indicators

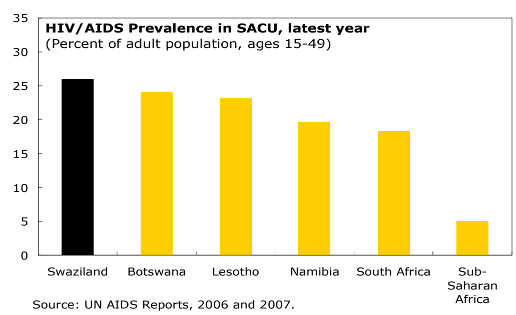


30. **Swaziland continues to promote regional economic integration and negotiate trade agreements in order to increase market access for its exports.** Discussions continue within SADC to initiate a free trade area and eventually a SADC customs union. In 2007Swaziland and four other SADC members initialed an Interim Economic Partnership Agreement with the EU for duty- and quota-free access to the EU market. Negotiations have also been concluded on a SACU-EFTA (European Free Trade Association) free trade agreement. SACU is negotiating with the US on a Trade Investment Development and Cooperation Agreement (TIDCA) and with the Latin American trading block MERCOSUR on a preferential trade agreement.

31. **The authorities are taking steps to mitigate the adverse effects of HIV/AIDS (Box 2)**. A plan will be provided to the Global Fund that details the use of $81 million that was awarded in 2007. The authorities are currently considering a multiyear plan to: (i) scale up investment in education of young children and orphans left behind by HIV/AIDS, providing them with free meals and reducing drop-out rates; (ii) provide short-term child support grants with assistance from the World Bank and IFC; and (iii) scale up use of antiretroviral therapy.



Source: Ministry of Health and Social Welfare, 10th. Round of Serosurveillance

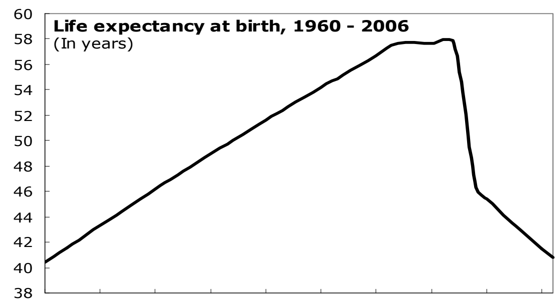


Source: UN AIDS Reports, 2006 and 2007.

Box 2. Macroeconomic Impact of HIV/AIDS in Swaziland

HIV/AIDS presents formidable longer-term challenges for Swaziland. Cross-country studies of the impact of HIV/AIDS on growth range from insignificant or very modest to losses of more than 2 percentage points a year. HIV/AIDS affects growth negatively by, among other things, lowering life expectancy, reducing incentives for human and physical capital formation, and limiting productivity growth.

Staff estimates based on two studies[1] suggest that if life expectancy (a measure of health and human capital) had stayed at 57 years— the level in mid-1990s before HIV/AIDS accelerated and growth decelerated—instead of the current estimate of 41 years, Swaziland's per capita GDP growth would have been higher on average by 1.3 percentage points a year.



Source: World Bank's World Development Indicators.

Using a different methodology, the International Labor Organization (2004) estimates that HIV/AIDS reduced per capita GDP growth in Swaziland on average by 1.8 percentage points each year from 1992 through 2002.

The adverse impact on education could be sizable, increasing the burden on future generations. According to the ILO (2004), in Swaziland the cost of hiring and training teachers to replace those lost to HIV/AIDS is projected to reach US$233 million (8 percent of 2007 GDP) by 2016.

The toll on Swaziland's agriculture, a major source of earnings for a large segment of the population, could be heavy. HIV/AIDS can lower the agricultural labor supply, reduce the productivity of affected farmers, as well as the income needed for purchasing farm inputs. These effects have resulted in an estimated 54 percent reduction in production of maize and 34 percent reduction in land cultivation (UNAIDS, 2002).

The impact on Swaziland's businesses is significantly larger than in comparator countries that also suffer from HIV/AIDS. According to the 2007 World bank investment climate assessment survey, over 50 percent of company managers reported much higher worker absenteeism due to sickness than other countries in Southern Africa. Among the workers surveyed, 25 percent reported being sick in the previous 30 days compared with less that 20 percent in Botswana and Namibia.

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[1] See Jeffrey D. Sachs and Andrew M. Warner, 1997, "Fundamental Sources of Long-Run Growth," *American Economic Review*, Vol. 87, no. 2., pp. 184–88; and Xavier Sala-i-Martin, Gernot Dooppelhofer, and Ronald I. Miller, 2004, "Determinants of Long-Term Growth: A Bayesian Averaging of Classical Estimates (BACE) Approach *American Economic Review*, Vol. 94, no. 4, pp. 813–35.

[2] International Labor Organization, 2004, "HIV/AIDS and work: global estimates, impact and response."

IV. Staff Appraisal

32. **Achieving government's target growth over the medium term remains elusive, without prompt structural reforms.** Risks stem from the eventual decline of SACU revenues and emerging financial vulnerabilities. The short-term outlook is further clouded by a global economic slowdown and the adverse impact of high food and fuel prices. Timely economic and structural reforms, increasing investment, and aggressively tackling the HIV/AIDS epidemic are necessary to stimulate growth and reduce poverty.

33. **Because SACU revenues are expected to stay high in the next few years, they offer an opportunity for Swaziland to generate fiscal savings** to help smooth out expenditure later when SACU revenues decline and to safeguard economic stability, address structural reforms, and improve the effectiveness of public policy. The authorities should take immediate steps to reduce the level of expenditures in 2008/09 and make further adjustments in the 2009/10 budget and the medium-term fiscal policy framework. Operationalizing the Revenue Authority and introducing the VAT could increase domestic revenue significantly. Much-needed spending reform requires improving the quality of expenditure, tangible civil service reform, and better assessment of investments. Expenditure must be reoriented toward priority sectors to reduce widespread poverty.

34. **The monetary regime under the CMA, including the exchange rate peg to the rand have served the country well given Swaziland's economic integration with South Africa**. Fiscal and structural adjustment is required to support confidence in the peg and ensure external stability. With comfortable reserve levels, the exchange rate does not appear to be misaligned. Monetary policy should stay tight to limit the effects from surges of food and fuel prices, and the CBS should keep its policy rate as close as possible to the SARB's.

35. **Improvement of the financial position of the Swazi Bank through privatization, tighter supervision of SCCOs, and addressing pyramid schemes are priorities for preserving financial stability.** Prompt enactment of financial sector bills will help safeguard financial stability**.** Addressing pyramid schemes implies better coordination among domestic and regional financial regulators, improving internal processes for dealing with fraudulent operations, and passing laws prohibiting pyramid operations. For the insurance and retirement funds, the domestic investment requirement should be reconsidered, with a view to gradual phase-out because it could create a nonmarket risk premium and make it harder to deepen the financial sector if the market perceives it to be a move toward capital control.

36. **Responses to food and fuel price surges should focus on the most vulnerable population, using existing distribution channels for food delivery and liberalizing food imports.** General subsidies and delayed pass-through of price adjustment should be discouraged**.**

37. It is proposed that the next Article IV consultation with Swaziland be held on the standard 12-month cycle.

Table 1. Swaziland: Basic Economic and Financial Indicators, 2005-2013

	2005	2006	2007	2008	2009	2010	2011	2012	2013
			Est.	Projections					
	(Annual percentage change, unless stated otherwise)								
National income and prices									
GDP at constant prices	2.2	2.9	3.5	2.6	2.5	2.5	2.5	2.5	2.5
GDP per capita at constant prices	1.8	2.5	3.1	2.1	2.1	2.1	2.1	2.1	2.1
GDP deflator	6.6	6.5	9.0	9.2	8.1	6.5	6.6	5.4	4.8
CPI (period average)	4.8	5.3	8.2	12.7	8.9	6.0	5.9	5.5	5.3
CPI (end of period)	6.3	5.5	9.8	13.5	7.5	5.9	5.7	5.4	5.3
External sector									
Current account balance (millions of U.S. dollars)	-102.6	-196.7	-41.2	-158.4	-64.2	-88.9	-115.9	-118.3	-102.4
Export volume, f.o.b.	-15.5	-2.6	-3.7	12.7	10.8	-7.5	-0.4	0.6	0.6
Import volume, f.o.b.	-2.0	-2.4	4.0	3.6	2.0	5.8	11.5	13.8	5.2
Nominal effective exchange rate [1/]	2.6	-4.2	8.7	...	...	...	...	...	...
Real effective exchange rate [1/]	-2.6	-8.0	3.3	...	...	...	...	...	...
Terms of trade	7.7	4.5	3.0						
Money and credit [2]									
Broad money	5.9	25.1	21.4	...	...	...	...	...	...
Domestic Credit	10.6	-4.9	-28.7						
Central government (net) [3]	-5.6	-26.7	-50.0						
Private sector	16.2	21.8	21.4						
Prime lending rate (percent; end of period)	10.5	12.5	14.5	...	...	...	...	...	...
Interest rate on 12-month time deposits (percent; end of period	3.5	8.5	10.0	...	...	...	...	...	...
Discount rate (end of period)	7.5	9.0	11.0	...	...				
	(Percent of GDP)								
Gross national savings	14.5	9.3	14.8	12.1	15.7	14.6	13.6	13.7	13.7
Of which : government	6.7	12.8	15.3	11.1	12.3	12.4	12.1	12.1	12.0
Gross domestic investment	18.6	16.7	16.2	17.4	17.7	17.2	16.8	16.8	16.3
Of which : government	8.8	7.9	8.5	9.4	10.2	10.2	10.2	10.2	10.2
Central government finances (fiscal year) [4]									
Total revenue and grants	33.2	43.0	39.7	39.0	38.7	38.5	37.3	37.2	36.9
Of which : South African Customs Union (SACU) receipts	18.7	28.5	23.8	25.6	24.9	24.5	23.3	23.0	22.3
Total expenditure and net lending	34.8	32.5	33.3	37.2	36.5	36.4	35.5	35.4	35.0
Current expenditure and net lending	26.7	25.1	24.8	28.1	26.6	26.5	25.5	25.4	25.0
Central government balance (including grants)	-1.6	10.5	6.4	1.7	2.1	2.2	1.8	1.8	1.8
Primary balance (including grants)	-0.4	11.4	7.4	2.6	2.9	2.9	2.5	2.5	2.4
Government debt	16.5	17.4	18.8	15.5	15.9	14.4	13.5	12.7	12.7
Non-SACU fiscal balance	-20.3	-18.0	-17.3	-23.9	-21.6	-20.8	-20.5	-21.5	-21.2
External sector									
Current account balance	-4.1	-7.4	-1.4	-5.3	-2.0	-2.6	-3.2	-3.1	-2.6
Trade balance (merchandise goods)	-10.2	-9.4	-8.5	-19.3	-15.3	-14.7	-15.0	-14.5	-13.3
Capital and financial account balance	-1.4	11.5	26.4	7.5	-0.4	2.4	4.0	5.1	5.6
Overall balance	0.4	5.6	12.4	1.1	-1.2	-0.1	0.4	1.0	1.5
External debt	17.2	16.6	16.7	17.2	16.0	15.2	14.5	13.9	11.9
Memorandum items :									
GDP in current prices (millions of emalangeni) [5]	16,050	18,078	20,386	22,856	25,321	27,634	30,177	32,621	35,017
Balance of payments (millions of U.S. dollars)	11	150	358	32	-38	-5	14	37	60
Gross official reserves (millions of U.S. dollars)	244	367	747	681	622	608	607	631	677
(months of imports of goods and nonfactor services)	1.3	1.9	3.6	3.2	2.9	2.8	2.6	2.6	2.7
Net official international reserves (millions of U.S. dollars)	240	363	743	677	618	604	603	627	674
(months of imports of goods and nonfactor services)	1.3	1.9	3.5	3.2	2.9	2.7	2.6	2.6	2.7
(months of imports of goods)	1.5	2.3	4.4	3.6	3.3	3.2	3.0	3.0	3.1
Total external debt (millions of U.S. dollars)	435	441	507	520	520	530	534	541	550

Sources: Swazi authorities; and IMF staff projections.

[1] IMF Information Notice System trade-weighted; end of period.

[2] In percent of beginning-of-period broad money.

[3] Includes government holdings abroad.

[4] The fiscal year runs from April 1 to March 31.

[5] The official GDP numbers from 1994 to 2006 were significantly revised in 2007, and recently in 2008.

Table 2. Swaziland: Summary of Central Government Operations, 2006/07-2013/14 [1]

	2006/07	2007/08	2008/09	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14
		Est.	Budget	Est. [2]		Projections			
				(Millions of emalangeni)					
Total revenue and grants	8,021	8,341	9,209	9,145	10,013	10,896	11,487	12,371	13,145
Tax revenue	7,683	7,565	8,846	8,852	9,672	10,519	11,081	11,913	12,652
SACU receipts	5,322	4,990	6,009	6,009	6,440	6,934	7,174	7,641	7,938
Non-SACU revenue	2,361	2,575	2,837	2,843	3,233	3,585	3,907	4,272	4,713
Nontax revenue	172	713	217	204	242	267	283	309	333
Total expenditure and net lending	6,063	6,993	9,504	8,737	9,462	10,287	10,922	11,760	12,490
Current expenditure	4,681	5,217	7,288	6,607	6,891	7,478	7,843	8,434	8,926
Wages and salaries	2,589	2,750	3,924	3,247	3,572	3,873	4,187	4,485	4,704
Goods and services	1,203	1,343	1,517	1,490	1,645	1,805	1,970	2,159	2,331
Interest payments	163	211	212	212	198	203	207	212	216
Subsidies and transfers	726	913	1,635	1,657	1,476	1,597	1,478	1,578	1,675
Capital expenditure	1,437	1,733	2,233	2,148	2,590	2,827	3,079	3,327	3,564
Net lending	-55	43	-18	-18	-18	-18	0	0	0
Primary balance	2,121	1,560	-82	620	749	812	773	822	871
Overall balance (including grants)	1,958	1,348	-295	408	551	610	565	611	655
Overall balance (excluding grants)	1,792	1,285	-440	319	452	499	442	461	494
Financing	-1,958	-1,348	295	-408	-551	-610	-565	-611	-655
Foreign (net)	214	98	40	129	96	75	79	90	94
Domestic (net)	-868	-1,446	255	-537	-646	-684	-644	-701	-749
Government deposits abroad	-1,304	-855	...	...	...	...	...		
Government debt [3]	3,252	3,940	3,641	3,736	3,736	3,821	3,900	3,990	4,084
Foreign	2,742	3,500	3,531	3,626	3,626	3,701	3,780	3,870	3,964
Domestic	509	440	110	110	110	120	120	120	120
				(Percent of GDP, unless otherwise specified)					
Total revenue and grants	43.0	39.7	39.2	39.0	38.7	38.5	37.3	37.2	36.9
Tax revenue	41.2	36.0	37.7	37.7	37.3	37.2	36.0	35.9	35.5
SACU receipts	28.5	23.8	25.6	25.6	24.9	24.5	23.3	23.0	22.3
Non-SACU revenue	12.7	12.3	12.1	12.1	12.5	12.7	12.7	12.9	13.2
Nontax revenue	0.9	3.4	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Grants	0.9	0.3	0.6	0.4	0.4	0.4	0.4	0.5	0.5
Total expenditure and net lending	32.5	33.3	40.5	37.2	36.5	36.4	35.5	35.4	35.0
Current expenditure	25.1	24.8	31.1	28.1	26.6	26.5	25.5	25.4	25.0
Of which:									
Wages and salaries	13.9	13.1	16.7	13.8	13.8	13.7	13.6	13.5	13.2
Goods and services	6.4	6.4	6.5	6.4	6.4	6.4	6.4	6.5	6.5
Interest payments	0.9	1.0	0.9	0.9	0.8	0.7	0.7	0.6	0.6
Subsidies and transfers	3.9	4.3	7.0	7.1	5.7	5.7	4.8	4.8	4.7
Capital expenditure	7.7	8.2	9.5	9.2	10.0	10.0	10.0	10.0	10.0
Primary balance	11.4	7.4	-0.4	2.6	2.9	2.9	2.5	2.5	2.4
Overall balance (including grants)	10.5	6.4	-1.3	1.7	2.1	2.2	1.8	1.8	1.8
Overall balance (excluding grants)	9.6	6.1	-1.9	1.4	1.7	1.8	1.4	1.4	1.4
Non-SACU fiscal balance (w/grants)	-18.0	-17.3	-26.9	-23.9	-22.7	-22.4	-21.5	-21.2	-20.4
Financing	-10.5	-6.4	1.3	-1.7	-2.1	-2.2	-1.8	-1.8	-1.8
Foreign (net)	-5.8	0.5	0.2	0.5	0.4	0.3	0.3	0.3	0.3
Domestic (net)	-4.7	-6.9	1.1	-2.3	-2.5	-2.4	-2.1	-2.1	-2.1
Government deposits abroad	-7.0	-4.1							
Government debt	17.4	18.8	15.5	15.9	14.4	13.5	12.7	12.0	11.5
Foreign	14.7	16.7	15.0	15.4	14.0	13.1	12.3	11.6	11.1
Domestic	2.7	2.1	0.5	0.5	0.4	0.4	0.4	0.4	0.3
Memorandum items:									
GDP at current prices (millions of emalangeni)	18,655	21,004	23,472	23,472	25,899	28,270	30,788	33,220	35,638
Wages and salaries (percent of curren	55.3	52.7	53.8	49.1	51.8	51.8	53.4	53.2	52.7

Sources: Ministry of Finance; and Fund staff projections.

[1] Without corrective policy measures. The fiscal year runs from April 1 to March 31.

[3] Includes requested supplementary budget

[3] Disbursements less amortizations.

Table 3. Swaziland: Monetary Survey, 2004-2008 [1]
(Millions of emalangeni)

	2004	2005	2006	2007	Mar-08	Jun-08
Monetary authorities						
Net foreign assets	1,450	1,520	2,532	5,060	5,815	5,818
Central Bank of Swaziland (CBS)	1,243	1,520	2,497	3,780	4,994	5,818
Of which : Capital Investment Fund (CIF), managed by CBS.	667	0	0	0	0	0
Government	207	0	35	1,280	821	0
Net domestic assets	-973	-1,031	-2,003	-4,354	-5,171	-5,047
Central government (net)	-933	-1,083	-2,012	-4,049	-4,553	-4,488
CBS claims on government	252	101	55	15	0	11
Government deposits with CBS	-1,185	-1,184	-2,067	-4,063	-4,553	-4,499
Domestic	-311	-1,183	-1,993	-2,780	-3,691	-4,495
Foreign [2]	-874	0	-74	-1,283	-862	-4
Private sector	10	9	20	8	8	9
Commercial banks (net)	0	1	22	2	2	2
Other items (net)	-50	43	-33	-315	-628	-570
Reserve money	477	490	565	706	645	771
Commercial banks						
Net foreign assets	490	374	762	698	749	1,145
Reserves	256	211	354	499	472	525
Domestic credit	3,344	3,832	4,581	5,385	5,656	5,507
Central government (net)	331	302	306	169	196	80
Claims on Government	332	315	369	344	425	379
Government deposits	2	13	64	175	228	299
Private sector	3,013	3,531	4,276	5,216	5,460	5,427
Other items (net)	-1,110	-1,196	-1,589	-1,559	-1,642	-1,697
Private sector deposits	2,946	3,221	4,088	5,023	5,235	5,480
Monetary survey						
Net foreign assets	1,941	1,894	3,294	5,757	6,564	6,963
Domestic credit	2,421	2,758	2,590	1,344	1,111	1,028
Central government (net)	-602	-781	-1,706	-3,880	-4,356	-4,408
Private sector	3,023	3,539	4,296	5,224	5,468	5,436
Other items (net)	-1,180	-1,182	-1,542	-1,828	-2,199	-2,235
Broad money	3,182	3,471	4,342	5,273	5,477	5,756
Currency in circulation [3]	236	242	251	249	234	275
Deposits	2,946	3,229	4,091	5,024	5,243	5,482
	nnual change in percent of beginning-of-period broad money					
Broad money	7.2	9.1	25.1	21.4	18.0	14.1
Net foreign assets	2.2	-1.5	40.3	56.7	68.1	37.8
Domestic credit	30.9	10.6	-4.9	-28.7	-32.9	26.7
Central government (net)	4.8	-5.6	-26.7	-50.0	-52.9	14.7
Private sector	26.1	16.2	21.8	21.4	20.0	12.0
Other items (net)	-26.0	-0.1	-10.4	-6.6	-17.2	-50.4
Memorandum items:						
Currency/broad money (percent)	7.4	7.0	5.8	4.7	4.3	4.8
Reserve money/deposits (percent)	16.2	15.2	13.8	14.0	12.3	14.1
Money multiplier (broad money/reserve money)	6.7	7.1	7.7	7.5	8.5	7.5
Velocity (GDP/period average broad money)	4.72	4.32	4.26	4.24	4.12	4.11

Sources: Central Bank of Swaziland (CBS); and Fund staff estimates.

[1] End-of-year data. (For 2008, as of end-June)

[2] Counterpart of government deposits held abroad.

[3] Excludes rand in circulation.

[4] For 2008, change from June 2007.

Table 4. Swaziland: Commercial Banks' Performance Ratios, Dec. 2003 - 2008

	2003 Dec.	2004 Dec.	2005 Dec	2006 Dec	2007 June	2007 Dec	2008 June
	(Percent)						
Performance Ratios							
Basle capital ratio (Tier 1)	14	14	15	20	23	21	18
Basle capital ratio (Tier 2)	20	16	17	26	23	24	20
Asset Quality							
Loans to deposit ratio [1]	75	73	83	86	88	105	86
Earning assets to total assets	90	87	92	65	67	69	73
Nonperforming loans to total loans [1]	2	3	2	4	4	6	8
Reserve for losses to total loans	9	8	7	10	9	8	6
Liquidity Ratios							
Liquid assets to total deposits	19	18	17	20	20	19	16
Available reserves to total deposits	18	19	20	10	12	12	5
Liquid assets to total assets	14	14	13	15	14	13	13
Profitability Ratios							
Net income to average total assets (return on assets)	4	3	3	6	3	3	4
Net income to average total equity (return on equity)	29	20	20	52	26	15	14
Total expenses to total income	60	64	68	71	74	63	68

Source: Central Bank of Swaziland.

[1] Excluding the Swaziland Development and Savings Bank, which is owned by the government and offers both development finance and commercial banking services since its recapitalization and relaunch by the government in 2001.

Table 5. Swaziland: Balance of Payments, 2005-2013 [1]
(Millions of U.S. dollars, unless otherwise specified)

	2005	2006	2007	2008	2009	2010	2011	2012	2013
		Est.	Projections						
Current account balance	-102.6	-196.7	-41.2	-158.4	-64.2	-88.9	-115.9	-118.3	-102.4
Trade balance	-258.1	-252.1	-246.5	-573.1	-487.3	-493.7	-537.7	-548.0	-528.8
Exports, f.o.b.	1,636.5	1,663.9	1,766.8	1,681.1	1,737.3	1,804.0	1,850.8	1,965.9	2,093.0
Imports, f.o.b.	-1,894.6	-1,916.1	-2,013.3	-2,254.3	-2,224.6	-2,297.7	-2,388.5	-2,513.9	-2,621.8
Services (net)	-120.4	-90.1	-52.1	-16.9	-17.5	-22.7	-24.0	-25.8	-27.7
Exports of services	282.4	283.5	454.1	304.6	315.9	328.0	346.7	373.6	401.1
Imports of services	-402.8	-373.6	-506.2	-321.5	-333.5	-350.7	-370.7	-399.5	-428.8
Goods and services balance	-378.5	-342.3	-298.6	-590.0	-504.8	-516.4	-561.7	-573.8	-556.5
Income (net)	178.3	14.0	63.7	39.0	22.9	-2.5	-16.7	-46.1	-78.6
Income (credits)	271.3	241.8	280.5	201.5	197.0	198.2	207.6	205.4	203.6
Income (debits)	-93.0	-227.8	-216.8	-162.5	-174.0	-200.7	-224.3	-251.6	-282.2
Of which : interest	-20.1	-21.9	-24.5	-26.5	-26.4	-26.5	-26.7	-27.1	-27.5
Transfers (net)	97.5	131.6	193.7	392.6	417.7	429.9	462.5	501.7	532.7
Official sector (mainly SACU receipts) [2]	339.6	366.5	403.0	623.9	663.6	692.2	705.7	730.1	747.5
Private sector	-242.1	-234.9	-209.2	-231.3	-245.9	-262.3	-243.2	-228.4	-214.8
Capital and financial account balance	-46.7	158.6	404.0	190.2	26.0	84.4	129.6	155.5	162.1
Capital account balance	-3.5	24.8	-30.1	23.8	23.9	29.4	38.5	28.6	28.0
Financial account balance (excluding reserve assets)	-43.2	133.8	434.1	166.3	2.0	55.0	91.1	126.9	134.1
Direct investment	-23.8	121.7	14.3	33.4	37.8	36.6	35.4	40.1	44.5
Portfolio investment	4.5	-4.0	5.2	-3.0	-3.2	-3.4	-3.6	-3.8	-4.0
Other investment	-23.9	16.0	414.5	135.9	-32.6	21.7	59.3	90.6	93.6
Errors and omissions	148.2	162.7	-4.5	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-1.1	124.6	358.3	31.8	-38.2	-4.6	13.7	37.2	59.7
Memorandum items:									
Current account/GDP (percent)	-4.1	-7.4	-1.4	-5.3	-2.0	-2.6	-3.2	-3.1	-2.6
Goods and services balance/GDP (percent)	-15.0	-12.8	-10.3	-19.9	-15.9	-15.3	-15.7	-15.1	-14.0
Direct Investment/GDP (percent)	-0.9	4.6	0.5	1.1	1.2	1.1	1.0	1.1	1.1
Net official reserves (end of period)	240.3	363.8	721.8	735.7	680.2	674.2	603.4	627.3	674.2
In months of imports of goods and services	1.3	1.9	3.4	3.4	3.2	3.1	2.6	2.6	2.7
Total SACU Receipts	474.5	704.4	719.1	747.3	794.8	829.2	845.3	874.5	895.3

Sources: Central Bank of Swaziland; and IMF staff projections.

[1] Without corrective policy measures.

[2] SACU: Southern African Customs Union. SACU transfers in the current account does not reflect the true level of SACU revenue because of the particular treatment of those transfers in the accounts where the authorities make an estimate based on the level of imports and adjust in 'other investment' to reflect the total SACU revenues.

Table 6. Swaziland: Millennium Development Goals

	1990	1995	2000	2006
Goal 1: Eradicate extreme poverty and hunger				
Employment to population ratio, total (% of people ages 15 and over)	42	44	40	39
Employment to population ratio, total (% of people ages 15-24)	26	27	23	22
Income share held by lowest 20%	..	2.7	4.3	..
Malnutrition prevalence, weight for age (% of children under 5)	..	..	9.1	..
Poverty gap at $1 a day (PPP) (%)	..	..	..	..
Poverty headcount ratio at $1 a day (PPP) (% of population)	..	..	..	..
Poverty headcount ratio at national poverty line (% of population)	..	..	69.2	..
Prevalence of undernourishment (% of population)	14	23	..	22
Vulnerable employment, total (% of total employment)	..	21	..	..
Goal 2: Achieve universal primary education				
Literacy rate, youth female (% of females ages 15-24)	..	..	90	..
Literacy rate, youth male (% of males ages 15-24)	..	..	87	..
Persistence to last grade of prmiary, total (% of cohort)	..	..	58	71
Primary completion rate, total (% of relevant age group)	61	61	64	67
School enrollment, primary (% net)	75	..	75	78
Goal 3: Promote gender equality and empower women				
Proportion of seats held by women in national parliament (%)	4	3	3	11
Ratio of female to male enrollments in tertiary education (%)	76	..	89	98
Ratio of female to male in primary enrollment (%)	99	..	94	93
Ratio of female to male in secondary enrollment (%)	96	..	100	100
Ratio of young literate females to males (% ages 15-24)	..	..	103	..
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	..	33.2	..	..
Goal 4: Reduce child mortality				
Immunization, measles (% of children ages 12-23 months)	85	94	72	57
Mortality rate, infant (per 1,000 live births)	78	78	98	112
Mortality rate, under-5 (per 1,000)	110	110	142	164
Goal 5: Improve maternal health				
Adolescent fertility rate (births per 1,000 women ages 15-19)	..	46	41	34
Births attended by skilled health staff (% of total)	..	56	70.0	..
Contraceptive prevalence (% of women ages 15-49)	20	..	28	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	390
Pregnant women receiving prenatal care (%)	..	..	87	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases				
Children with fever receiving antimalarial drugs (% of children under age 5)	..	..	26	..
Condom use, female (% ages 15-24)	..	..	..	..
Condom use, male (% ages 15-24)	..	..	..	..
Incidence of tuberculosis (per 100,000 people)	267	337	801	1,155
Prevalence of HIV, female (% ages 15-24)	..	..	..	23
Prevalence of HIV, total (% of population ages 15-49)	..	..	..	33
Tuberculosis cases detected under DOTS (%)	..	..	33	49
Goal 7: Ensure environmental sustainability				
Annual freshwater withdrawals, total (% of internal resources)	..	..	40.1	..
CO2 emissions (kg per PPP $ of GDP)	0.2	0.1	0.3	0.2
CO2 emissions (metric tons per capita)	0.6	0.5	1.0	0.9
Forest area (% of land area)	27	..	30	31
Improved sanitation facilities (% of population with access)	..	48	48	48
Improved water source (% of population with access)	..	62	62	62
Marine protected areas, (% of surface area)	..	..	..	..
Nationally protected areas (% of total land area)	..	..	..	4
Goal 8: Develop a global partnership for development				
Aid per capita (current US$)	70	64	13	30
Debt service (PPG and IMF only, % of exports of G&S, excl. workers' remittances)	5.6	1.7	2.3	1.7
Internet users (per 1,000 people)	..	0.0	1.0	3.7
Mobile phone subscribers (per 100 people)	..	..	3.2	22.0
Telephone mainlines (per 100 people)	1.8	2.3	3.0	3.9
Other				
Fertility rate, total (births per woman)	5.3	4.9	4.1	3.5
GNI per capita, Atlas method (current US$)	1,200	1,500	1,370	2,400
GNI, Atlas method (current US$) (billions)	0.9	1.4	1.4	2.7
Gross capital formation (% of GDP)	19.1	20.0	18.6	17.2
Life expectancy at birth, total (years)	57	58	45	41
Literacy rate, adult total (% of people ages 15 and above)	..	..	80	..
Population, total (millions)	0.8	0.9	1.0	1.1
Trade (% of GDP)	161.7	168.1	178.7	167.5

Source: World Development Indicators database, June 2008

Table 7. Swaziland: External Debt Sustainability Framework, 2002-2013
(Percent of GDP, unless otherwise indicated)

	Actual					Projections							
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	Debt-stabilizing non-interest current account [6]
Baseline: External debt	29.5	22.7	18.2	17.2	16.6	**16.7**	**17.2**	**16.0**	**15.2**	**14.4**	**13.8**	**11.9**	**-1.1**
Change in external debt	7.6	-6.8	-4.5	-1.0	-0.6	0.1	0.6	-1.3	-0.8	-0.7	-0.6	-1.9	
Identified external debt-creating flows	-10.0	-20.9	-13.2	6.1	3.3	0.2	3.8	0.5	1.2	1.9	1.8	1.1	
Current account deficit, excluding interest payments	-6.2	-7.8	-4.1	3.0	6.7	0.7	4.5	1.3	1.9	2.5	2.4	1.7	
Deficit in balance of goods and services	-2.3	-2.5	1.6	15.0	12.8	9.8	19.5	15.5	14.8	15.2	14.6	12.0	
Exports	81.4	84.5	90.1	76.0	73.0	72.9	65.8	63.0	61.1	59.4	59.7	53.9	
Imports	79.1	82.0	91.7	91.0	85.7	82.7	85.3	78.5	75.8	74.6	74.4	65.9	
Net non-debt creating capital inflows (negative)	-7.5	-3.9	-3.1	0.8	-4.4	-0.6	-1.0	-1.1	-1.0	-0.9	-0.9	-0.9	
Automatic debt dynamics [1]	3.7	-9.2	-6.1	2.3	1.0	0.1	0.3	0.3	0.3	0.3	0.3	0.2	
Contribution from nominal interest rate	1.3	1.0	0.8	1.2	0.7	0.6	0.8	0.7	0.7	0.6	0.6	0.5	
Contribution from real GDP growth	-0.4	-0.7	-0.4	-0.4	-0.5	-0.5	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	
Contribution from price and exchange rate changes [2]	2.8	-9.5	-6.5	1.5	0.8	...	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets [3]	17.6	14.1	8.7	-7.1	-4.0	-0.2	-3.2	-1.8	-2.0	-2.6	-2.4	-3.0	
External debt-to-exports ratio (percent)	36.2	26.8	20.2	22.7	22.8	22.8	26.2	25.3	24.8	24.3	23.1	22.0	
Gross external financing need (in percent of GDP)[4]	-3.8	-6.0	-2.4	5.1	8.0	2.1	6.0	2.7	3.3	3.9	3.7	3.2	
Scenario with key variables at their historical averages [5]						**15.9**	**9.8**	**6.7**	**3.2**	**-1.1**	**3.2**	**3.0**	**-2.6**
Key Macroeconomic Assumptions Underlying Baseline													
Real GDP growth (percent)	1.8	3.9	2.3	2.2	2.9	3.5	2.6	2.5	2.5	2.5	2.5	2.5	
GDP deflator in US dollars (change in percent)	-11.3	47.3	40.5	-7.8	-4.4	10.7	-3.4	5.4	4.5	3.4	3.3	2.7	
Nominal external interest rate (percent)	5.5	5.2	5.1	6.2	4.2	4.2	4.6	4.5	4.5	4.4	4.4	4.2	
Growth of exports (US dollar terms, percent)	-1.0	30.0	33.8	-6.8	1.1	14.5	-10.6	3.4	3.8	3.1	6.5	6.6	
Growth of imports (US dollar terms, percent)	-13.8	29.8	40.4	9.6	-0.8	10.6	2.2	-0.7	3.5	4.2	5.6	4.7	
Current account balance, excluding interest payments	6.2	7.8	4.1	-3.0	-6.7	-0.7	-4.5	-1.3	-1.9	-2.5	-2.4	-1.7	
Net non-debt creating capital inflows	7.5	3.9	3.1	-0.8	4.4	0.6	1.0	1.1	1.0	0.9	0.9	0.9	

[1] Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

[2] The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).

[3] For projection, line includes the impact of price and exchange rate changes.

[4] Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

[5] The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

[6] Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Table 8. Swaziland: Public Sector Debt Sustainability Framework, 2002-2013
(Percent of GDP, unless otherwise indicated)

	Actual					Projections							
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	Debt-stabilizing primary balance [9]
Baseline: Public sector debt [1]	22.8	19.2	19.6	17.4	17.1	**16.5**	**15.9**	**14.7**	**13.7**	**12.9**	**12.2**	**11.6**	**0.0**
o/w foreign-currency denominated	24.2	19.9	15.9	14.7	14.5	14.5	15.4	14.2	13.3	12.5	11.8	11.3	
Change in public sector debt	-2.8	-3.6	0.5	-2.2	-0.3	-0.6	-0.6	-1.2	-0.9	-0.9	-0.7	-0.6	
Identified debt-creating flows	-6.6	-4.1	-1.3	2.2	-8.3	-9.3	-2.3	-2.9	-3.4	-3.1	-2.8	-2.4	
Primary deficit	3.0	2.0	1.6	0.7	-8.7	-8.3	-1.4	-2.1	-2.9	-2.6	-2.5	-2.5	
Revenue and grants	26.7	27.5	31.7	33.4	40.9	40.5	39.3	38.8	38.6	37.6	37.2	37.0	
Primary (noninterest) expenditure	29.8	29.5	33.3	34.1	32.2	32.2	37.9	36.6	35.7	35.0	34.8	34.5	
Automatic debt dynamics [2]	-9.6	-6.2	-2.9	1.5	0.4	-1.0	-0.9	-0.8	-0.5	-0.5	-0.3	0.1	
Contribution from interest rate/growth differential [3]	-1.2	-0.8	0.0	-0.4	-1.0	-1.0	-0.9	-0.8	-0.5	-0.5	-0.3	0.1	
Of which contribution from real interest rate	-0.8	0.0	0.5	0.0	-0.6	-0.4	-0.5	-0.4	-0.2	-0.2	0.0	0.4	
Of which contribution from real GDP growth	-0.4	-0.8	-0.4	-0.4	-0.4	-0.5	-0.4	-0.4	-0.3	-0.3	-0.3	-0.3	
Contribution from exchange rate depreciation [4]	-8.4	-5.3	-3.0	1.9	1.4	...	...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [5]	3.8	0.5	1.8	-4.4	8.0	8.7	1.7	1.7	2.4	2.2	2.1	1.8	
Public sector debt-to-revenue ratio [1]	85.2	69.7	61.8	52.2	41.8	40.8	40.4	37.8	35.5	34.2	32.7	31.3	
Gross financing need (percent of GDP) [6]	5.8	3.7	5.5	2.7	-10.2	-5.8	-1.0	-1.4	-1.5	-1.1	-1.1	-1.3	
Scenario with key variables at their historical averages [7]						**24.9**	**26.4**	**27.0**	**28.2**	**29.3**	**30.3**	**31.2**	**-0.7**
Scenario with no policy change (constant primary balance) in 2007-2012						**16.5**	**11.4**	**5.0**	**-1.5**	**-6.9**	**-12.2**	**12.8**	**0.0**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline													
Real GDP growth (in percent)	1.8	3.9	2.3	2.2	2.9	3.5	2.6	2.5	2.5	2.5	2.5	2.5	
Average nominal interest rate on public debt (in percent) [8]	5.2	6.0	7.2	6.7	6.1	6.4	6.3	5.6	5.4	5.4	5.4	8.0	
Average real interest rate (nominal rate minus change in GDP deflator, percent)	-3.3	0.1	2.6	0.1	-3.3	-2.5	-2.9	-2.5	-1.1	-1.1	0.0	3.2	
Nominal appreciation (increase in US dollar value of local currency, percent)	40.4	30.1	17.9	-11.0	-9.3	...	...	...	...	...	...	...	
Inflation rate (GDP deflator, percent)	8.5	5.9	4.6	6.6	9.5	9.0	9.2	8.1	6.5	6.6	5.4	4.8	
Growth of real primary spending (deflated by GDP deflator, percent)	6.0	3.0	15.5	4.3	-2.8	3.5	20.9	-1.0	0.1	0.3	1.9	1.8	
Primary deficit	3.0	2.0	1.6	0.7	-8.7	-8.3	-1.4	-2.1	-2.9	-2.6	-2.5	-2.5	

1 Gross debt of the general government.

2 Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3 The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as -g.

4 The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.

5 For projections, this line includes exchange rate changes.

6 Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

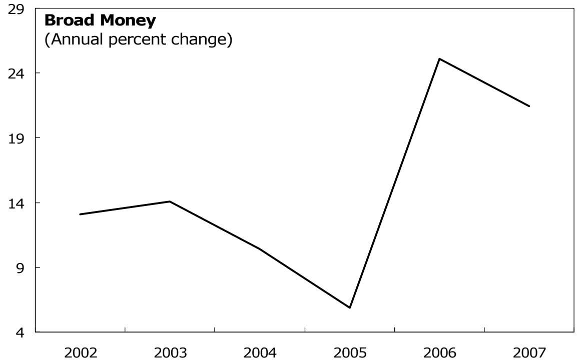
7 The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8 Derived as nominal interest expenditure divided by previous period debt stock.

9 Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

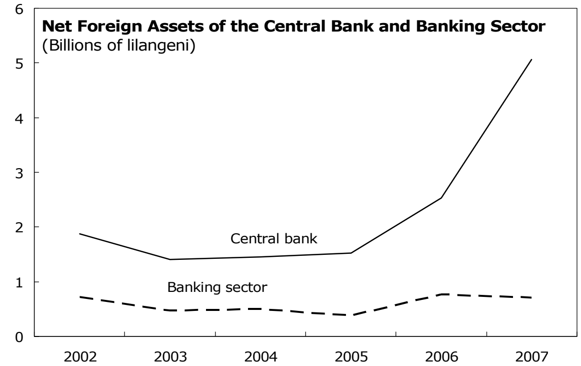
Figure 2. Swaziland: Monetary and Financial Developments

Broad money continues to grow...



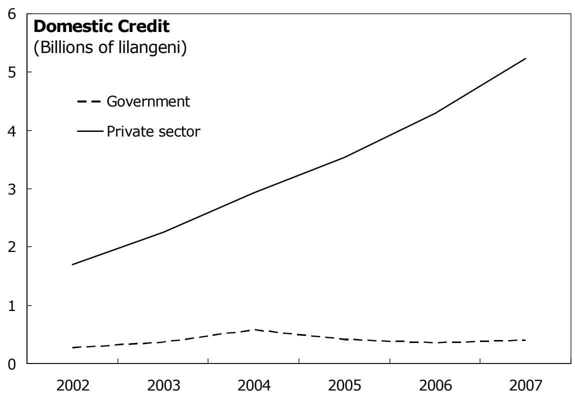
Sources: National authorities and IMF staff projections.

...and net foreign assets of the Central Bank increased.



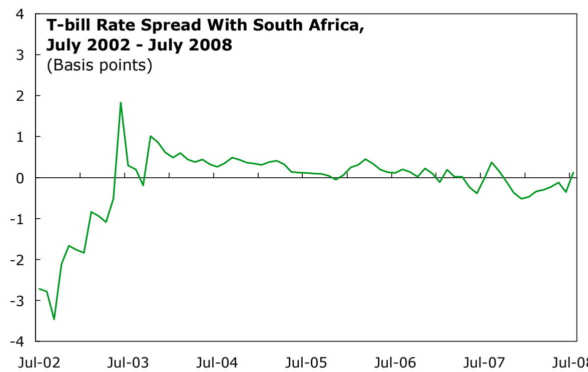
Sources: National authorities and IMF staff projections.

The decline in government borrowing has given way to expanded credit to the private sector ...



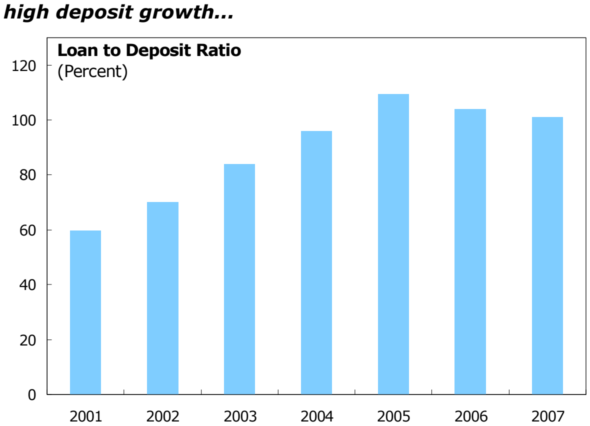
Sources: National authorities and IMF staff projections.

..and the T-bill rate is broadly in line with South Africa.



Sources: National authorities and IMF staff projections.

The loan to deposit ratio has leveled off on account of high deposit growth...



Sources: National authorities and IMF staff projections.

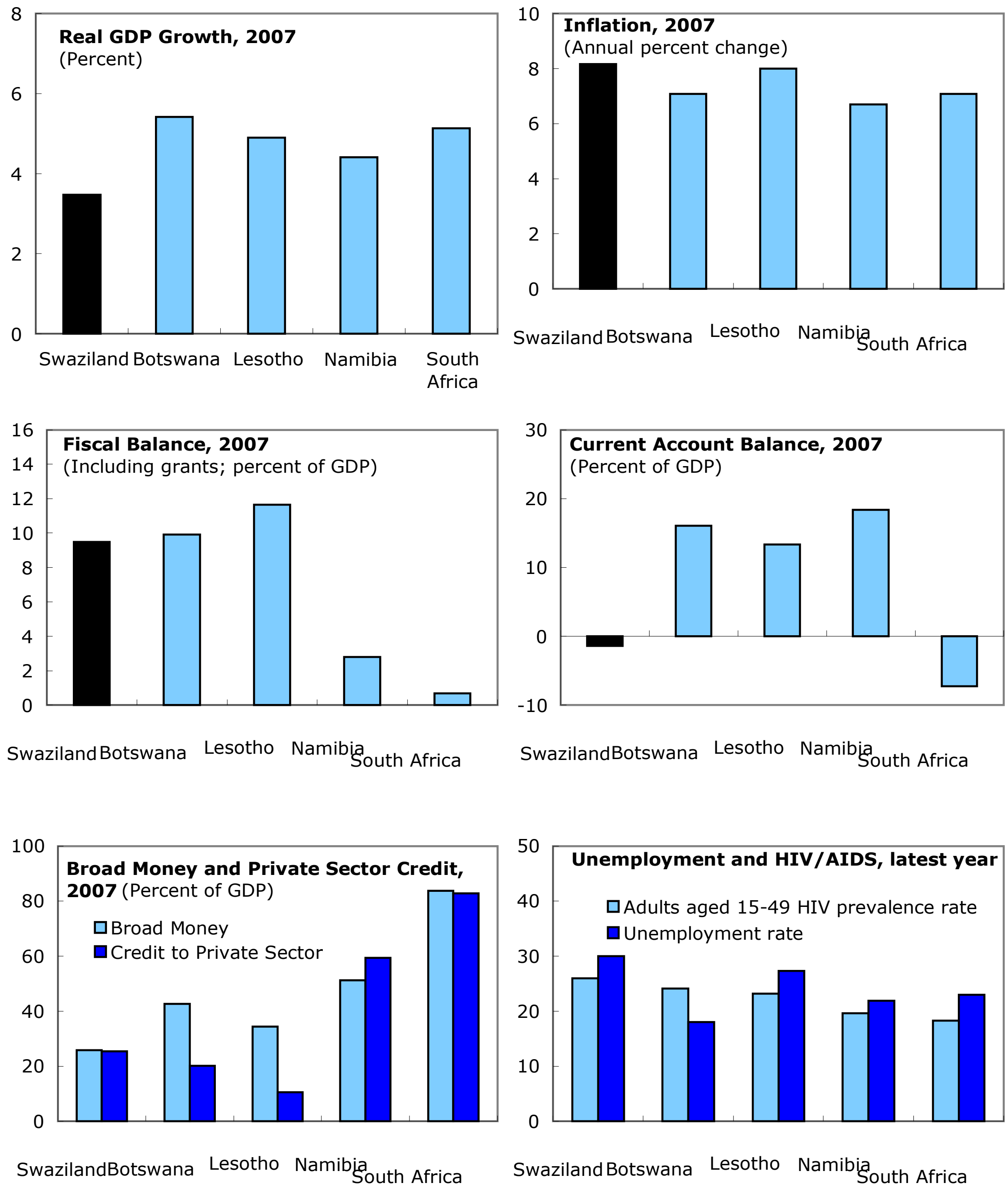
...while financial markets continue to be shallow.

Comparative Monetary Indicators, 2007

	Percent of GDP	
	Broad Money	Private Sector Credit
Swaziland	25.9	25.4
Lesotho	34.3	10.5
Botswana	42.7	20.2
Namibia	51.3	59.4
South Africa	83.7	82.8

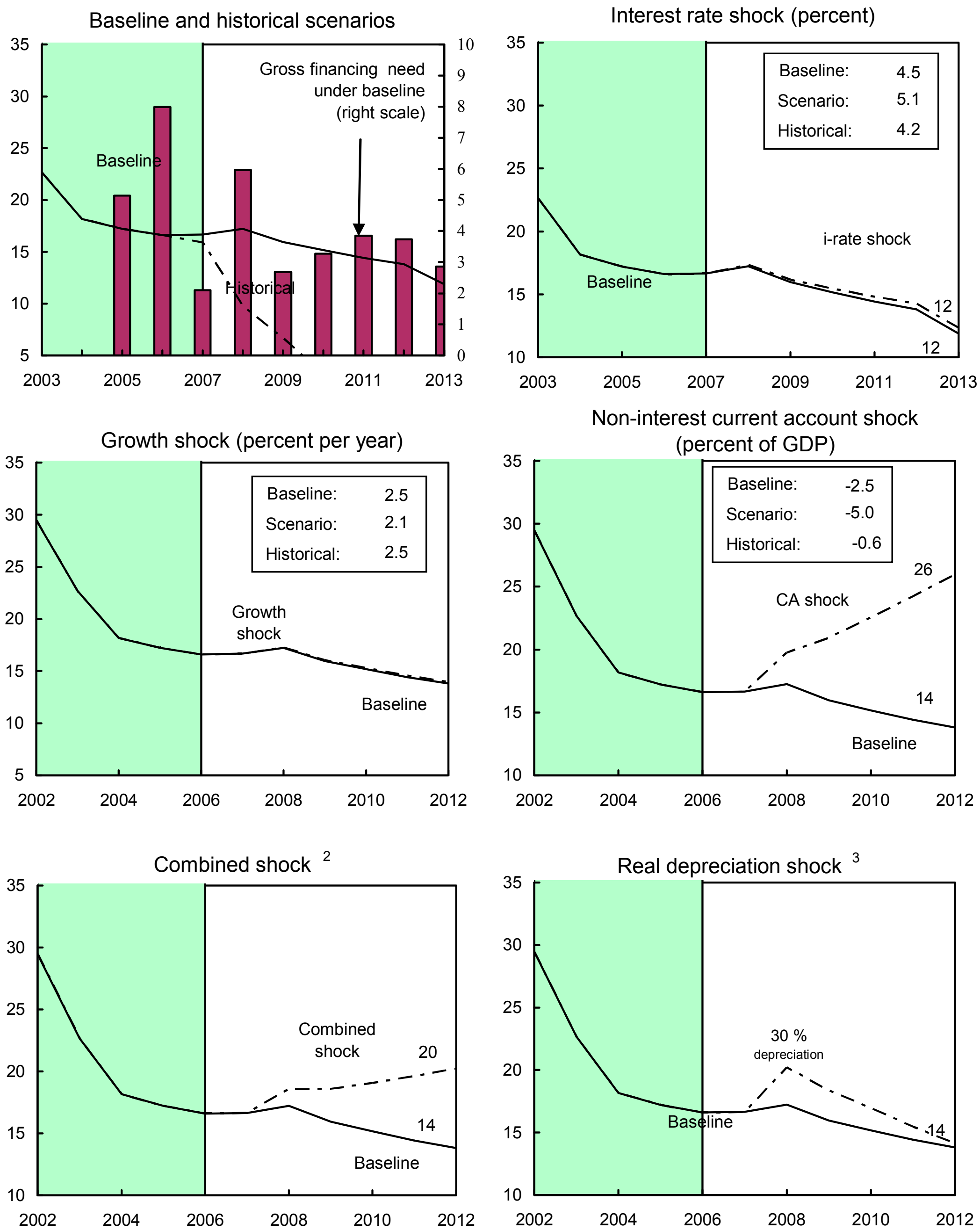
Sources: IFS and WEO.

Figure 3. Swaziland: Regional Comparison



Source: World Economic Outlook and International Financial Statistics.

Figure 4.Swaziland: External Debt Sustainability: Bound Tests [1]
(External debt in percent of GDP)



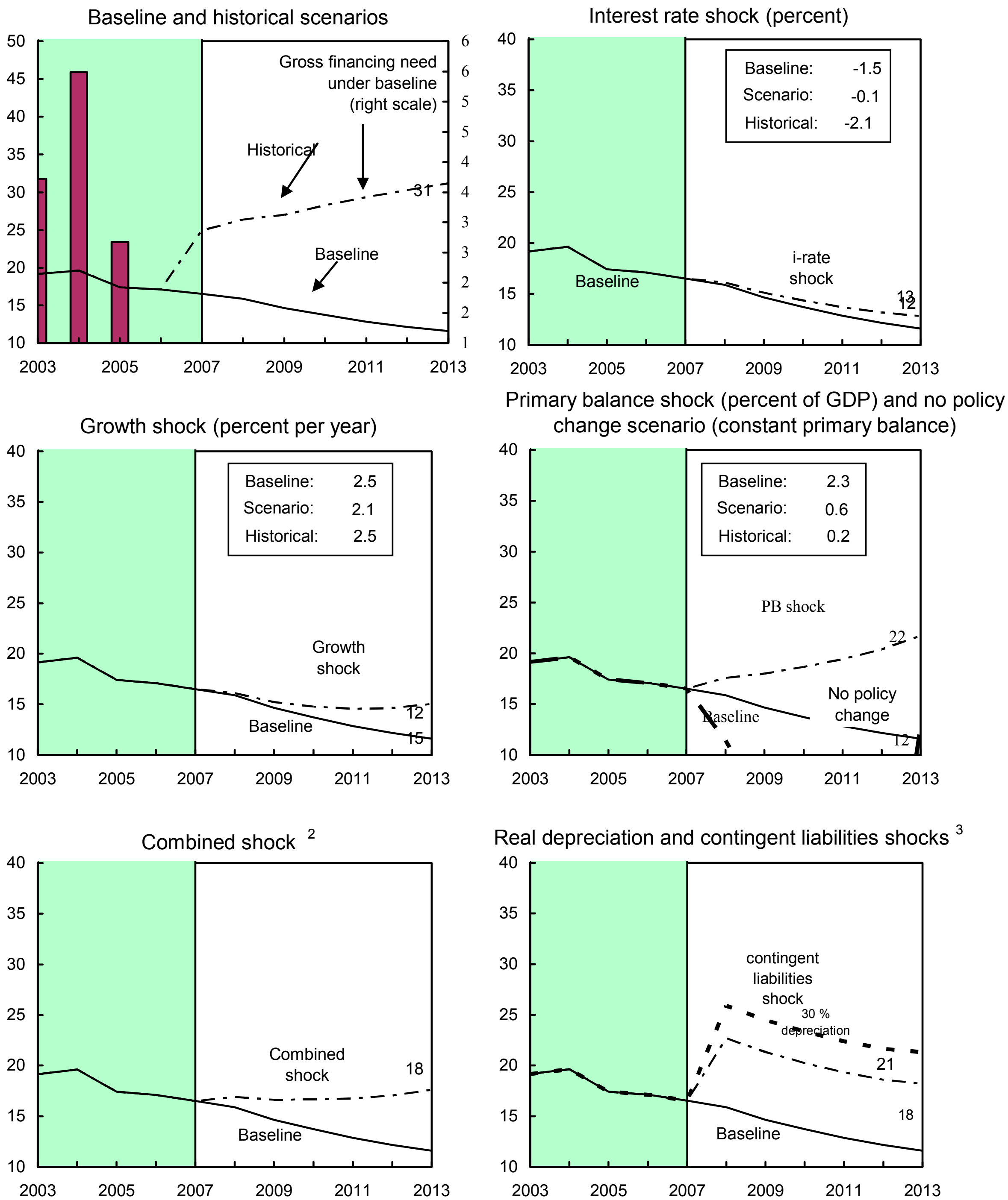
Sources: International Monetary Fund, Country desk data, and staff estimates.

[1] Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

[2] Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

[3] One-time real depreciation of 30 percent occurs in 2008.

. Figure 5:Swaziland: Public Debt Sustainability: Bound Tests [1]



Sources: International Monetary Fund, country desk data, and staff estimates.

[1] Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

[2] Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

[3] One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2008, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

INTERNATIONAL MONETARY FUND

KINGDOM OF SWAZILAND

Staff Report for the 2008 Article IV Consultation—Informational Annex

Prepared by the staff representatives for the
2008 Consultation with the Kingdom of Swaziland

Approved by Anne-Marie Gulde-Wolf and Anthony Boote

October 1, 2008

- **I. Relations with the Fund.** Describes financial and technical assistance by the IMF and provides information on the exchange rate system.
- **II. The JMAP Bank-Fund**. Describes the priorities and main activities of the World Bank Group and the IMF, and areas of cooperation in their work with the authorities of Swaziland.
- **III. Statistical Issues.** Assesses the quality of statistical data. Weaknesses in several categories of economic statistics are hampering analyses of economic developments.
- **IV. Social and Demographic Indicators**.

Contents Page

I. SWAZILAND: RELATIONS WITH THE FUND

(As of August 31, 2008)

I. **Membership Status:** Joined September 22, 1969; Accepted the obligations of Article VIII, sections 2, 3 & 4: December 11, 1989.

II. **General Resources Account:**	SDR Million	% Quota
Quota	50.70	100.0
Fund holdings of currency	44.15	87.1
Reserve position in Fund	6.56	12.9

III. **SDR Department:**	SDR Million	% Allocation
Net cumulative allocation	6.43	100.0
Holdings	2.55	39.6

IV. **Outstanding Purchases and Loans:** None

V. **Financial Arrangements:** None

VI. **Projected Payments to the Fund:**
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming			
	2008	2009	2010	2011
Principal				
Charges/Interest	0.03	0.12	0.12	0.12
Total	0.03	0.12	0.12	0.12

VII. **Implementation of HIPC Initiative**: Not applicable

VIII. **Exchange Rate Arrangement**

The Lilangeni (plural: Emalangeni) continues to be pegged at parity to the South African rand, which—alongside with the Lilangeni—is also legal tender. The intervention currency is the U.S. dollar; exchange rates for the U.S. dollar are based on the floating middle rate of the South African rand against the U.S. dollar. The rate on August 31, 2008 was E1 = US$0.1301185

Swaziland has accepted the obligations of Article VIII, Sections 2–4; it maintains two exchange restrictions arising from limits on the provision of foreign exchange for advance payments for imports: (i) an overall limit of E 250,000, and (ii) a 33.33 percent limit for the import of certain capital goods. The Swazi lilangeni is pegged at par with the South African rand, which is also legal tender.

IX. Article IV Consultation

Swaziland is on the standard 12-month cycle. The last Article IV consultation discussions were held in Mbabane in November 2007. The staff report (IMF Country Report No. 08/85, March 2008) was considered by the Executive Board on January 23, 2008.

X. Technical Assistance

FAD

Dates	*Purpose*
1997	Tax reform
1999	Review a new income tax bill
March 2007	Revenue administration and Revenue Authority

LEG

Dates	*Purpose*
1998	Draft a new income tax bill and amendments to the Sales Tax Act
April 2007	Exchange Control Regulations
December 2007	Follow up on AML/CFT

LEG/MCM (MFD)

Dates	*Purpose*
November 2004	AML/CFT
May 2004	Legislative drafting /FIU

MCM (MFD)

Dates	*Purpose*
1997	Drafting of the Financial Institutions Act
1998-2000	Bank supervision
February 2003	Strengthening the CBS and the financial system, monetary and foreign exchange operations, development of the government securities market, the payment system, and banking supervision
July 2003	Development of the government securities market, and the strengthening monetary and foreign exchange operations
July 2004	A workshop for Senior Bank Supervisors in East and Central Africa
July 2004	Financial Sector Reform and Strengthening, including nonbank financial institutions. Under FIRST
January 2005	Foreign exchange operations and foreign exchange reserves management
Oct. 2005–April 2006	Reserves management
November 2005	Central bank accounting, central bank organization and financial sector supervision
April 2007	Supervision of saving and credit cooperatives
August 2007	Bank supervision, follow-up

September 2007	Supervision of insurance companies and pension funds
March 2008	Supervision of insurance companies and pension funds
April 2008	Central bank accounting, central bank organization and financial sector supervision

STA

Dates	*Purpose*
1998	Multisector mission to assess statistics system
April 1999	Balance of payments statistics
April 1999	Government finance statistics
July 2002	Participation of GDDS
June 2003	Government finance statistics
October 2003	Balance of payments statistics/GDDS Project for Anglophone Africa
October 2003	Government Finance Statistics/GDDS Project for Anglophone Africa
June 2004	Government Finance Statistics/GDDS Project for Anglophone Africa
July 2004	National Accounts Statistics/GDDS Project for Anglophone Africa
October 2004	Consumer Prices Index/GDDS Project for Anglophone Africa
November 2004	Monetary Statistics/GDDS Project for Anglophone Africa
January 2005	Consumer Prices Index/GDDS Project for Anglophone Africa
April 2005	National accounts statistics/GDDS Project for Anglophone Africa
May 2005	Balance of payments statistics/GDDS Project for Anglophone Africa
May 2005	Consumer Prices Index/GDDS Project for Anglophone Africa
September 2005	Consumer Prices Index/GDDS Project for Anglophone Africa
October 2005	Balance of payments statistics/GDDS Project for Anglophone Africa
November 2005	Government Finance Statistics/GDDS Project for Anglophone Africa
October 2006	National accounts statistics/GDDS Project for Anglophone Africa
March 2006	Balance of payments statistics/GDDS Project for Anglophone Africa
March 2006	Consumer Prices Index/GDDS Project for Anglophone Africa
March 2006	Monetary Statistics/GDDS Project for Anglophone Africa
July 2006	Consumer Prices Index/GDDS Project for Anglophone Africa
November 2006	Balance of payments statistics and External Debt/GDDS Project for Anglophone Africa
June 2007	Consumer Prices Index
August 2007	National accounts statistics/GDDS Project for Anglophone Africa
November 2007	Monetary Statistics/GDDS Project for Anglophone Africa
July 2008	Government Finance Statistics/GDDS Project for Anglophone Africa

II. Swaziland: The Joint Management Action Plan Bank–Fund

(As of September 9, 2008)

	Product	Provisional Timing of missions	Expected Delivery date
A. Mutual information on relevant work programs			
The World Bank work program in the next 12 months	Local Government Project HIV/AIDS project Post-Basic Education and Training Sector Study Civil Service Pension Reform TA Investment Climate Assessment Follow-up TA Fiduciary Assessment Institutional Assessment of PFM/GAC ESW Debt management TA Strengthening PEM –IDF grant (on-going) Disaster Risk Reduction and Recovery (focus on agriculture sector growth)-TA		Q3 of FY09 Q3-Q4 of FY09 July 2008 Q4 of FY09 Q4 of FY09 Q4 of FY09 FY09 FY09 FY10 FY09
The Fund work program in the next 12 months	AFR: 2008 Article IV Consultation [including Financial Sector Strategy Note] Selected Issues Paper—The role of Non-Bank Institutions in SACU countries Technical assistance: FY2008/09 Financial sector * Supervision of insurance and retirement fund * Bank and non-bank supervision * Multi sector mission Statistics * Government finance statistics * Multi sector mission—financial, national accounts, GFS and BOP	 July 23-August 5 2008 October 2008 4 missions 1 mission 1 mission July 2008 1 mission	 Board meeting plan for October 2008 As part of the 2008 Article IV Staff report
B. Requests for work program inputs (as needed)			
Fund request to Bank	Growth diagnostic and assessment of competitiveness Governance and PEM Assisting the authorities with food strategy and scaling up agricultural yield.		
Bank request to Fund	Periodic macro updates Possibly collaboration in responding to increasing food prices/food security		
C. Agreements on joint products and missions			
Joint products in next 12 months	Bank staff participated in the 2008 Article IV Consultation mission.	July, 2008	

III. SWAZILAND: STATISTICAL ISSUES

Data provision has some shortcomings, but is broadly adequate for surveillance. Staff's analysis was affected by shortcomings in certain areas, including the national accounts and the external sector. The authorities provide available data to the Fund with a lag of one to two months, except for the national accounts and international trade data, which are reported irregularly.

GDDS metadata were posted on the Fund's Dissemination Standards Bulletin Board on February 11, 2003. The metadata for all sectors—except the financial sector—were updated in October 2005, subsequently the financial sector metadata were updated in October 2007. Swaziland has undertaken to use the GDDS as a framework for the development of its national statistical system and participates in the GDDS Project for Anglophone African Countries. Under this project (funded by the U.K. Department for International Development (DFID)), the country participates in the national accounts and the monetary and financial statistics modules with the Fund, and in the labor statistics and agricultural statistics with the World Bank. Swaziland's Central Statistical Office has a webpage (http://www.gov.sz/home.asp?pid=75) that needs updating.

Real sector statistics
STA GDDS missions have resulted in significant improvements in the national accounts. Current and constant price (base=2000) GDP estimates are now available from both the production and expenditure approaches. These new estimates have not yet been published, as there are still some shortcomings concerning the treatment of Southern African Customs Union revenue. For national accounts data, AFR missions rely on estimates provided by the Central Statistical Office (CSO). The authorities are planning the first labor force survey with support from the World Bank/GDDS project.

Price statistics
The consumer price index was significantly revised in May 2007 with technical assistance provided in the context of the GDDS initiative. The dissemination of the new consumer price index is a significant milestone for the CSO. Four new geographical indices, as well as a national index, with updated market basket weights, are now available. These new consumer price indices incorporate improvements in compilation methodology, market basket coverage, flexibility for introducing new pricing outlets and new varieties of products, and enhanced processing capabilities. Monthly consumer price data are published by the CSO with a one-month lag. For *International Financial Statistics (IFS)* purposes, the consumer price index is reported at the national level for the all-income group.

Government finance statistics
Fiscal data are provided to AFR staff only during missions and/or following budget announcements. The Central Bank of Swaziland (CBS) reports fiscal data on central government operations to STA for publication in *IFS and the GFS Yearbook* on an irregular basis and with significant lags–the latest data are for 2003. Data on transactions in financial assets and liabilities are not reported. A June 2003 mission reviewed government finance

statistics (GFS) compilation and introduced the *GFSM 2001* framework. An October 2003 mission made recommendations to improve the coverage, classification and consistency of fiscal statistics. A June GFS 2004 mission further developed the bridge tables and derivation tables used to compile GFS, assisted in the reconciliation of the fiscal and monetary accounts, and made recommendations concerning these topics, as well as the extra budgetary accounts, the Ministry of Finance Economic Classification Spreadsheet, budget classification, and data dissemination. A mission in July 2008 found that resources assigned to GFS are extremely limited and that differences in institutional coverage largely explain the large discrepancies between operations and financing data. The mission recommended the elaboration of standardized GFS reports directly from the accounting system.

Monetary and financial statistics
The CBS uses the standardized forms to report monthly monetary and financial statistics to STA, and data are reported on a timely basis. The 2006 MFS mission noted that substantial improvements were achieved, particularly in the data for the CBS. The mission found that, some progress had been made in the reporting of data on the other depository corporations (ODCs), but quality problems remained. The majority of the ODCs reported various degrees of difficulty in providing accurate data to the CBS. The mission recommended that the CBS arrange regular meetings with the ODCs to promote improved classification and sectorization. The CBS started to include the Swaziland Building Society into the monetary data backdated to December 2006. However, the credit and savings cooperatives, representing about 8 percent of the deposits of the commercial banks, are still outside the deposit corporations' survey. A recent MFS mission discussed the proper treatment of pension funds and insurance companies in the financial survey.

Balance of payments statistics
The CSO publishes data on foreign trade on a quarterly basis, but the lack of sufficient computer resources results in long lags in the production of trade data, especially regarding imports. AFR missions use trade data provided by the CBS. The CBS publishes balance of payments statistics on a semiannual and annual basis. It now adheres to a methodology consistent with the fifth edition of the *Balance of Payments Manual*. Shortcomings in the timeliness and availability of data need to be addressed.

SWAZILAND: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

(AS OF SEPTEMBER 16, 2008)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	Aug 08	Sept 08	M	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Dec 07	May 08	M	M	M
Reserve/Base Money	Jul 08	Sept 08	M	M	M
Broad Money	Jul 08	Sept 08	M	M	M
Central Bank Balance Sheet	Jul 08	Sept 08	M	M	M
Consolidated Balance Sheet of the Banking System	Jul 08	Sept 08	M	M	M
Interest Rates[2]	Jul 08	Aug 08	M	M	D
Consumer Price Index	Jul 08	Aug 08	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2007	Jun 08	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2007	Jun 08	A	A	A
External Current Account Balance	2007	Jun 08	A	A	A
Exports and Imports of Goods and Services	2007	Jun 08	Q	A	A
GDP/GNP	2007	Jun 08	A	A 2/ 3/	A
Gross External Debt	2007	Jun 08	A	A	A
International Investment Position[6]	2006	Oct 07			

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D), weekly (W), monthly (M), quarterly (Q), annually (A), irregular (I); and not available (NA).

IV. SWAZILAND: SOCIAL AND DEMOGRAPHIC INDICATORS

Area (sq. km.)	17,364	**Population Density** (per sq. km)	65.47
Population	1.1 million		
Population		**Health**	
Population growth rate	1.7	Population per physician (2000)	5,675
Life expectancy at birth (2005)	41.5 yrs	Public health expenditure (2004,	4.02
Infant mortality rate (per thousand)	110	(percent of GDP)	
Urban Population (% total)	24.38	HIV prevalence rate (ages 15-49)	25.9
Population younger than 15	.		
(percent of total population)			
GDP per capita (US dollars)	2,312	**Education**	
Access to safe water (2004)		Adult literacy rate (2002, percent)	80.9
Percent of total population	62	Primary school enrollment	80
Urban	87	(2005, net, percent)	
Rural	54		
		Poverty Indicators (2001)	
Labor Statistics (thousands)			
		Share of income, lowest 20 percent	4.34
Labor Force	338	(percent)	
		GINI Index	50.4
Formal Employment (2005)	92		
Private Sector	65		
Public Sector	28		

Sources: *International Financial Statistics;* World Bank, *World Development Indicators, April 2006*, UNAIDS, 2006, *2006 Report on the Global Aids Epidemic*; and national authorities. Data refer to 2006, unless otherwise indicated.

Swaziland: Tentative Work Program

Discussions for the 2009 Article IV consultation	July 23–August 5, 2009
Board meeting on the 2009 Article IV consultation	October 16, 2009

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 08/138
FOR IMMEDIATE RELEASE
October 27, 2008

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2008 Article IV Consultation with the Kingdom of Swaziland

On October 17, 2008, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Kingdom of Swaziland.[1]

Background

Growth recovered moderately in 2007 to 3.5 percent, but inflation escalated into double digits—initially owing to high food and fuel prices. Sustained high rates of economic growth remain elusive, clouded by low investment climate, the slow pace of economic reforms, deterioration of preferential treatment of Swaziland's main exports, and arising financial sector vulnerabilities. The years of persistently low growth have led to high unemployment and rising poverty; a situation made worse by the high prevalence of HIV/AIDS that suppresses productivity.

High Southern African Customs Union (SACU) revenue contributed to the second consecutive budget surplus −-despite expanded public expenditure, an improved current account and a build-up of international reserves to a comfortable level. The recent depreciation of the nominal exchange rate along with the South African rand, to which it is pegged, impacted positively on the export sector.

Swaziland's inflation rate increased from 9.8 percent at end 2007 to 13.4 percent end-July 2008, reflecting rising food and fuel prices. To mitigate the surge on commodity prices, the

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

government uses a delayed-pass-through policy for some items. Interest rates generally have risen in line with developments in South Africa but the authorities decided in June 2008 not to match the latest 50 basis point increase by the South African Reserve Bank (SARB)

The outlook is subject to several risks: high dependence on SACU revenues, which is unlikely to be sustained; uncertainties about the viability and timing of investment projects; low competitiveness sores; an investment climate that keeps the cost of doing business high; the prevalence of HIV/AIDS; the external environment and emerging financial sector vulnerabilities.

Executive Board Assessment

Executive Directors welcomed the strengthening of Swaziland's current account balance and external reserve position in 2007. At the same time, Directors noted that Swaziland's economic growth is low by regional standards, and that poverty and social indicators remain weak. Fuel and food price shocks have also increased inflationary pressures. Directors cautioned that the global financial turmoil could add to the downside risks and the challenges posed by an HIV/AIDS epidemic and the erosion of trade preferences. Therefore, they recommended continued pursuit of sound macroeconomic policies and determined implementation of structural reforms to stimulate private sector development.

Directors commended the government's achievement of budget surpluses in 2006 and 2007. They urged continued fiscal restraint in 2008 and beyond to ensure medium-term fiscal sustainability in light of the projected decline in revenue from the Southern African Customs Union (SACU), on which the budget is heavily dependent. They welcomed the authorities' intention to save windfall SACU revenues in 2008. Directors encouraged the authorities to press ahead with revenue and expenditure reforms to achieve a sustainable non-SACU fiscal position.

Directors supported the authorities' efforts to broaden the tax base and improve tax administration, in particular through the introduction of a value added tax and the establishment of a Revenue Authority. They stressed the importance of strengthening public expenditure management and re-orienting public spending toward infrastructure and priority social sectors. The on-going enhancements to the procurement system and the forthcoming reform of the Public Finance Management Act were also viewed as crucial. Directors emphasized the need for civil service reform to lower the relatively high government wage bill and achieve better service delivery.

Directors agreed that Swaziland's membership in the Common Monetary Area and the currency peg to the South African rand continue to serve the country well. They supported the build-up of international reserves to maintain confidence in the peg. They noted the staff's assessment that the real effective exchange rate is broadly adequate at present. To improve growth prospects and compensate for eroding trade preferences, Directors encouraged the authorities to accelerate structural reforms.

Directors observed that, notwithstanding limited monetary independence and historical practice, the Central Bank of Swaziland decided in June 2008 not to increase its policy rate to match the increase in the repo rate of the South African Reserve Bank. They encouraged the Central Bank of Swaziland to monitor closely developments in inflation and capital flows, and to stand ready to adjust its policy rate as needed with a view to keeping it as close as possible to the repo rate of the South African Reserve Bank.

Directors observed that the banking sector remains well-capitalized, liquid, and profitable, with low non-performing loans. They welcomed the authorities' decision to privatize the government-owned bank. However, Directors considered the recent growth of non-bank financial institutions, with inadequate regulation and supervision, to be a cause for concern. They stressed that tighter supervision of savings and credit cooperatives is a priority for preserving financial stability. In this connection, they urged timely passage of pending financial legislation and early implementation of the Financial Service and Regulatory Authority. The emergence of pyramid schemes calls for swift and decisive actions, as such schemes pose additional risks to financial stability. Directors also encouraged increased cross-border collaboration among regional supervisory agencies. Most Directors encouraged the authorities to reconsider the requirement that insurance and pension funds invest a portion of their assets locally, noting that it could reduce return on these funds.

Directors believed that the Poverty Reduction Strategy and Action Plan approved last year provides a sound basis for reducing poverty, and advised that its implementation and monitoring strategies be clarified. They welcomed the recently-adopted measures to improve the investment climate and to minimize the impact of the erosion of trade preferences, particularly those to reduce corruption and improve governance, and encouraged further progress.

Directors welcomed the authorities' response to food and fuel price shocks. They recommended that measures to alleviate the impact of high food and fuel prices focus on the most vulnerable population and effectively utilize existing distribution channels to deliver assistance. Prompt and automatic pass-through of international price increases would also help depoliticize price adjustments.

A few Directors supported a review of Swaziland's classification as a lower middle-income country, in light of the country's weak social indicators.

Swaziland: Selected Economic and Financial Indicators, 2003-2008

	2003	2004	2005	2006	2007 Est.	2008 Proj
Domestic economy						
Real GDP	3.9	2.5	2.2	2.9	3.5	2.6
Consumer price inflation (period average)	7.4	3.4	4.8	5.3	8.2	12.7
Consumer price inflation (end of period)	4.6	3.2	6.3	5.5	9.8	13.5
External economy	(In millions of U.S. dollars, unless otherwise indicated)					
Exports, f.o.b.	1,387	1,809	1,636	1,664	1,767	1,681
Imports, f.o.b.	-1,283	-1,718	-1,894	-1,916	-2,013	-2,254
Current account balance 1/	124	71	-103	-197	-41	-158
(In percent of GDP)	6.8	3.1	-4.1	-7.4	-1.4	-5.3
Gross official international reserves	265	262	244	367	747	681
(In months of imports of goods and nonfactor services)	2.1	1.5	1.3	1.9	3.6	3.2
Debt service (in percent of exports of goods and nonfactor services)	1.1	1.0	1.0	1.1	1.1	1.3
Financial variables	(In percent of GDP, unless otherwise indicated)					
Total government revenue and grants 2/	27.9	32.1	33.2	43.0	39.7	39.0
Total government expenditure and net lending 2/	30.8	36.9	34.8	32.5	33.3	37.2
Overall government balance (incl. grants) 2/	-2.9	-4.7	-1.6	10.5	6.4	1.7
Change in broad money (in percent)	14.1	10.4	5.9	25.1	21.4	...
Interest rates (in percent) 3/	4.2	4.1	3.5	8.5	10.0	...
Discount rate (in percent)	8.0	7.5	7.5	9.0	11.0	...

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 Samuel Itam, Alternate Executive Director for the Kingdom of Swaziland and Rachel Kemunto Gesami, Advisor to Executive Director
October 17, 2008

1. My authorities wish to acknowledge the Fund's engagement, support, and productive dialogue. They thank the staff for the well-balanced set of reports, which clearly identifies the challenges for their country's development process, as well as the various policy options for medium to long term. We are in broad agreement with the thrust of the analyses, conclusions, and recommendations in the reports.

Recent Economic Developments

2. Swaziland's economic performance has been positive in several areas since the recovery from the 2006 drought, but overall performance has remained below the levels attained in other lower middle-income countries. The modest rebound in GDP growth of 3.5 percent in 2007 has been difficult to sustain because of several external shocks, including the rise of food and fuel prices, and the restrictions on export outlets for sugar and textiles following the end of the Multi-Fibre Agreement. Inflation, estimated to have increased to an annual average of 8.3 percent in 2007 because of rising food and oil prices, has accelerated. However, the budget recorded a second consecutive surplus (6.4 percent of GDP) and international reserves rose to the equivalent of 3.5 months of imports in 2007 on the strength of higher SACU receipts. The Central Bank of Swaziland (CBS) has tightened its monetary policy stance by increasing its discount rate and the issuance of securities. Although the banking sector has been adequately supervised, supervision of the savings and credit cooperative sector has had to be enhanced by the monetary authority. Further, the authorities have begun the process of privatizing the government owned commercial bank. They are also working towards deepening the financial sector and strengthening its institutional and legal structure to enhance resource allocation and provide a safeguard for its operation.

3. Swaziland has been facing uncertainties and difficulties in attracting foreign direct investments. Low competitiveness scores, an investment climate that keeps the cost of doing business high, the prevalence of HIV/AIDS and other social challenges remain daunting for the authorities. These adverse factors, together with the current surges in food and fuel prices, have aggravated the unemployment situation and poverty. The classification of Swaziland as a lower middle-income country has added another dimension that has contributed to denying the country concessional resources to fight HIV/AIDS and reduce poverty.

4. These challenges notwithstanding, the authorities have embarked on a number of economic and structural reforms aimed at enhancing economic growth to levels comparable to those achieved by other countries in the region. They are fully aware that the process of reform implementation requires them to be resolute.

Fiscal Developments

5. The authorities recognize the importance of pursuing a prudent fiscal policy as the main instrument to restoring macroeconomic stability and engendering satisfactory economic growth. Increased pro-poor fiscal outlays in 2008/2009 have been made to address the problems of the HIV/AIDS pandemic, worsening social indicators, and deepening poverty. The authorities have, however, taken steps to reduce other expenditures in 2008/09, with further adjustments to come in 2009/2010. In order to better manage public expenditures, the government is highlighting improvement of the procurement system, reform of Public Finance Management Act, and support for the reform of public enterprises. They also plan to assess expenditure and budget allocation based on social rate of return and government priorities in social services consistent with the Poverty Reduction Strategy and Action Program (PRSAP).

6. The authorities plan to focus on reducing the fiscal deficit, excluding SACU revenues, and increasing domestic revenues over the medium term. This approach would help the adjustment needed to ensure fiscal sustainability and smooth expenditure over the medium term. Operationalizing the Revenue Authority Act will introduce the requisite institutional framework and facilitate improvements in revenue collection. In addition, the authorities intend to strengthen revenue administration with the introduction of VAT.

7. The authorities are committed to implement civil service reforms, including reduction in the wage bill and implementation of performance contracts. They, however, are aware of the difficulties involved, including the predicament of right-sizing the civil service in a relatively weak economic environment and high unemployment. Of particular challenge is developing the appropriate safety nets to mitigate the adverse effects of the envisaged civil service right-sizing.

8. The authorities intend to continue with reorienting expenditure toward priority sectors in order to enhance economic growth and reduce widespread poverty. In this regard, further efforts are needed to ensure that the framework for macroeconomic stability is consistent with the PRSAP. They recognize the increasing challenges, especially in the medium to long term, of meeting the health and education needs of its youthful population. In an effort to revitalize the health sector, they have embarked on a comprehensive review to begin a process of zero-based budgeting for the sector.

Response to the Food and Fuel Price Increases

9. The authorities are committed to dealing with the high food and fuel prices, focusing on fiscal viability, minimization of market distortions, and effective delivery of essential services and support to the most vulnerable groups. They plan to discourage general subsidies and undue delay in passing through of price increases. The National Disaster Management Agency will be working on improving coordination among all stakeholders.

Monetary and Exchange Rate Developments and Financial Sector Reform

10. The Swazi authorities consider the regime of the Common Monetary Authority (CMA), including the peg to the rand, as having served the country well and remaining appropriate. Going forward, the authorities plan to maintain a tight monetary stance in order to address the second round effects of food and fuel price increases. They are also committed to strengthening the financial sector. In this regard, the central bank is pressing for a timely compliance of all banks with prudential regulations, further improvement of the supervision of Savings and Credit Cooperatives (SCCOs), comprehensive address of pyramid schemes through better coordination among domestic and regional financial regulators, improved internal processes for dealing with fraudulent operations, and laws prohibiting pyramid operations. Also, the authorities are seeking an early passage of the Financial Services and Regulatory Authority Bill. In addition, the authorities are further reviewing its legal structure and modernizing its operations with Fund support in a number of areas, including strengthening reserve management, dealing with anti-money laundering and strengthening banking supervision.

11. Banking soundness indicators are positive with well-capitalized, liquid, profitable and low nonperforming loans. However, the government-owned Swazi Bank continues to have relatively high nonperforming loans and faces difficulties meeting compliance requirements. A few major SCCOs also face severe financial difficulties. Notable progress has been made in establishing a framework for regulation and supervision of banks as well as insurance and pension funds. New regulations have been introduced that require all insurance and pension funds to increase their holdings of domestic assets from 10 to 30 percent of total assets in the next three years. The authorities continue to foster cooperation and monetary integration at the regional level, and remain fully committed to the ideals of the CMA as a means to anchor inflation and promote economic growth. 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.

Structural Issues

12. The authorities acknowledge the need and are committed to significantly improve the investment climate and enhance competitiveness through the acceleration of structural reforms and reduction of the cost of doing business. Other measures receiving attention include strengthening the anti-corruption commission; reducing labor market rigidities; simplifying business licensing requirements and procedures; and carrying out land reform that would help increase agricultural productivity. In addition, the authorities believe that the continued harmonious industrial climate, the country's good infrastructure and proximity to markets, and a relatively well-educated labor force augur well for future investment inflows.

13. The authorities are keenly aware that the process of transforming the economy will depend on implementing a number of structural reforms, perseverance with sound macroeconomic management, improvement of competitiveness, and development and implementation of a new set of investment incentives that are budget neutral. Foreign investors would bolster this effort as an indigenous entrepreneurial class of small and medium sized entrepreneurs (SMEs) is developed. The government, together with its SACU partners, will continue to pursue an aggressive bilateral trade negotiations agenda to achieve this goal.

Conclusion

14. The Swazi authorities face difficult challenges and have embarked on a strong reform agenda to revive economic growth. They count on the international community and their cooperating partners to assist them in dealing with the multiplicity of problems that could undermine the achievement of the MDGs. The continued classification of the country as lower middle-income, based only on GDP per capita and ignoring the poor social indicators facing the majority of the population, has hampered the authorities' efforts to secure concessional resources to finance social reforms. The country has all the social indicators of a poor developing country, with more than two thirds of the population living below the poverty line. HIV/AIDS continues to ravage the country and this, together with the worsening incidence of poverty, is causing untold harm. Therefore, we believe that there is need to review the methodology used to classify countries and address appropriately the serious concerns that have been expressed by Swaziland and other countries.