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Lesotho: Joint AfDB–World Bank Country Assistance Evaluation

- Lesotho—landlocked by and economically dependent on South Africa—experienced rapid growth during much of the 1990s, spurred in part by the World Bank–supported Lesotho Highlands Water Project (LHWP), but poverty reduction proved elusive.
- The World Bank also supported education, health, agriculture, and private sector development. With the exception of education, other World Bank assistance programs were ineffective.
- The World Bank’s overall country assistance program had a moderately unsatisfactory outcome, uncertain sustainability, and modest institutional development impact.
- Major areas of AfDB assistance include the transportation and social sectors. Overall, the program had a satisfactory outcome and likely sustainability, but modest institutional development impact.
- The evaluation conducted by the World Bank and the African Development Bank (AfDB) suggests that the strategies and activities of both banks should focus on reducing poverty and inequality by accelerating human capital development, combating HIV/AIDS, strengthening institutions, and developing the private sector.

Background

Lesotho is a small, poor country (GNP per capita, \$540). Half of its two million people live below the poverty line and income inequality is among the highest in the world. Lesotho is landlocked and completely surrounded by, and economically dependent on, the Republic of South Africa (RSA). Lesotho’s economy is based on limited agricultural and pastoral production and light manufacturing (textiles, clothing, and leather), supplemented by large, but declining, remittances from Lesotho miners in RSA. Recently there have also been royalties from supplying water to the RSA through the World Bank–supported LHWP. Added to the formidable challenge of the difficult physical and economic environment is a fragile and unpredictable political situation.

Substantial improvements in stabilization and growth have been achieved, stimulated in part by the LHWP. GDP growth averaged 4 percent yearly during the 1990s, but dropped sharply toward the end of the decade. Progress in structural reforms and sectoral policies such as privatization, health, agriculture, and rural development has been less impressive. The

country’s development continues to be challenged by widespread poverty, low quality of education and health services, a very high incidence of HIV/AIDS, weak institutions, lagging private sector development, and insufficient donor coordination.

World Bank Assistance During the 1990s

Bank assistance to Lesotho moved from an emphasis on stabilization and growth to a focus on poverty reduction and private sector development in the latter part of the 1990s. Throughout the decade the Bank supported joint work with the government and the IMF on successive policy framework papers. The Bank also supported a jointly prepared poverty assessment and a strategic economic options report, in which the government charted its post-apartheid economic strategy. But other planned analytical work was only partially carried out. Notably absent are periodic reviews of public expenditures.

The LHWP was the most important of Bank programs, but education, health, agriculture and rural development, and private sector development also received support. Ten-year commitments to Lesotho

tripled from \$100 million in the 1980s to \$300 million in the 1990s, because of LHWP. Annual average net disbursements were \$13 million and net transfers \$10 million during FY90–00, with peaks of nearly \$30 million for each in FY93 following LHWP approval.

The successful macroeconomic policies and the substantial impact of construction associated with the LHWP helped Lesotho achieve substantial GDP growth during the 1990s. Although the World Bank financed less than 4 percent of the first-phase LHWP cost of \$3.7 billion, it facilitated an agreement between South Africa and Lesotho, served as a catalyst in securing external finance, and advised on project formulation and implementation. Although the LHWP succeeded in generating sustained export revenue for Lesotho, the Bank did not provide adequate technical support for improving rural welfare from the proceeds of water sales. And the Bank erred by not insisting on including the Muela power plant as an integral part of the project under the management of the central oversight authority. This would have facilitated Muela's financing and implementation, and also created an incentive for Lesotho and South Africa to save on costs. Finally, with the exception of education, other Bank assistance programs were ineffective.

Taking all these successes and failures into account, the outcome of the World Bank assistance program is rated as moderately unsatisfactory. The Bank's contribution to institutional development was considered modest because most of the institutions established were weak and unsustainable. Sustainability of the reforms is uncertain, since growth has depended on large inflows of aid, and these may decline.

There may be growth in manufacturing and agriculture, but this will depend on enhanced political stability, better governance, and deeper parastatal reform. Such prospects are uncertain, and the economy remains vulnerable to changes in the subregion. An improved environment for growth and private sector development depends on enhanced stability, better governance, and deeper parastatal reform. Prospects for all of these changes are uncertain, and the economy remains vulnerable to changes in the subregion. Overall, Bank performance fell short. Lesotho's institutional capacity was overestimated whereas the implementation risks associated with political instability were underestimated.

African Development Bank–Operations Evaluation Department (AfDB–OPEV) Evaluation Findings

Since it began operations in Lesotho in 1974, the AfDB has committed \$275 million for 27 projects, 3 lines of

credit, and 6 studies. The public utilities and transport sectors are the main beneficiaries, with 28 percent and 26 percent of the portfolio respectively, followed by the social sector (24 percent), agriculture (13 percent), and industry (9 percent). The evaluation dealt mainly with the major areas of AfDB assistance to Lesotho, particularly the transport and social sectors. Overall, the outcome of the AfDB program was rated as barely satisfactory. Performance in non-lending activities was unsatisfactory: policy dialogue between Lesotho and AfDB was inadequate, AfDB capacity building efforts in the country were limited to the Ministries of Finance and Planning, and coordination with other donors was insufficient. The key lesson is that prior economic and sector work is crucial in the formulation of appropriate AfDB operational strategy for a country. Sustainability of the outcome appears likely, given the demonstrated commitment of the government (through the budgetary provisions) to the intervention projects. The impact on institutional development is, however, modest, as Lesotho continues to experience weaknesses in institutional capacity.

OED Recommendations

Future World Bank assistance to Lesotho should be centered on the following:

- Reduce poverty and inequality in the medium to longer term by focusing on the quality of education and human capital development at all levels.
- Place HIV/AIDS programs prominently on the agenda.
- Use Bank involvement in the LHWP and in agricultural policy formulation to strengthen rural institutions and enhance the enabling environment for private sector development.
- Identify data weaknesses, most urgently in areas related to poverty reduction, and promote monitoring and evaluation systems.
- Enhance Bank consultations with donors through a stronger operational representation in Maseru.

OPEV Recommendations

OPEV recommended that future AfDB strategy in Lesotho focus on the development challenges facing the country: poverty, unemployment, weak institutional capacity, the HIV/AIDS pandemic, private sector development, vulnerability to external policy changes, and governance issues.

Task Manager: Fareed Hassan (202) 473-1671

Director: Gregory Ingram (202) 473-1052 • Group Manager: Ruben Lamdany (202) 473-0118

OPEV Director: Gabriel Kariisa (225) 2020-4052 • Task Officer: Oladeji Oja (225) 2020-4262

FTBs published by OEDPK: ecampbellpage@worldbank.org (202) 473-5365

