SOUTHERN AFRICA QUARTERLY REVIEW AND ANALYSIS

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ANGOLA
BOTSWANA
LESOTHO
MADAGASCAR
MALAWI
MAURITIUS
MOZAMBIQUE
NAMIBIA
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PREFACE

The Southern Africa Quarterly Review and Analysis Report is a new publication, jointly produced by the Southern Africa Region Departments A and B of the African Development Bank. This publication is part of the African Development Bank's surveillance of economic and policy developments in Southern African countries. It also attempts to draw some implications of quarterly developments for the outlook period. The report is prepared by the Country Economists and is produced from information gathered through consultations, review of country documents, and other relevant sources.

I. REGIONAL OVERVIEW

The Southern African region, in general, continues to recover from the impact of the global financial crisis, with most of the countries expected to record near pre-crisis growth rates in 2011. Counter-cyclical fiscal and monetary measures adopted in response to the global financial crisis and the recovery in commodity prices and increasing activity in the primary sector in most of the countries have helped in the quick economic recovery. However continued dependence on the primary sector in most of the regional countries presents risks, especially given the uncertainty in commodity prices.

On the other hand, the ongoing political crises in Zimbabwe and Madagascar, as well as the diplomatic standoff in Malawi have been receiving negative regional and international media attention. In addition, Southern Africa's income inequalities and high levels of unemployment, including the region's powerhouse, South Africa, present downside risks for social stability. Notably, some of the countries in the region have had to content with crippling labor unrest as was the case in Botswana. Moreover, worsening fiscal positions in some of the Southern Africa Customs Union (SACU) member countries present limited opportunities for investments that would contribute to poverty reduction. Swaziland, in particular, is facing the worst fiscal crisis in decades and is now unable to make payments for basic public services like education and health. Similarly, the IMF recently declared Malawi's extended credit facility off-track leading to suspension of budget support by most development partners. Despite these challenges, the region still provides some of the best investment opportunities in Africa.

Following decades of civil wars in Angola and Mozambique, the prevailing peace has made it possible for the two countries to enjoy the highest economic growth rates in recent years, save for the 2009 global financial crisis-related economic slowdown. Until 2011, prudent economic policies in Malawi proved that poverty reduction was not impossible. Notably, Zambia graduated into the lower-middle-income category in July 2011, on the back of continued exceptional performance in agriculture, the recovery in the mining sector and good policies. Southern Africa is also doubling its efforts at deeper regional integration, hence an increased focus on regional infrastructure.

South Africa recently approved a multi-billion dollar infrastructure investment programme, with the power utility, Eskom, targeting investments of more than US$43 billion. Some of these investments have a regional scope. Furthermore, the discovery of oil in Namibia, resource- related infrastructure and productive investments in Mozambique and Zambia, as well as further consolidation of services investments in Mauritius are all examples of the potential that the region has to offer. The proposed Grand Free Trade Area incorporating the Southern Africa Development Community (SADC), the Common Market for East and Southern Africa (COMESA) and the East African Community (EAC) present further opportunities for the development of both hard and soft forms of infrastructure.

Finally, there are prospects for an improved macroeconomic environment. In particular, most of the countries have single-digit inflation levels; foreign reserves are being built-up, while efforts to ensure fiscal sustainability are being made. This improved macroeconomic environment coupled with reforms targeted at enhancing the business environment, as reflected in Mauritius' continued reform program, augur well for the region's economic vibrancy and prosperity.

The individual country briefs, which provide further details for each of the 12 countries in Southern Africa, follow immediately. This inaugural edition of the Southern Africa Quarterly Review and Analysis also includes a special section focusing on **Reforms for Private Sector Participation in Infrastructure Development** in Zimbabwe, which may be relevant to other countries in the region.

AFDB

Task Team members, Albert Mafusire, Helga Peres and Imen Chorfi, coordinated the preparation of the Southern Africa Quarterly Review and Analysis Report under the general guidance of the Regional Directors, Ebrima Faal and Chiji Chinedum Ojukwu.

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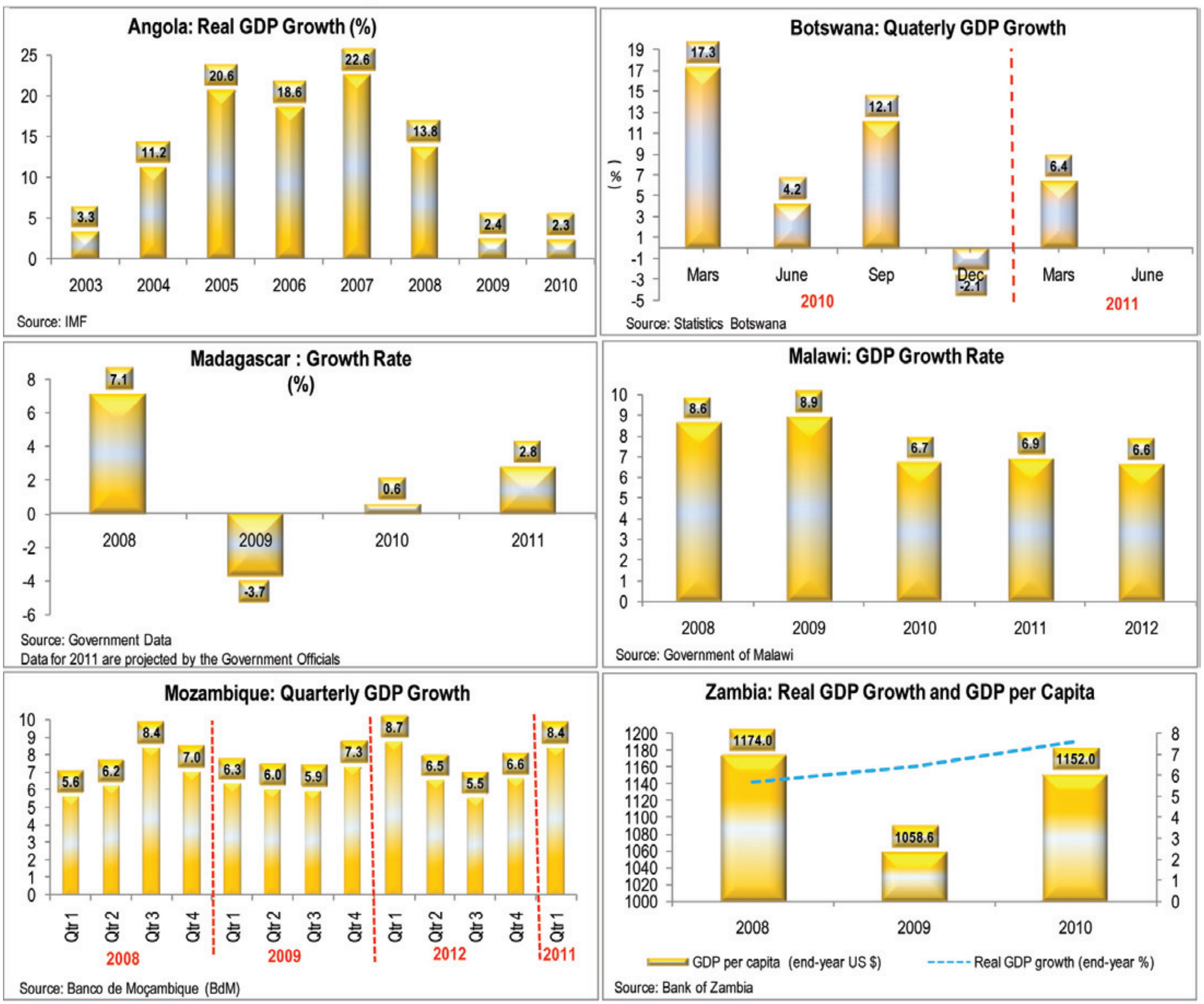
GDP growth rate for Selected Southern African Countries



II. COUNTRY ANALYSES

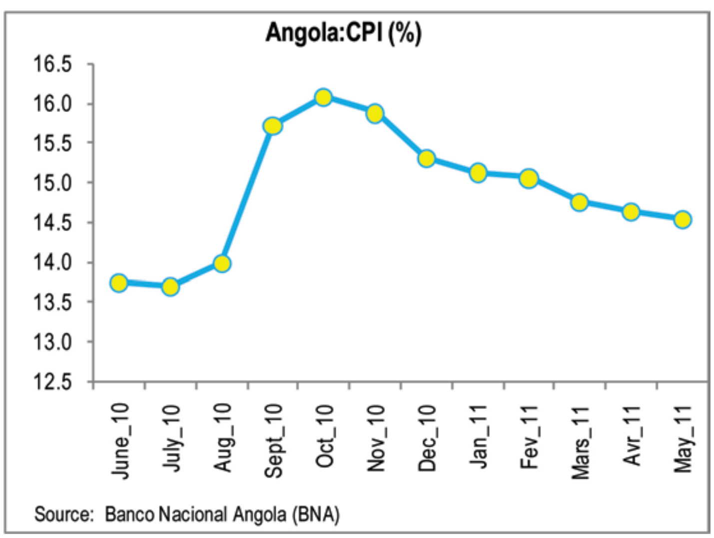
ANGOLA

Highlights

- Due to its good macroeconomic performance in May and June, Angola's credit rating was upgraded by major credit rating agencies. Fitch and Standard & Poor´s raised the rating from "B+" with positive outlook, to "BB" with stable Outlook. Moody's raised the rating from "B1" with positive Outlook to "Ba3" with stable Outlook. This puts Angola at just one level away from the investment grade "BBB", which the country expects to attain after the 2012 elections.
- The IMF concluded, in June, the fifth review of Angola's 27-month Stand-By Arrangement. The arrangement approved in November 2009 provides for US$1.4 billion, US$1.25 billion of which has been disbursed to date. The good conclusion of the review will enable Angola to withdraw a further US$ 136 million.
- The government's domestic arrears, accumulated since the 2008-2009's financial crisis, peaked at1.5 % of GDP in June 2010. The government admitted US$ 6.8 billion in domestic arrears was still to be settled by the end of 2010. However, most of the debt was cleared during the first quarter of 2011, and all arrears should be settled by the end of July through cash payments.

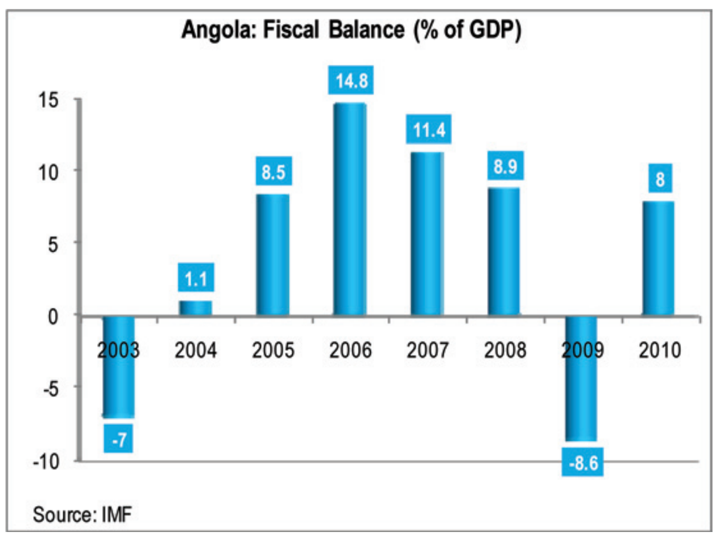
Macroeconomic Management Overview

Economic Growth: Following the stalling of growth in 2009, increases in revenue from oil exports in 2010 revived Angola's growth, recorded at 4.5%. The oil sector constitutes nearly 60% of GDP, 80% of the state budget, and nearly all exports. Despite the non-oil sector outpacing oil sector growth, on average, by 2% during the last decade, economic activities and, in particular, agriculture (roughly representing only 11% of GDP) has been slow to develop. In 2011, the macroeconomic environment is improving. GDP growth rate is expected to climb to 7.5%, with rises in oil prices outweighing the drop in oil production, now expected to be, on average, 1.7 million barrels per day.



Monetary Policy and Banking System: The 2011 monetary program targets three main objectives: increase gross international reserves by at least US$1.7 billion; gradual adjustment of the value of the Kwanza in line with market fundamentals; bringing down inflation to around 12%. Inflation, until early 2010 resiliently around 14%, peaked by mid-2010 at 15.88% before slowly starting a downward trend to reach 14.76% in May 2011. The central bank (BNA) has eased monetary policy in the face of the kwanza stabilization against the dollar (now at US$ 1:93.29Kz) by decreasing short-term interest rates. Notwithstanding BNA's focus on reining in inflation, the revision of the government's budget scheduled for July 2011 could jeopardise its target of 12% inflation. The Angolan banking system was not impacted by the global crisis. However, the country's liquidity crisis and the spike in public debt yields have diverted bank credit from the private to the public sector. Non-performing loans have risen from 2.6% to 7.1%, triggered, in part, by the financial distress of firms that are owed substantial sums by the government.

Fiscal Policy: After the 2009 crisis, higher oil prices in 2010 helped the reversal of the previous year's 8.6% fiscal deficit to a 7.5% surplus. With a conservative oil price of US$ 72per barrel, the 2011 budget forecasts a 4.5% surplus. The National Reconstruction Program expanded, with capital expenditure reaching 11.6% of GDP, and budget spending in social areas increased to 31.5% of GDP. However, the continued rise of oil prices will accommodate a supplementary budget to be presented in August. The Government's reform program envisages the reduction of the non-oil fiscal deficit, at -20.4% in 2010, to -19% in 2015, but as the country reaches peak -oil production, efforts to diversify beyond oil are crucial for long-term fiscal sustainability.



External Position: The 2010 upturn in oil markets in combination with a reduction in imports, outweighed lower oil production, resulting in a sharp improvement in the current account, to a surplus of 0.6% of GDP. The tightening of monetary and fiscal policies contributed to a buildup of US$ 3 billion in Gross Foreign Reserves (GFR), reaching US$ 16.2 billion (roughly 4.3 months of imports). The pickup in economic activity in 2011 will increase imports, while oil production will remain stable due to technical limitations. Hence, the 2011 current account should be negative at -4.5%. Despite the settling of domestic arrears, GFR should rise to US$ 17.9 billion and are expected to be US$ 26.8 billion in 2015. The Kwanza recovered slightly, stabilizing broadly around Kz 93:1 US$, while the spread to the parallel market has reduced to nearly 5%. External debt-to-GDP will remain relatively low at 20%, with a debt-service ratio of 10.2%.

Institutional and Structural Reforms

Public Sector Management: The government intends to finalize a debt management strategy during the next quarter. Uncertainty surrounds the creation of the Sovereign Welfare Fund (SWF) with debate ongoing as to whether the ability to engage in countercyclical policies outweighs the great need for short-term investment after decades of war. The 2012 legislative elections might delay the implementation of the SWF.

With the support of the African Development Bank (AfDB), the Ministry of Planning, is implementing measures to improve project budgeting, appraisal and monitoring capacity. The objective is to limit approval only to well-designed projects that have high economic and social rates of return.

The National Assembly is currently evaluating a comprehensive legislative package on tax reform. The reforms are aimed at modernizing the tax administration, improving tax compliance, broadening the tax base while scaling back tax exemptions, and putting in place efficient legal processes for handling tax cases.

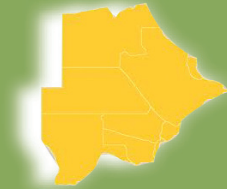
Private Sector Reform: The government is setting up dedicated units in line ministries to manage public- private partnerships, with the objective of supplementing state activities in areas such as power generation, urban water supply, and road maintenance. Relevant legislation should be completed in the 3rd quarter. Other areas with on-going reforms are: weak contract enforcement; difficulties in transferring property; and multiple layers of regulation. A reform program has been initiated to address weaknesses in the judicial system and the expansion of the court system. Licensing in the trade sector has been simplified; however a broader review of licensing processes towards increased deregulation is due in 2011.

Issues Requiring Particular Attention

Fiscal sustainability will be the prime issue for the short and medium-term. The creation of a Sovereign Wealth Fundis essential to put an end to the disruptive boom-bust cycle associated with oil price volatility. Also needing attention is the continuation of the reforms on public financial management transparency, and safeguard measures for the operation of public entities.

Donor Coordination Activities

ODA accounts for roughly 1% of the state's budget. Without a formal aid coordination framework in place and a difficult operational environment, donor coordination activities should focus on strengthening the fiduciary environment in order to foster a conducive environment for policy-based operations.❋



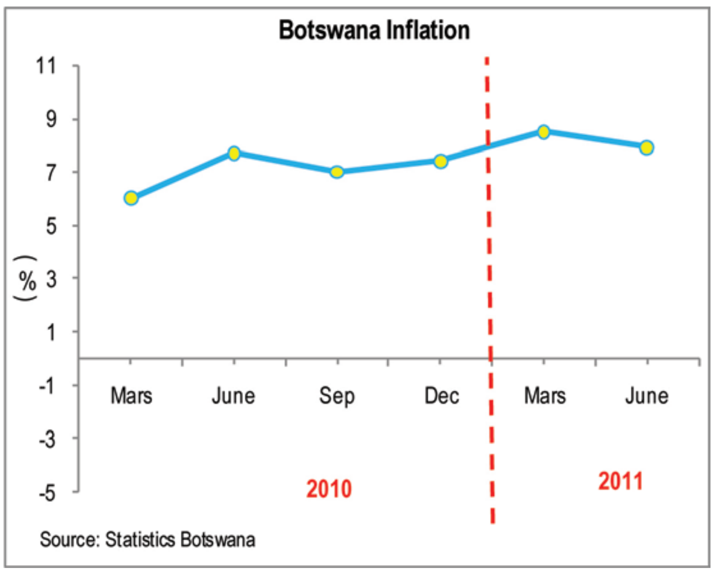
BOTSWANA

Highlights

- Botswana experienced a prolonged eight-week public sector strike from 18th April 2011, demanding a salary increase of 16%. This demand came at the time the government was striving to narrow the budget deficit to a sustainable level, following a drastic decline in revenue due to the global financial crisis. Although the strike was terminated following a compromise on an increase of 3%; its impact will be felt as the government compensates the increase by scaling down expenditure, especially on development projects.
- Diamond exports have strongly recovered, nearing the pre-crisis level of US$3.36 billion in 2007, with diamond exports in 2010 amounting to US$3.21 million. Exports for the first five months of 2011 reached US$1.8 billion. This performance contributed to the healthy GDP growth of 6.4% during the first quarter of 2011, and consequently improved government finances.

Macroeconomic Management Overview

Economic Growth: Botswana's economy has rebounded strongly from the economic downturn. In 2010, the economy grew by 7.2%, compared to a contraction of 4.9% in 2009. Growth was broadly balanced across sectors, where mining and non-mining sectors grew by 7.0% and 7.3% respectively. Economic growth is expected to remain high in the period ahead.



Monetary Policy and Banking System: The Bank of Botswana's objective is to lower inflation to the target range of 3-6 %. However inflation was outside the target range, averaging 8% between January and May 2011 owing to exogenous factors, mainly fuel prices and food imports (see Figure 1). The Bank of Botswana prime lending rate was however reduced to 9.5% in December 2010, but it is likely to be increased due to the persistent high inflation rate. The exchange rate between the Pula and major international currencies has remained stable despite rising inflation; aided mainly by the recovery in mining exports. There has been modest growth in the money supply associated with low government expenditure and sluggish recovery in personal incomes. The distribution of commercial bank credit across sectors is however skewed to household consumption standing at around 60% of total loans and advances. Productive sectors have gotten very little credit, with business services getting 8.5%, construction 4.3%, manufacturing 4%, and agriculture 0.8%. This credit distribution runs counter to the notion of economic diversification by promoting investment in the non-mining productive sectors.

Fiscal Policy: Botswana's budget for the 2011/12 fiscal year demonstrates that the Government is committed to controlling spending and ensuring the country's long-term fiscal sustainability. The fiscal balance has shown significant improvement with overall deficit falling from 10.9% in 2009/10 to 8.1% in 2010/11 and projected to further decline to 5.2% in 2011/12. The medium term objective is to attain a balanced budget by 2012/13.

Balance of Payments: Botswana has seen significant external trade improvement following the recovery in global demand for diamonds. In 2010, merchandised exports and imports increased by 27% and 13%, respectively, leading to a 70%drop in the trade deficit. However, the country's current account widened from 4.7% of GDP in 2009 to 5.1% in 2010, largely on account of the deterioration in the income and services accounts. Notwithstanding the widening of the current accounts deficit, gross foreign reserves remained stable, averaging around US$8.3 billion from January to May 2011, an amount equivalent to 20 months of imports.

Institutional and Structural Reforms

Support for economic diversification: To spur economic diversification, the government has granted special treatment to the local private sector in the procurement of public goods and services. To this end, the central government, local authorities and parastatal organizations are now required to purchase all their products and services from locally-based manufacturers and service providers; provided the goods and services are locally available, competitively priced and meet tender specifications

Trade facilitation for regional integration: Botswana is spearheading a number of projects, among which is the construction of the Kazungula Bridge over Zambezi River, to be jointly financed with the Zambian government. In April 2011, the two countries agreed to move to the construction phase of the bridge and related boarder facilities. The financing of the project, estimated to cost US$220 million, will be shared equality among the two countries and the Bank is expected to be one of the project's financiers.

Donor Coordination Activities

The recent Bank mission to Botswana for the mid-term review of the Country Strategy Paper provided an opportunity to discuss possible areas of support and collaboration with some development partners in the country. ❋

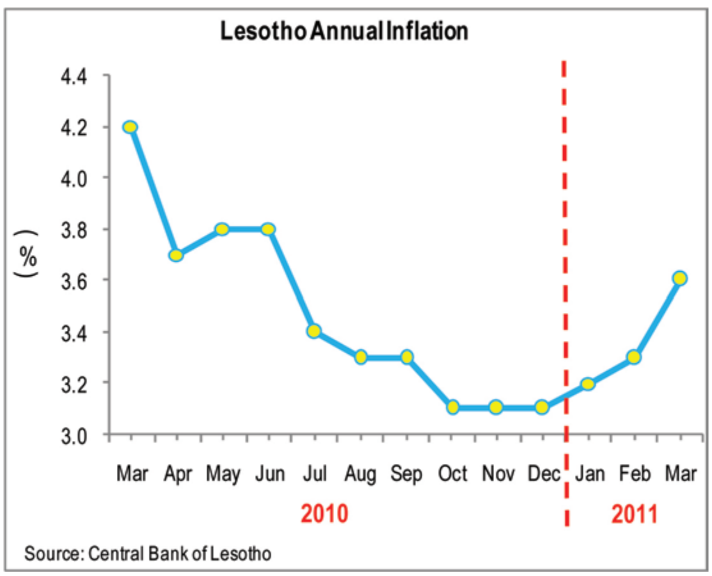
LESOTHO

Highlights

- By the end of March 2011, the economy showed signs of recovery in almost all sectors of the economy. Growth was driven by recovery in global demand for diamond and strong consumer demand.
- Fiscal sustainability remains a real concern in the wake of slow recovery in SACU revenues. This prompted government to rundown its deposits to finance the fiscal deficit, mainly driven by a marked increase in personnel expenditures and a sharp drop in revenues.
- The attainment of Millennium Development Goals (MDGs) remains a challenge given difficulties in combating HIV/AIDS and malaria, reducing child mortality, improving maternal health, fostering environmental sustainability and eradicating extreme poverty.

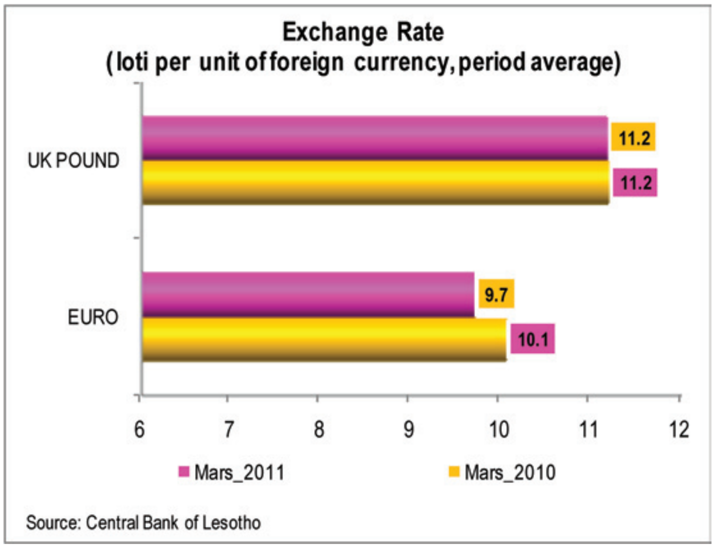
Macroeconomic Management Overview

Economic Growth: Almost all sectors of the economy showed signs of recovery during the first quarter ending March 2011. Underpinning this recovery in the primary and tertiary sectors were increased domestic production and higher global demand for diamonds, increased consumer confidence mirrored by increased sales of goods and services, respectively. Notwithstanding the above, the floods experienced in December 2010 had a devastating effect on the economy, as they destroyed roads and caused water pipes to burst thereby affecting businesses.



Source: Central Bank of Lesotho

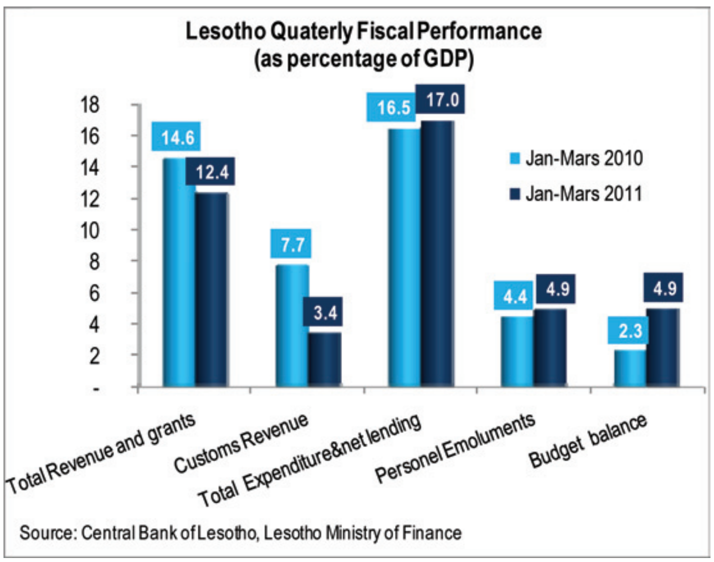
Monetary Policy and Banking System: The monetary policy stance of the Central Bank of Lesotho is driven by the need to maintain price stability, which in turn is anchored by the maintenance of parity between the loti and the South African rand. Money supply (MI) grew by 2.3 per cent on an annual basis, reflecting increases in demand deposits. Domestic credit extension grew by 30.7% mainly due to increases in credit to businesses and households. While the credit deposit ratio increased to 40% from 31% the same period last year, it remains low, an indication that liquidity at the commercial banks is still very high. The government continues to drawdown its deposits in order to finance its budget, with net claims on the Banking system having increased by 33.7%.



Source: Central Bank of Lesotho

Year-on-year inflation was recorded at 3.6% in March 2011. The main drivers for inflation were respectively housing, water, electricity and other fuels category, alcoholic beverages and tobacco, food and non-food beverages. However, inflation remained within the Common Market Area target range of 3-6% per annum.

The loti appreciated against the US dollar, the Euro and the pound sterling which are the currencies of Lesotho's main trading partners. On an annual basis, the loti appreciated by 6.5, 3.5 and 0.2%against the US dollar, the Euro and the pound, respectively. While the appreciation of the loti is favorable to imports, it has reduced the competitiveness of the country's manufactured exports.



Source: Central Bank of Lesotho, Lesotho Ministry of Finance

Fiscal Policy: During the first quarter of the year, the overall fiscal deficit was recorded at 4.6% of GDP; an increase of 2.7% compared to the same period in 2010. The deficit was mainly driven by a sharp drop in revenues, in particular, customs revenues and a marked increase in personnel expenditures. The deficit was mainly financed through domestic sources, in particular, by running down of government deposits with the banking system. Fiscal sustainability remains a real concern in light of the slow recovery of SACU receipts and an expected increase in expenditures to support local government and national elections in 2012.

Balance of Payments: The country's current account deteriorated by 3.5% of GDP in the quarter under review compared to the same period in 2010. Import expenditures outstripped a good performance in diamond and textiles and clothing exports. This was compounded by a decline in the other exports over the same period. Income and current transfers registered a decline mainly due to lower remittances from Basotho miners in South African mines, lower investment incomes due to reduced global interest rates and reductions in SACU non-duty receipts. Despite the widening of the current account, gross reserves were sufficient to cover 5.9 month of imports and to support exchange rate parity between the loti and South Africa rand.

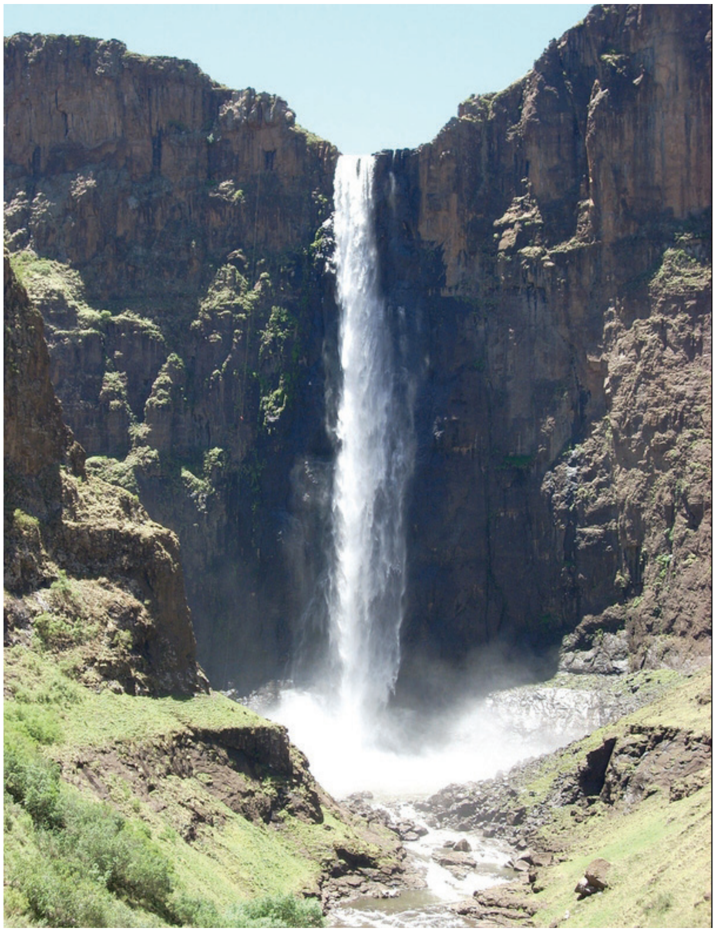
Institutional and Structural Reforms

Public Sector Management: Progress continues to be made towards improving the quality of financial management. The Medium Term Framework (MTEF) is being used in budget preparation by ministries. Also, an integrated Financial Management Information system (IFMIS) was rolled out to all ministries in April 2009.

Private Sector Reform: The 2011 "Doing Business" indicators identify several areas in which Lesotho's ranking should improve. These include starting a business, dealing with construction permits, obtaining credit, registering property, protecting investors, trading across borders, and enforcing contracts. Additionally, the new land bill, which was passed by Parliament and assented to by the King in 2010, is expected to ease access to land and promote investment. The areas where Lesotho fares relatively well include paying taxes and closing a business.

Human development and cross-cutting Issues: Lesotho continues to have challenges of attaining some of the MDG targets. It has particular difficulties in combating HIV, Malaria and other diseases; ensuring environmental sustainability; reducing child mortality, improving maternal health; and eradicating extreme poverty and hunger. The population under income poverty is put at 43% and multiple deprivations at 48%. The Human Development Index (HDI) has improved from 0.397 in 1980 to 0.427 in 2010, ranking Lesotho above the Sub-Saharan average of 0.389.

Trade Facilitation: Lesotho is confronted with challenges resulting from outdated and ineffective customs procedures and systems, delays in the clearance of imports and exports, and other administrative inefficiencies resulting in high transaction costs.



Donor Coordination Activities

The country is engaged with a number of development partners covering various areas with good coordination, but no harmonized disbursement procedures. The African Development Bank (Budget support, health, education, water, energy and multi-sector), EC (Budget support, human development, water and sanitation, social protection), World Bank (Human development, budget support, agricultural, water, human development, infrastructure), Irish Aid (Health, governance, HIV/AIDS, fast-track initiatives, governance), DFID (Public Financial Management, capacity building, agriculture, HIV/AIDS, social protection, trade), UNDP (Governance, HIV/AIDS, energy, environment) and USAID (HIV/AIDS). Other donors include IFAD (Agriculture), South Africa (Water), Kuwait (Water and health), Saudi Arabia (water), GTZ (capacity building and institutional support) and MCC (water). Despite the lack of harmonized procedures on disbursement and procurement, with each donor applying its own guidelines and procedures, budget support disbursements are based on joint assessment and use of one account for the resources.

MADAGASCAR

Highlights

- The SADC[1] road map was approved following the amendment of the conditions for the return of political exiles before elections, including former president Marc Ravalomanana. However, the country's international recognition depends on the approval of the SADC road map by the African Union Peace and Security Council as well as the International Contact Group on Madagascar and the United Nations prior to its signing by all of the country's stakeholders at the end of July 2011.
- The continuation of the political crisis coupled with the suspension of a major part of foreign aid has had adverse consequences on the country's economic and social situation: in 2010[2], 76% of the country's population was considered poor compared to 68% in 2005; primary school completion rate declined by 5 points and about 200 health centers were closed.
- The lack of clarity on the country's political future continues to impact private sector activities and continues to affect foreign investment. The country's economic prospects remain bleak and might further deteriorate if the crisis continues following the freezing of foreign aid.

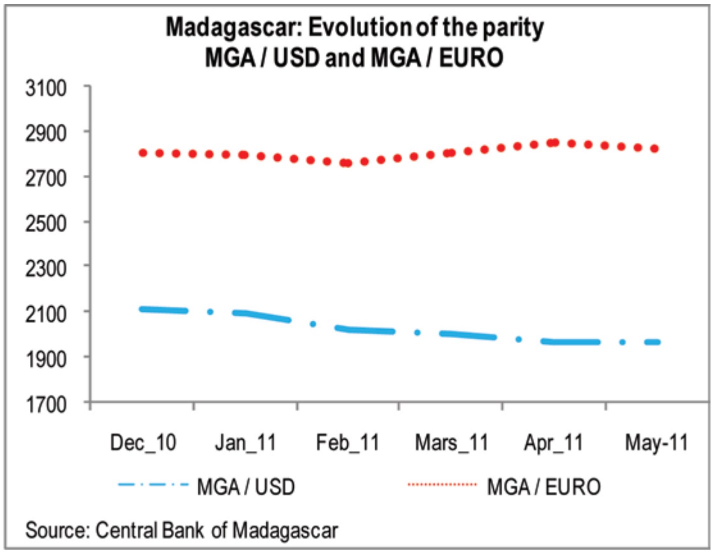
Macroeconomic Management Overview

Economic Growth: The country's authorities forecast a 2.8% growth in 2011 (against 0.6% in 2010), driven mainly by the secondary sector (+12.6%), in particular, the extractive industries (228%) and the tertiary sector (+2.8%). There are no new data to support these forecasts. However, it is already obvious that these growth prospects will not materialize due to delays in exploitation activities of a major mining project – the Ambatovy project – which have been put off till next year and the sluggishness in BTP recovery due to the suspension of foreign aid which accounts for 70% of public investments.

Monetary Policy and Banking System: The country's money supply registered a small increase (+1.3%) between December 2010 and April 2011. Net credit to the State reduced significantly by about 24%, reflecting efforts made by the government since 2010 to reduce its financing of the banking system. With regard to credits to the economy, they have recorded a moderate increase of 2.5% during the period, as the central bank maintained its prime rate at 9.5% since August 2009, despite the challenging context.

Concerning the Inflation, the central bank's objective was to contain inflation to 7.6% in 2011. However, between December 2010 and May 2011, the rate of inflation increased by 3.3% and it stood at 10.2% year-on-year. The increase was greater during the first two months of the year and it impacted both imported products (+4.2% due to petroleum products) and local products (+ 3.5%), especially rice.

Regarding the exchange rate, the objective of monetary authorities, in 2011, was to maintain the value of the Ariary through exchange rate stabilization. Over the first five months of the year, the country's currency appreciated by close to 1% on average against the Euro and by 4% against the dollar, reflecting more of a decline in the value of the dollar on global markets rather than a reflection of traditional factors such as massive inflows of foreign capital or exchange rate fluctuations.



Fiscal Policy: Information[3] on budget implementation during the first semester of 2011 is inadequate for a proper analysis of the inflows, expenses and financing. The 2011 budget provides for a 15% increase in receipts as against the figure for 2010, based on a complete return of foreign aid. Forecasted expenses show an increase of 24%. The budget deficit is expected to be contained at 2% and mainly financed with foreign aid. Given the current context, the primary objective of the government is to maintain a balanced budget which requires the adjustment of the overall level of public expenses to that of available resources, by using public investments as the adjustment variable.

Balance of payments: The country's balance of payments has recorded a structural deficit. In this regard, the government's forecast indicates a deterioration of the overall balance estimated at DTS 182.1 million against DTS 96.1 million in 2010, resulting from the capital account. The current account deficit will improve to DTS 851.1 million (against DTS 896.1 million in 2010) following an expected increase in exports. The balance of payments for goods and services as well as those for financial and capital transactions would respectively register deficits at DTS 981.3 million (against DTS 989.4 million in 2010) and DTS 846.2 million (against DTS 668.2 million in 2010). The expansion of the latter could be explained by a decline in foreign direct investments following the end of mining projects installation. The inadequacy of available data makes it impossible to carry out profound analysis at the level of this section.

1 Four (4) SADC meetings were held recently to resolve the country's crisis (Livingston in Zambia on March 31); Windhoek in Namibia on May 20; Gaborone in Botswana on June 7 and Sandton in South Africa from June 11 - 12.

2 According to a 2010 Periodic Household Survey (EPM 2010)

3 Final data for the first semester will only be released in August 2011 at the end of the next budget review.

However, provisional information on external trade in the first quarter of 2011 shows an increase in exports of 10.4% and a decline in imports of 1.4% compared to the same period in 2010.

Institutional and Structural Reforms

Due to the country's situation, more importance is given to the management of daily affairs rather than to reforms in both the private and public sectors. The most important reforms are being carried out mainly in the area of public finances within the framework of the implementation of the 2011 finance law. Thus, there are plans underway for a new investment code, including fiscal and customs policy with a view to promoting production in certain sectors such as agriculture, information and communication technology, tourism and energy, in particular, renewable energies. No progress report is available on the implementation of these reforms. Regarding trade, we can note the recent creation of the Resource Center on International Trade (CRCI) through the private sector, designed to serve as an agency for the promotion of exports and the support of international negotiations. No major development has been noted in the area of regional integration during the period. With regard to private sector development, various evaluations[4] of the business climate highlight low business performance due to an inappropriate regulatory framework and recurrent financing problems. No major reforms have been planned in this domain for now.

Issues Requiring Particular Attention

Special attention needs to be given to the resolution of the political crisis which is adversely impacting the country's growth prospects and is rolling back some of the country's economic and social gains.

Donor Coordination Activities

Despite the crisis, donor coordination is a reality both at the global and sectoral levels (private sector development, water and sanitation, rural development and social sectors).

4 In reference to the « Doing business » annual report and the report on the evaluation of the investment climate (World Bank, October 2010)

MALAWI

Highlights

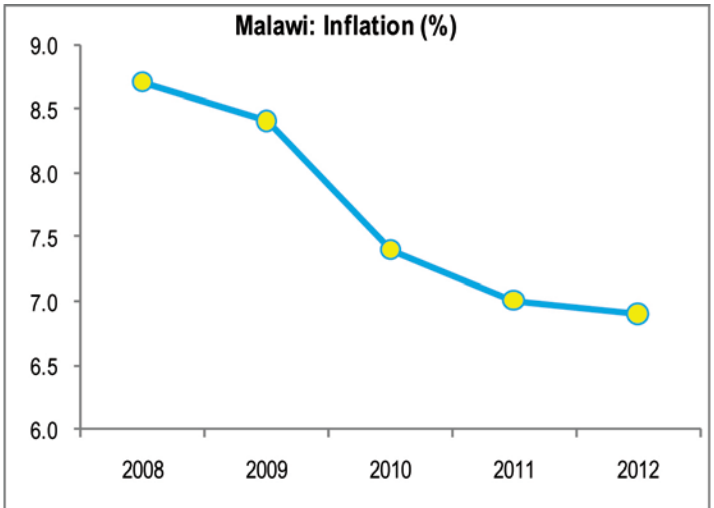
- The deteriorating Government-donor relations are expected to negatively impact growth following concerns over political governance and macroeconomic management issues. In particular, the impasse between the Government of Malawi (GoM) and the IMF on the ECF with respect to a rigid foreign exchange policy will also affect budget support resources from development partners (DPs).
- The GoM adopted a zero-deficit budget for the 2011/12 fiscal year, with the government financing all recurrent expenditure, while resources from DPs will be used for development expenditure. The zero-budget announcement came at a time when Malawi was facing deteriorating foreign exchange challenges and weak bilateral relations with some of its traditional donors.
- According to 2011 Global Peace Index, Malawi was ranked second to Botswana in Africa as the most peaceful country on the continent. However, recent political developments arising from concerns over political and economic governance concerns may lead to a serious escalation of political discontent.

Macroeconomic Management Overview

Economic Growth: Malawi is projected to grow by 6.9 % in 2011 and 6.6 % in 2012. This is higher than the projected global GDP growth of 4.5% in both 2011 and 2012, and Sub-Saharan Africa's growth which is projected at 5.5 % in 2011 and 5.9 % in 2012. It is expected that this overall growth will be anchored by growth in agriculture (6.4% in 2011 and 7.3% in 2012), mining and quarrying (33.1% and 15.6%), construction (9.0% and 6.2%), finance and insurance (9.2% and 8.6%) as well as wholesale and retail (6.5% and 5.9%).While the government's projected growth trends are in line with those of the IMF, they are more optimistic as the later projects growth at 6.1% in 2011 and 5.9% in 2012, on account of foreign exchange and fuel shortages which are likely to impact on industrial production. A significant decline in tobacco revenues in 2011, coupled with less than expected donor inflows, will significantly contribute to the foreign exchange shortages. Tobacco, which generates about 60% of Malawi's foreign exchange earnings, is fetching very low prices[5].

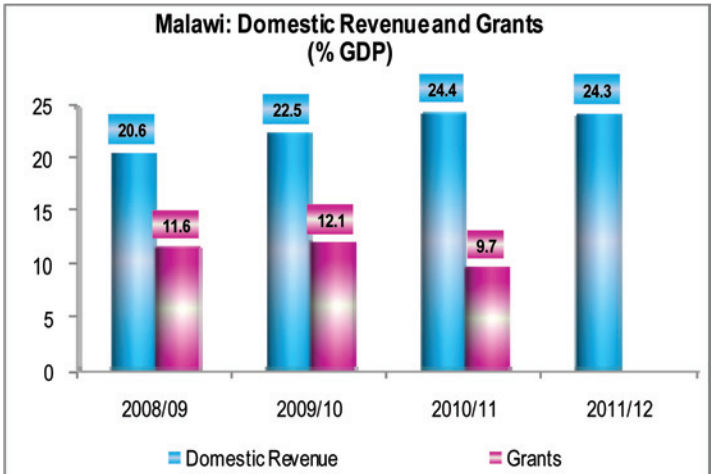
Monetary Policy and Banking System: Inflation in Malawi has been on the decline from 15.5% in 2005 to 7.45% in 2010. The 2011/12 budget assumes that inflation will slide further down from 7.4 % in 2010 to 7.0 % by the end of 2011. The devaluation of the kwacha and rising oil prices are likely to reverse this trend in 2012. Inflation stood at 7.1% in April 2011. A downward inflationary trend has been sustained in Malawi, largely due to increases in agricultural production, fiscal prudence and a fixed exchange rate regime, and other factors. Going forward, GoM recognizes that the anticipated global oil price increases may exert pressure on domestic price, and anticipates that such pressure will be mitigated through tight monetary policy. During the2010/11 fiscal year, an expansionary monetary policy was pursued, with broadly defined money supply (M2) increasing by 16.1% to MWK203.6 billion in March 2011.

The 2011/12 budget does not make an explicit assumption on the exchange rate, but there is less flexibility in its exchange rate management. The Malawi Kwacha remained relatively stable against the US Dollar in April 2011, but depreciated against currencies of the country's major trading partners. Both the Budget Statement and the April 2011 Aide Memoire prepared by the CABS Development Partners note that low tobacco prices, high fuel import costs and high costs of imported fertilizers pose challenges on the foreign reserve position. Malawi needs about USD 144.6 million in 2011 for procuring farm inputs (fertilizer).



Source: Government of Malawi

Fiscal Policy: The GoM has employed the Zero-Deficit Budget reform measure as an indication that it has some capacity to grow its domestic resources, building on a rising domestic revenue trend (attributed to improvements in revenue collection and tax compliance) and declining grants. The GoM has also indicated its desire to graduate from excessive donor dependence.



Source: Government of Malawi

5 Tobacco export earnings for 2011 are projected to go down by at least 33% from US$450 million to US$300 million. By May 2011, the earnings had fallen by 78.8%.

In line with the Malawi Growth and Development Strategy (MGDS), the most funded individual votes are education (13.1%), agriculture (12.4%), and health (8.8%). The budget for agriculture continues to be dominated by the Farm Input Subsidy Programme (FISP). The FISP accounts for 55.7% of the vote allocation. Commendable improvements have been introduced in the budget, including the Medium Term Expenditure Framework (MTEF), the streamlining of budget documentation to increase readability, and the posting of the documentation on the Internet to increase availability.

Balance of Payments: Foreign exchange reserves, which amounted to 3.6 months of imports in 2010, have declined to 2.1 months of import cover by April 2011. Trade deficit worsened to MWK 106.2 billion (representing current account deficit 19.98% of GDP) in 2010 from MWK 54.3 billion (13.09% of GDP) recorded in 2009.It is projected that trade deficit will continue to worsen in 2011 with the deficit rising to MWK 114,812.23 billion (18.7% of GDP). The deteriorating external balance is a result of faster growth in imports expenditure compared to exports revenue, due especially to less than expected tobacco prices.

Institutional and Structural Reforms

Public Sector Management and Recent Developments: Malawi is in the process of finalizing the drafting of its second medium term national development strategy, the Malawi Growth and Development Strategy (MGDS II, 2011-16).[6] The thematic areas for the MGDS II remain the same like those of MGDS I. MGDS II has nine key pillars that are aimed at enhancing wealth creation and reducing poverty. Furthermore, the country is finalizing the designing of the Public Finance Management (PFM) Reform programme which will identify areas of focus over the next five years.

Private Sector Reform: The 2011 "Doing Business Survey" by the World Bank Group noted reforms in the areas of 'Registering Property' and 'Enforcing Contracts'. Malawi eased property transfers by cutting the waiting time for consents and registration of legal instruments by half, leading to a jump of 20 places in international rankings (from 101 to 81 out of 183 economies).

Human Development and Cross-cutting Issues: Malawi is on the right path to reducing poverty and fighting HIV/AIDS. Poverty has gone down from 52% in 2004 to 40% in 2010 with a 2010 HDI standing at 0.385 from 0.336 in 2005. HIV/AIDS national prevalence rate was at 12% in 2009 from around 24% in 1998. The country is also set to meet the MDG targets on universal primary education, gender and Maternal Mortality Rate (MMR). The expected decline in donor resources could reverse this trend, especially as Malawi does not have a comprehensive social protection system to provide safety nets to the disadvantaged citizens apart from the Farm Input Subsidy Programme.

Donor Coordination Activities

Development Partners (DPs) have joined the civil society in expressing their concerns over the amendment and enactment of laws that would infringe on democratic, civil and political rights and over the expulsion of the British High Commissioner to Malawi. Due to the IMF ECF programme being off track, DPs providing budget support (AfDB, EU, Germany, Norway and World Bank) were yet to commit themselves to supporting the 2011/12 budget[7].Budget support represents 30% of all grants and 6% of the total revenues and grants in the FY 2011/12 budget.

6 The thematic areas of MGDS II are Sustainable Economic Growth; Social Development; Social Support and Disaster Risk Management; Infrastructure Development; Improved Governance; and Cross-Cutting Issues.

7 Malawi's fiscal year runs from 1 July to 30 June.

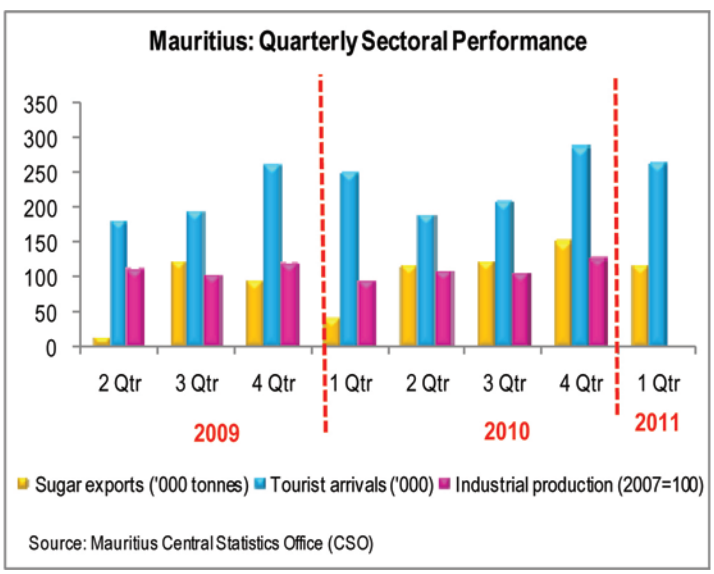
MAURITIUS

Highlights

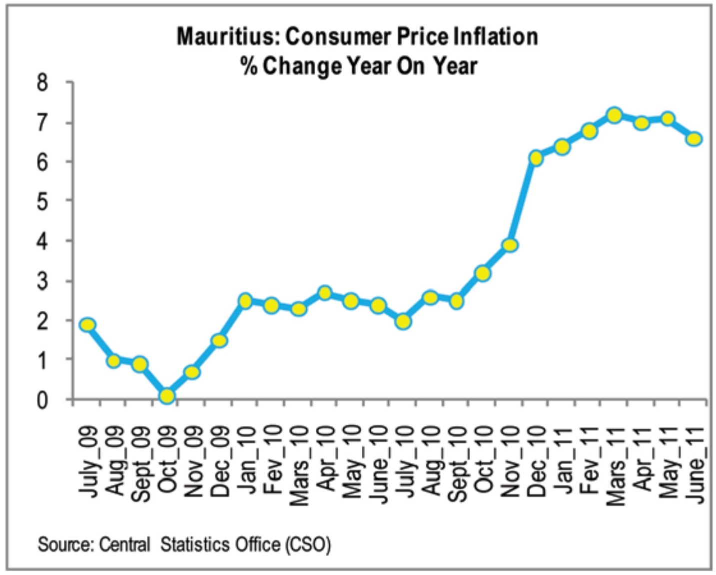
- The governing coalition, led by Prime Minister Navinchandra Ramgoolam of the Mauritian Labour Party (MLP), remains in place in spite of media hints of a rift between the main parties. The coalition enjoys a solid parliamentary majority allowing the government to push forward reforms contained in the 2010-2015 Government Program.
- The government has adopted an Economic Restructuring and Competitiveness Program (ERCP) and embarked on measures to accelerate sugar sector reforms and diversify tourism products to attract non-traditional visitors.
- On the social front, the Government of Mauritius (GoM) is keen to contain the household water crisis that has hit some parts of the country following this year's drought, rising food prices and high unemployment, estimated at 8.3% in the first quarter of 2011.
- In June 2011, the government announced an ambitious multi-year US$10bn program to upgrade the country's infrastructure with a view to tripling the country's US$9.2bn GDP by 2030 through improved competitiveness.

Macroeconomic Management Overview

Economic Growth: Economic recovery remains on course with real GDP growth projected at 4.5% in 2011 from 4.1% in 2010. 2011 first quarter earnings from tourism reached MUR11.9bn, 8% higher than the same period in 2010. At 6.6% in June 2011 from 2.4% in 2010,the inflation rate has accelerated on the back of rising global commodity prices, prompting the Monetary Policy Committee (MPC) to raise the key repo rate for the second time this year by 25 basis points to 5.50%.



Some key sectors may be responding positively although prospects for full recovery remain unclear. At 116,000 tonnes, 2011 first quarter exports of sugar more than doubled those of the same period in 2010. Tourist arrivals during the first quarter were 5% and 13% higher compared to the same period in 2010 and 2009, respectively. Noteworthy were increases in tourists from India and China by 33.4% and 30.1%, respectively, during the period albeit from a low base.



Monetary Policy and Banking System: Inflationary pressures are threatening economic recovery. Year-on-year consumer price inflation peaked at 7.2% in the first quarter of 2011 as the cost of fuel and food imports rose (53% of Mauritius' CPI basket are imported goods). A rise in the key repo rate from 4.75% to 5.25% in March 2011 helped ease inflation to 6.6% in June 2011. However, the key repo rate was raised further by 25 basis points in June 2011 as year-on-year core inflation rose by 4.6% in May 2011.

The Mauritian Rupee has registered a 14% year-on-year appreciation against the dollar as at the end of June, negatively impacting the competitiveness of exports.

Fiscal Policy: The country's fiscal policy remains expansionary in the wake of the Eurozone challenges, which should counter the strong revenue performance and keep the deficit wide at an estimated 4.8% of GDP in 2011.The 2011 budget seeks to consolidate economic recovery and improve public service delivery. In line with increased spending plans, total revenues,85% of which are from domestic sources, are projected to grow by 11.7%. Current expenditure is projected to increase by 7% to MUR72.6bn and capital expenditure by 36% to MUR11.4bn. The budget projects a fiscal deficit of 4.3% of GDP in 2011.

External Sector: A 15.7% year-on-year rise in trade deficit in the first quarter of 2011 will put pressure on the current accounts deficit projected at 9.7% of GDP. The external sector registered a trade deficit of MUR16.9bn in the first quarter of 2011, 15.7% higher than the same period last year. At MUR17.8bn, total exports during the period increased by 25.6%, buoyed by solid performance of the sugar sector, which grew by 167.1%. However, the value of imports increased by 25.6% to MUR34.7bn driven by a 63.6% sharp increase in fuel imports. External reserves remain strong at US$2.6bn in the first quarter of 2011 up from US$2.1bn,compared to the same period in 2010. The current accounts deficit should continue to widen owing to the deteriorating trade balance.

Institutional and Structural Reforms

An IMF Public Expenditure and Financial Accountability (PEFA) report for the period July 2007 to December 2010 released in the first quarter of 2011 shows strong PFM reform progress. Primary expenditure deviation from budget estimates was less than 5%. The assessment also showed that the tax, budget, procurement and audit systems were of credible quality. However, there was consistent under-spending of up to 25% on the capital account due to capacity challenges.

In line with its ambitious agenda to triple the country's US$9.2bn GDP by 2030, the GoM in June 2011 announced a multi-year US$10bn program to upgrade the country's infrastructure for greater competitiveness. Cabinet approval in June 2011 of a National Information and Communication Technology Strategic Plan (2011-2014) aimed at achieving a knowledge-based economy and a regional ICT hub. The GoM is keen to deepen trade and investment ties with Asia and act as a bridge for Africa. The first half of 2011 saw the GoM signing a MUR300mn cooperation agreement with China. Financial sector reforms are progressing with the adoption of CAMEL rating and the establishment of Islamic banking.

Donor Coordination Activities

The Bank is discussing with the World Bank to collaborate on analytical work for the remaining period of the 2009- 2013 CSP to enhance dialogue with the GoM in view of the risks facing the economy. A soft Eurozone economy, high global commodity prices and inflation present major risks to the Mauritian economy. Further hikes in the key repo rate will strengthen the local currency; reduce private sector borrowing and overall demand and stoke unemployment.

MOZAMBIQUE

Highlights

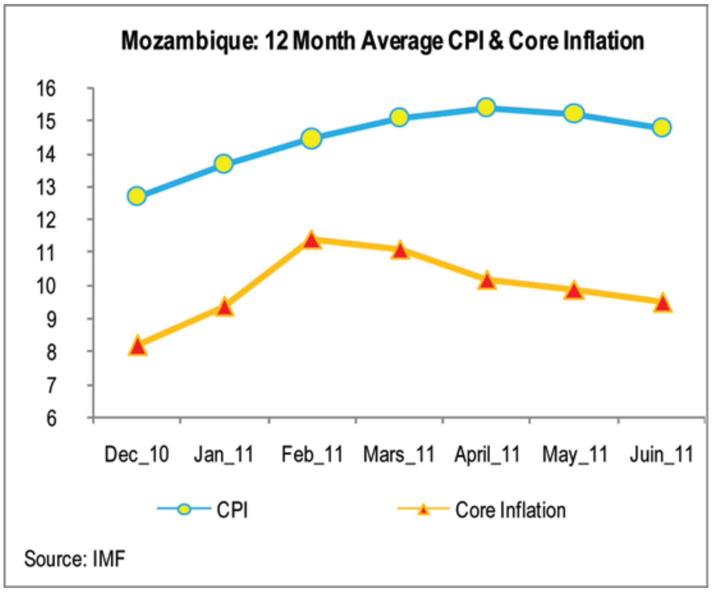
- The persistence of poverty despite consecutive years of high growth rates and bursts of social unrest have all combined to focus the government's attention on achieving social stability and inclusive growth. As a consequence, in 2011, the government has been working on the development of social safety nets, namely, the reintroduction of subsidies on selected food items. However, the cost of such a solution exceeds the budgetary capacity. Hence, the GoM is now looking into alternative schemes, potentially following the successful Brazilian "Bolsa Familia" Program.
- In June, the Maputo Headline CPI went finally below double-digit at 9.3%. However, the recently approved increase in fiscal spending and exchange rate fluctuations, in particular, a potential depreciation of the Rand, could jeopardize the inflation target of 8.4% in 2011.
- The new Poverty Reduction Strategy (PARP) released in May addresses the stagnant poverty reduction by specifically focusing on creating employment opportunities and continued human and social development. The strategy puts particular emphasis on agricultural productivity, and the creation of SMEs.

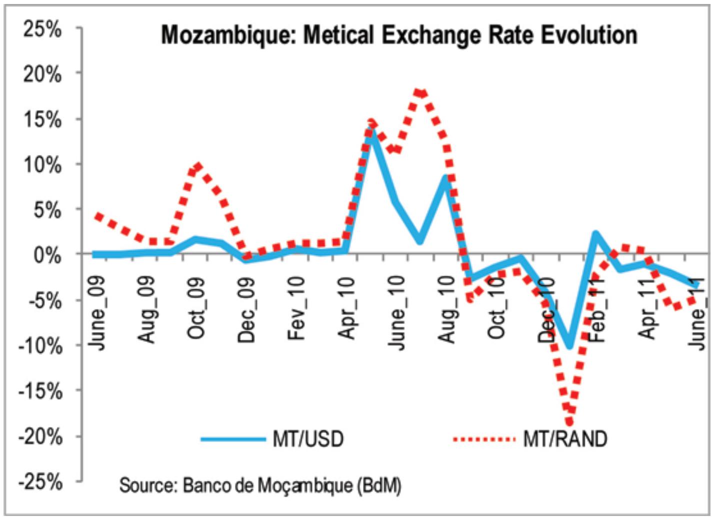
Macroeconomic Management Overview

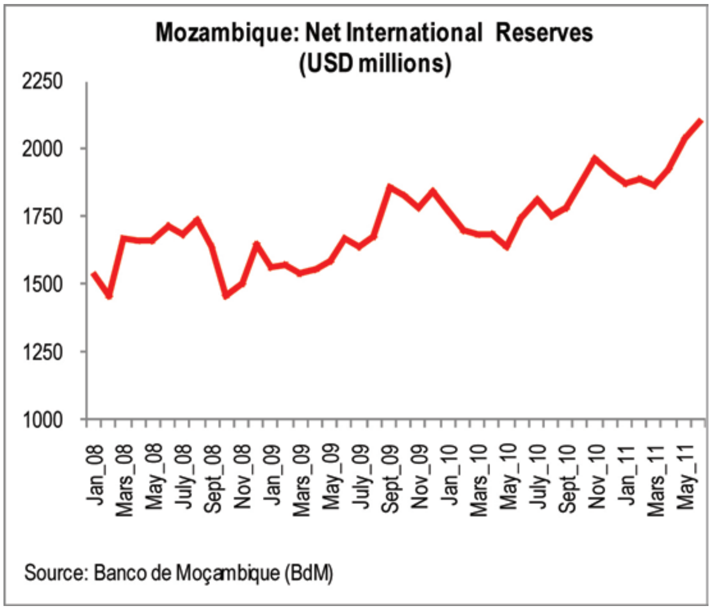
Economic Growth: The Mozambican economy showed its resilience in 2010 with a growth rate of 6.8%, a 0.5% increase over the 2009 rate. The most dynamic sectors were Transport & Communications and the Financial Sector, with growth standing above double-digit that continued into 2011.In the first quarter, overall growth was at 8.4% y-o-y, with the services sector growing by 10.7%. Even so, the key economic drivers will continue to be the inflows of foreign direct investment, particularly in the natural resources sectors; the increase in public spending, notably in infrastructure and social areas; and a dynamic agricultural sector, accounting for 25% of GDP.

Monetary Policy and Banking System: During the 2nd quarter, inflation reversed its upward trend. Maputo's year-on-year headline CPI broke the double-digit barrier at 9.3%. The reversal is supported by favourable trends in food and fuel prices, but mostly, the tight monetary policies enforced by the Bank of Mauritius (BoM) throughout 2010 and in 2011. Money supply expansion also contracted, with M3 growth declining from 13.7% in April to 12.5% in May. Moreover, credit growth declined to 17% compared to53% during the same period last year. The present policy challenge is the trade-off between constrained credit to the private sector and the control of inflationary pressures. The monetary contraction is also reflected in the appreciation of the Metical. With a recovery of 25% against the US$ (now at 28.64MT) and 21% against the ZAR (now at 4.3 MT), the currency is now approaching its pre-crisis average levels.

Fiscal Policy: Despite the programmed 6.5% fiscal deficit for 2011, almost double that of the previous year, the budget was considered to be within the objectives of a tight fiscal policy. Whereas the initial budget focused on boosting infrastructure investment, April's budget revision resulted in a deficit of 7% of GDP, reallocating resources from capital to current expenditure, mostly to support subsidies and social programs. The







increased strain on the budget poses two challenges to the government: (i) creating fiscal space through a further increase of revenue collection and (ii) designing a debt management strategy so as not to crowd out private domestic borrowers, and external non-concessional borrowing in line with its debt sustainability.

External Position: Net International Reserves, now at US$ 2,095.2 million, built steadily since January, thanks to the growth in raw materials exports, outweighing the rising import bill fueled by higher costs of oil and food. Mega-projects (mainly in Coal and Aluminum) represent 80% of goods exported. This helped to improve the country's external position. Current reserves provide a comfortable level of 5.5 months of imports coverage.

Institutional and Structural Reforms

Public Sector Management: The new Debt Management Committee (DMC) is expected to become operational in the next quarter. Until the end of 2011, the DMC should support the finalization of the second Government **Debt Sustainability Analysis**, advise on the first annual borrowing plan for 2012, and establish procedures to ensure timely and regular data provision. The Medium-Term Debt Strategy should also be approved by end 2011.

The third Public Expenditure and Financial Accountability (PEFA) assessment was completed in March with the support of the African Development Bank. The final report should be available in the 3rd quarter.

Natural Resource Management: With the Bank's support, the GoM is working on its full-fledged Extractive Industries Transparency Initiative membership and to improve the transparency of natural resource revenues. The Government is also considering options to enhance revenues from the natural resources sector.

Private Sector Reform: The implementation of the recently approved Priority Measures Action Plan for the Tax System Simplification will allow an improvement in the business environment. The program envisages the facilitation of tax payment through local banks and the lowering of transaction costs for taxpayers. The action will also strengthen the Large Taxpayers Division of the Revenue Authority.

Issues Requiring Particular Attention

Fiscal sustainability will be the prime issue for the short and medium-term. Social pressure and the ambitious development agenda will pressure for budgetary expansion. These will pose challenges for fiscal sustainability and financing of the budget deficit, especially in a scenario of slowly decreasing donor resources. Excessive public expenditure could also challenge inflation control.

Donor Coordination Activities

The G-19 (the group of 19 main donors providing budget support), found the recently approved PARP matrix to be a positive evolution over the previous one. Besides the improvement of some technical indicators, the G-19 suggested that the GoM include specific Natural Resource Management and Infrastructure Investments indicators in the PARP monitoring matrix.

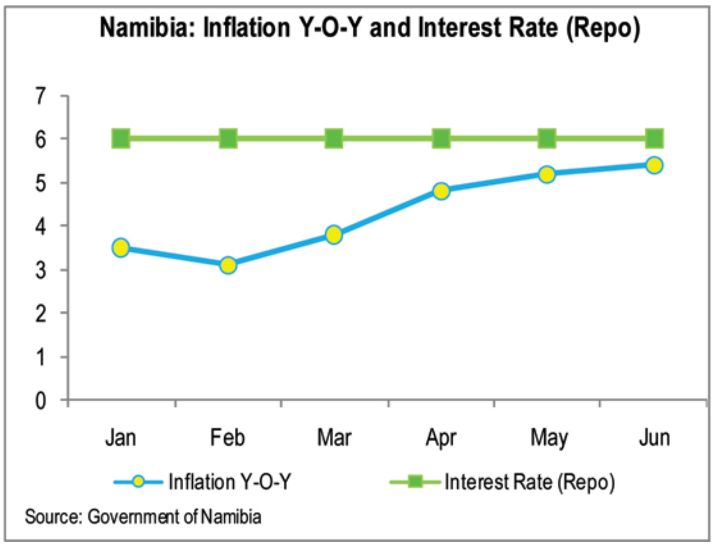
NAMIBIA

Highlights

- The Namibian economy started recovering in 2010 with a 4.8% estimated growth after shrinking by about 1.0% in 2009 due to the impact of the global economic crisis.
- Following the counter-cyclical measures in response to the global financial crisis, the country is currently facing fiscal challenges, including adjusting to the structural reduction in SACU revenues.
- Key sources of uncertainty to economic growth include the moderation of the global economic recovery, high food and oil prices and the appreciation of the Namibian dollar.
- High levels of unemployment (51%) and inequality (Gini Coefficient of 0.74) pose additional risks to the existing stable social and political environment.

Macroeconomic Management Overview

Economic growth: The economy rebounded from the negative impact of the global financial crisis, with real GDP estimated to have grown by 4.8% in 2010, boosted by stimulus measures pursued by the government since 2009 and higher mineral prices. Strong performance was registered in the primary sector (19%), while growth was moderate in both the secondary (3.9%) and tertiary (3.5%) industries. Real GDP growth is expected to slow down to 4.1%, reflecting the moderation of mining and agricultural activities, which were affected by flooding and above average rainfall, respectively. In 2012, real GDP growth is projected to increase to 4.6%,as demand for minerals continues to grow, commodity prices will remain strong.



Monetary Policy and Banking System: Annual inflation registered a downward trend from 2009, falling to 3.1% in 2010 in tandem with trends in South Africa, the source of the bulk of Namibia's imports. However, inflationary pressures have since started building up with year-on-year inflation accelerating to 5.4% in June 2011 due to rising food and fuel prices. Consistent with overall economic conditions, the Bank of Namibia's Monetary Policy Committee continued to pursue an expansionary monetary policy and decided to maintain the Repo rate unchanged at 6% in April 2011.

Namibia's exchange control regime is administered in the context of the Common Monetary Area Agreement. Hence, the Namibia dollar has undergone considerable volatility in the past few months, in line with the South African rand to which it is pegged at par. It appreciated to N$6.6 vis-à-vis the U.S. dollar in early January 2011, its strongest rate since November 2007, but fell to N$7.3 in mid-February as political events in North Africa eroded investors' confidence in emerging markets. It has rallied since then to N$6.8 in June 2011.

Fiscal performance: The budget for 2011/12 aims at creating 104,000 jobs over the next three fiscal years, by focusing spending on four sectors (agriculture, transport, tourism, and housing and sanitation). Total revenue and grants as a proportion of GDP fell by 4.5 percentage points to 25.2% of GDP in 2010/11 and is expected to increase slightly by 3.5% in 2011/12 in spite of the fact that Southern African Customs Union (SACU) revenues, which contributed about 30% to Namibia's total government revenue in 2010/11, will remain low. An increase in total expenditure by 7 percentage points to 38.3% of GDP in 2011/12 is expected to lead to the expansion of the fiscal deficit to 10.3% of GDP in 2011/12 from 1.1% in 2010/11. The deteriorating fiscal balance reflects the government's expansionary fiscal policy to counteract the effect of the global economic crisis and the structural reduction in SACU revenues emanating from the sluggish global economic growth. The deficit is expected to be financed by domestic borrowing and, to a lesser extent, foreign debt. It is projected to narrow to 7.2% of GDP in 2012/13 and 6.9% in 2013/14.

External sector: The current account deficit (including official transfers) is expected to deteriorate to 5.7% of GDP in 2011 from 2.2% in 2010, as the trade deficit widens. While the appreciation of the Namibian dollar in 2011 is expected to boost imports, export earnings are unlikely to grow at the same rate. Movements in the current account are expected to continue to be strongly influenced by dynamics in Namibia's share of SACU receipts, which are expected to drop in 2011. With Namibia persistently running a deficit in the capital and financial account, the overall balance of payments is expected to remain in a deficit in 2011. However, Namibia's gross reserves are expected to remain relatively unchanged at about 3.5 months of imports in 2011.

Namibia's debt levels remained sustainable and significantly below the 30% of GDP threshold, despite the expansionary fiscal policy. The total public debt stock is expected to reach 27.4% of GDP in 2011/12, 4.3% of which is foreign, up from 20.1% in 2010/11. Public debt increased by 6.6% to N$13.8 billion in the first quarter of 2011/12. The cost of servicing the debt is estimated at N$1.8 billion in 2011/12.

Institutional and Structural Reforms

Public Sector Management: The Government has stepped up efforts aimed at improving governance institutions and mechanisms in the country. In the area of public financial management (PFM), capacity building programmes are being undertaken with the objective of improving the effectiveness and efficiency of PFM in order to further promote fiscal transparency and accountability. An integrated tax management system is being developed in order to simplify the tax administration. In order to enhance the public procurement system, the cabinet approved the new Tender Board Bill, which is expected to be tabled in Parliament this year. A number of other bills have also been submitted for consideration by the cabinet, including: (i) the Namibia Trade Board Bill aimed at incorporating the SACU agreement into Namibian law; (ii) the Audit bill that deals with the appointment and conditions of service of staff of the Office of the Auditor-General, as well as administrative matters pertaining to this office; and (iii) the State Finance Amendment Bill, to remove audit issues, including the powers, duties and functions of the Auditor-General, from the State Finance Act through the proposed Audit Bill.

Private Sector Reform: The cabinet approved the 2010-2020 Financial Sector Strategy, whose main objective is to develop a more resilient, competitive and dynamic financial system. The strategy aims at addressing a wide range of issues, including limited competition, punitive banking charges, limited access to financial services and low participation of Namibians in the banking sector. The Government is in the process of amending the Pension Funds Act and the Long-Term Insurance Act in order to facilitate the smooth implementation of regulations that oblige portfolio investors (Pension Funds and Insurers) to invest at least 35% of their assets locally in order to curb capital outflows, estimated at N$37.7 billion in 2009 and N$27.4 billion in 2010.

Trade Facilitation: The Minister of Works and Transport requested Parliament to ratify the memorandum of understanding (MoU) on the development of the Walvis Bay-Ndola-Lubumbashi Development Corridor. The multi-modal transportation corridor, spanning Namibia, Zambia and the DRC, aims at facilitating the movement of goods and people and has the potential to benefit Namibia through the port of Walvis Bay, which would have to be upgraded to cope with increased trade. The MoU has already been approved by the cabinet.

Issues Requiring Particular Attention

The downside risks for the economic outlook include the uncertainty in global commodity prices in view of the moderation in global economic recovery. A sustained appreciation of the Namibian dollar could also reduce Namibia's competitiveness and hamper economic growth.

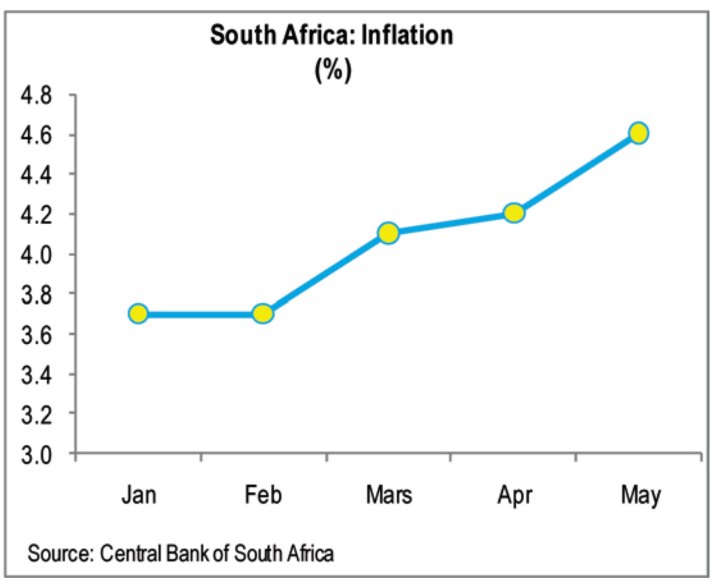
SOUTH AFRICA

Highlight

- South Africa has continued with counter-cyclical fiscal and monetary policy stances, but gradually withdrawing the fiscal stimulus. However, growth momentum continues to be weak, highlighting the risk that South Africa is lagging behind other emerging economies in economic recovery.
- The ascendance of South Africa into the BRIC group of fast growing emerging economies spurs its geopolitical importance as a gateway of foreign investment into the continent. However, the recent surges in short term capital inflows into the country raised concerns about external competitiveness, financial stability and sterilization cost of reserve accumulation.
- Regionally, South Africa will, in the medium term, benefit from the proposed Tripartite Free Trade area covering SADC, COMESA and EAC. Yet sluggish recovery and sovereign debt crisis in the Eurozone, coupled with recent political instability in the Middle East and North Africa, present short term downside risk to growth and recovery.

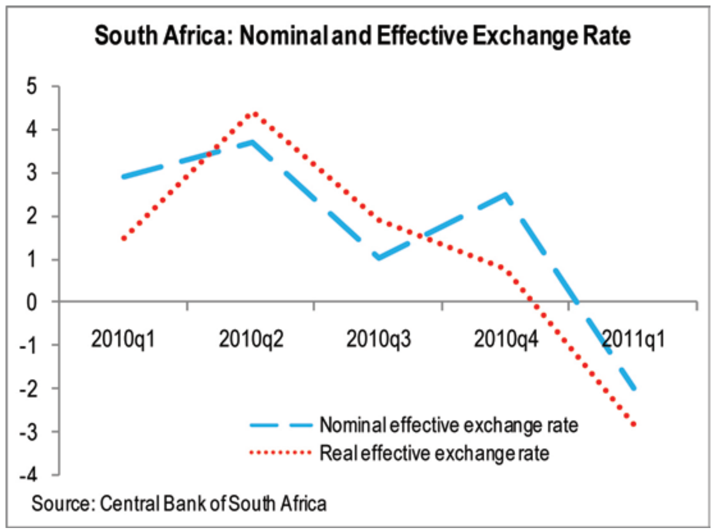
Macroeconomic Management Overview

Economic Growth: Structural challenges such as inadequate infrastructure and capacity, and persistently high levels of unemployment constrain the economy from achieving 6-7% growth. Economic activity gained momentum in the first quarter of 2011, with real gross domestic product expanding at an annualized rate of 4.8%. Growth was driven primarily by an increase in manufacturing activity, which expanded by nearly 15%. On the demand side, growth was anchored by rising real final private consumption expenditure which was, in turn, driven by rising real income, lower interest rates, modest reduction in household debt ratio and improved consumer confidence. In April, manufacturing sales index increased marginally while the production index declined to 102.7 from 105.1 in March 2011, implying that growth may slow during the second quarter.



Monetary Policy and Banking System: The main priority of the central bank during the quarter was currency stabilization, primarily through reserve accumulation. Inflation rose to 4.6% in May 2011 due to higher food and fuel prices, but remained well within the policy target range of 3-6% (see Figure 1). The main risks to inflation outlook remain food and administered prices, particularly oil prices due to supply shocks related to geo-political events in the Middle East and North Africa. Despite the relaxation of exchange controls, the rand continued to appreciate fluctuating between 6.71 and 6.85 per US dollar during the second quarter of 2011. Two main factors contributing to the strengthening of the rand were high levels of short-term capital inflows of about R20.8 billion during the first quarter of 2011 and the depreciation of the US dollar against the Euro.

Broad money supply (M3) growth declined from 8.2% in January to 6.0% in April 2011while growth in quasi-money (M2) fell from 6.67% in January to 4.77% in April and to slightly rise to 5.46% in May. The slow growth both in broad and narrow money supply partly reflects sluggish demand for domestic credit (see Figure 2 below).



Fiscal Policy: South Africa's adoption of counter-cyclical fiscal policy prior to the 2008-2009 crisis helped the economy to rapidly rebound from the recession and grow by 2.8% in 2010. The primary deficit was 1.8% of GDP while the overall deficit was 4.5% of GDP for the fiscal year that ended on March 31, 2011. Public expenditure rose by 10% year-on-year in 2010/11 fiscal year while its share fell to 28.6% of GDP for the same period compared to 29.2% during the previous year. In spite of the improved revenue collection, the rising wage bill, accounting for 55.7% of the total tax revenue during 2010, has become a major concern.

Total tax revenue for the fiscal year that ended on March 31, 2011 was R656 billion while total national expenditure was R785 billion. About 97% of the national government deficit of R126.9 billion was financed from domestic borrowing.

Balance of Payments: Trade deficit reached R2.4 bn in April from a surplus of R0.97 bn in March 2011. The current account deficit increased to 3.1% of GDP during the first quarter of 2011 from 1% in the previous quarter due to faster growth in imports and sluggish growth in exports.

Major exported items included metals, minerals and other commodities. Foreign direct investment declined by 80% in 2010 to a mere US$1.3 bn compared to nearly US$6 bn in the previous year while reserve accumulation reached an all-time high of US$50 bn in June 2011 covering over 19 months of import (see Table 1).

The rand nominal effective exchange rate declined by 3% from the end of March to the end of May 2011 partly due to further risk aversion to weakness in the US dollar following concerns over the US sovereign debt outlook (see Figure 1). On the other hand, the rand year-on-year real effective exchange rate increased by 2.5% at the end of the first quarter, signifying a marginal loss in the competitiveness of South African firms involved in the production of exportable goods.

Institutional and Structural Reforms

South Africa ranked 27th in intellectual property protection and 29th in property rights globally based on the GCI 2010-2011 report. The country's financial market development is impressive, ranking 9th globally during the same period. The new public procurement rule introduced during this quarter underpins the government's determination to stem out corruption and improve efficiency in service delivery. While South Africa performs well in terms of "Ease of doing business", ranked 34th globally in 2010, it does not fare well in terms of trading across borders and registering property. Human development remains another major challenge. South Africa's university enrolment rate was only 15%, which places it at 99th globally according to the GCI 2010-2011 report. Infrastructure deficit, low capacity and high unemployment remain major structural bottlenecks to growth.

Issues Requiring Particular Attention

The key challenge for the country is the high level of unemployment which currently stands at 25%.Out of the 32 million working age population, only about 13 million people (40%) are employed while 50% of the youth is unemployed. The New Growth Path (NGP) strategy aims to create 5 million jobs in the coming ten years through enhanced investment in 5 key sectors, skills development, improve public service delivery, and enhance regional economic integration. The Bank's future operations should therefore be underpinned by the NGP strategy for enhanced visibility and impact.

Donor Coordination Activities

Bank interventions in South Africa are closely coordinated with major interventions of other multilateral donors. The Bank's biggest operation in South Africa, the Medupi power project, is financed in collaboration with the World Bank and Export Credit Agencies while the renewable energy project is a joint initiative of the Clean Technology Fund, IBRD, the AfDB and the government.

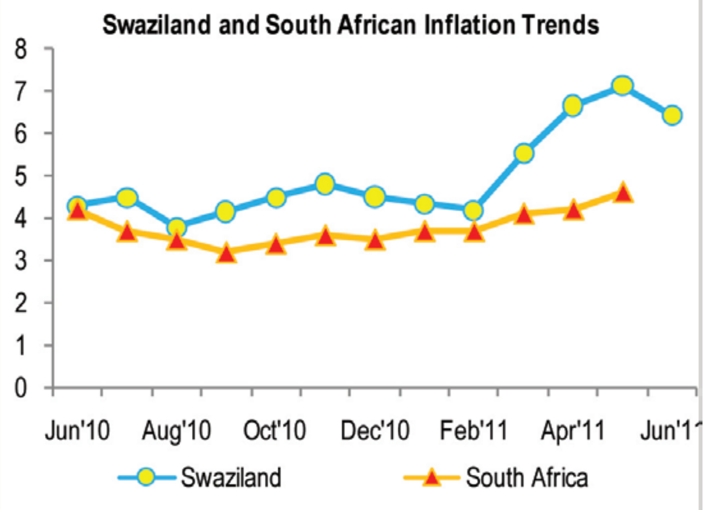
SWAZILAND

Highlights

- In spite of the relatively stable political environment in Swaziland, increasingly recalcitrant trade unions and allegedly informal political opposition groups are demanding the freeing up of democratic space, government transparency, a crackdown on perceived corruption and equitable sharing of the burden of adjustment necessitated by the fiscal crisis.
- Swaziland's weak institutional structures and capacity constraints are slowing reform implementation. Invariably, the slow reform process is worsening the fiscal crisis and threatening continued delivery of government services and macroeconomic stability.
- The yet to be agreed revision of the Southern African Customs Union (SACU) revenue sharing formula is likely to result in a permanent reduction in revenues to Swaziland, which highlights the imperatives for fiscal reform.

Macroeconomic Management Overview

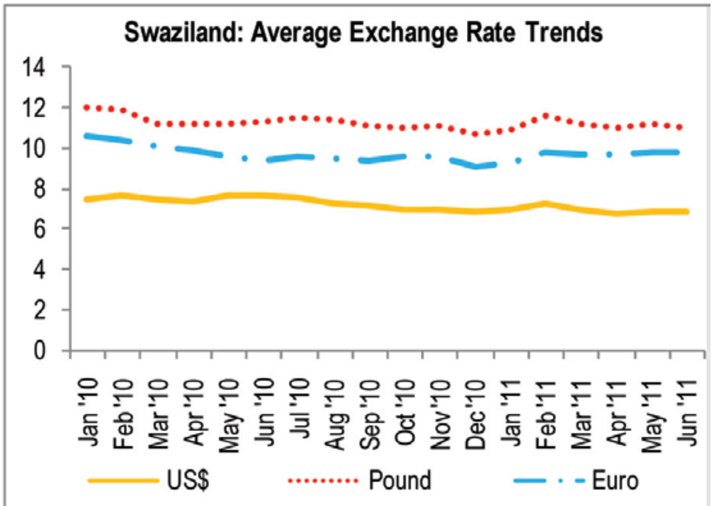
Economic Growth: Swaziland is expected to record real GDP growth of less than 1% in 2011. Overall, the country has been in a low growth trap over the past decade, compared to other member countries in the Sothern African Customs Union (SACU). A combination of low foreign direct investment and reduced government expenditure due to the fiscal crisis largely account for the reduced growth in 2011. Downside risks for negative growth exist unless government quickly addresses the fiscal crisis and avoid further closures of small businesses and stem a domino effect onto the retail and financial sectors. However, the Central Bank estimates that growth in agriculture, manufacturing and tourism sectors will be sufficient to avoid negative growth.



Source: Central Bank of Swaziland and Central Bank South Africa

Monetary Policy and Banking System: In sync with regional trends, inflation is edging upwards, increasing from 5.5% in March to 7.1% in May 2011, largely driven by food and fuel prices. This trend is in stark contrast to the steep decline in inflation from 12.6% at the end of 2008 to less than 5% by end of 2010. Given that policy interest rates were maintained at 5.5% while domestic credit expansion is weakening, as banks become more cautious in the face of a sharp increase in non-performing loans (up by more than 300% between January and June 2011), inflationary pressures will likely be limited to administered energy prices and the depreciation of the lilangeni against the United States (US) dollar.

Domestic credit contracted by almost 1% in May compared to April 2011, with net claims on government increasing by 5.4% over the same period. On a year-on-year basis, the lilangeni has appreciated by about 12.7% and 2.5% against the US dollar and the Euro, respectively, but depreciated by 4.3% against the pound by the end of June 2011. However, the lilangeni is beginning to show signs of weakness against the US dollar due to the continued sovereign debt crisis in the Eurozone. On the other hand, money supply growth was depressed, with broad money (M2) and narrow money (M1) having contracted by 3.6% and 4.5% between February and May 2011, respectively.



Source: Central Bank of Swaziland

Fiscal Policy: Government budgeted for a 3.5% increase in nominal expenditure in 2011/12 compared to 2010/11, only to be reduced by 14%. A second review of expenditures is underway as the government has failed to secure external financing for the deficit, estimated at 13% in 2011/12, compared to 7.5% in 2010/11. Moreover, the loss of confidence by the private sector is making it difficult to raise domestic financing. On the other hand, revenues declined by about 25% in 2010/11 compared to 2009/10, while revenue collection during the first two months of the current fiscal year amount to 16% of the previous year. While acknowledging the seasonality in revenue collections and the teething problems of the recently established Swaziland Revenue Authority, it is important that extra efforts be made to realign expenditures to revenue collection if fiscal sustainability is to be maintained.

Balance of Payments: Faced with the cash flow problem, government ran down foreign reserves by 39.5% over the year to May 2011. Therefore, there is a potential risk to the maintenance of the parity between the lilangeni and the rand if the government were to further use foreign reserves to finance its expenditures. The government, however, acknowledges the risks associated with any further drawdown on foreign reserves and has restrained itself from doing so. Swaziland will, however, continue to face balance of payments pressures in view of the estimated current account deficit of 18.5% of GDP in 2011 and poor recovery in foreign direct investment inflows.

Institutional and Structural Reforms

The government is finalizing the Economic Recovery Strategy (ERS) which is expected to spur greater private sector participation in economic activities. The ERS aims to lift annual economic growth to 5% and create at least 30 thousand jobs by 2014 by restoring investor and consumer confidence, structural reforms, infrastructure development, human capital investments and macroeconomic stability. Moreover, private sector activities are limited due to a poor business environment. The 2011 World Bank "Ease of Doing Business" Report ranks Swaziland at 118, down from 115 in 2010.Thegovernment accounts for 40% of GDP, with public enterprises accounting for another 8% of GDP.

There are key challenges to realizing the objectives of the ERS. Bills needed to implement critical reforms are still to be approved by parliament. Moreover, the weak institutional and capacity constraints pose additional challenges for reform implementation. In addition, Swaziland faces high levels of poverty, estimated at 63% of total population; high unemployment and the highest prevalence of HIV/AIDS in the world.

Issues Requiring Particular Attention

Whereas the government committed itself to ring-fencing health and education expenditures, with a view to reducing the impact of the fiscal crisis on the poor, stocks of drugs and medicines have fallen to two-month levels against the preferred four-months due to non-payments to suppliers. This development could put the 64 thousand people on ARV treatment at risk of disrupting their treatment regime. In education, the second term payments for Free Education grants to schools have not been effected, resulting in primary schools facing operational challenges.

Donor Coordination Activities

While donor activity in Swaziland is limited, due to its lower middle-income status, there has been strong cooperation on HIV/AIDS and the fiscal crisis has made it imperative that donors coordinate their operations more closely in support of urgent reforms and provision for financial assistance. Together with the IMF, World Bank and the European Union, the Bank is considering support for public financial management reforms by providing budget support and technical assistance through the Middle Income Countries (MIC) Grant Trust Fund.

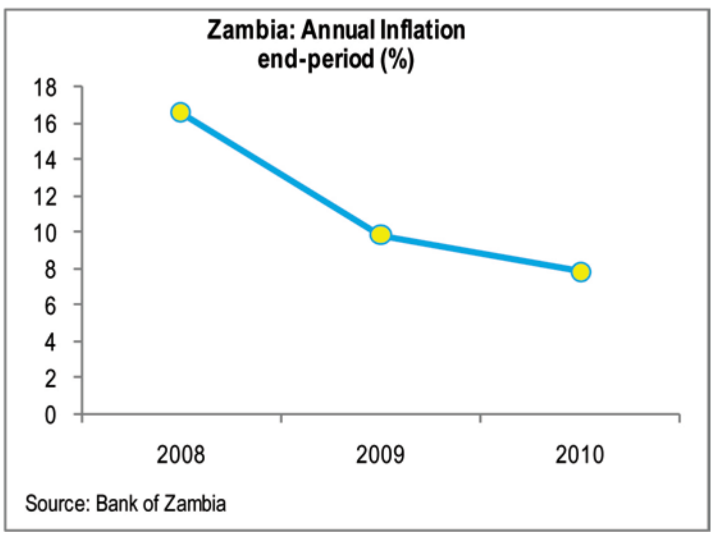
ZAMBIA

Highlights

- Preparations for the forthcoming tripartite general elections appear to be progressing smoothly. The Electoral Commission of Zambia is also in the process of compiling the final Voter Register following the verification exercise which ended on 12 June 2011.
- Zambia was in mid-July 2011 reclassified by the World Bank to a lower middle income country status, following continued sound macroeconomic performance for an extended period of more than six years. GDP per capita increased to US$1.151 in 2010 compared to US$ 349 in 2001.
- Persistently high levels of rural and urban-poverty, widening income inequality and a rather slow pace of economic diversification are the key challenges.

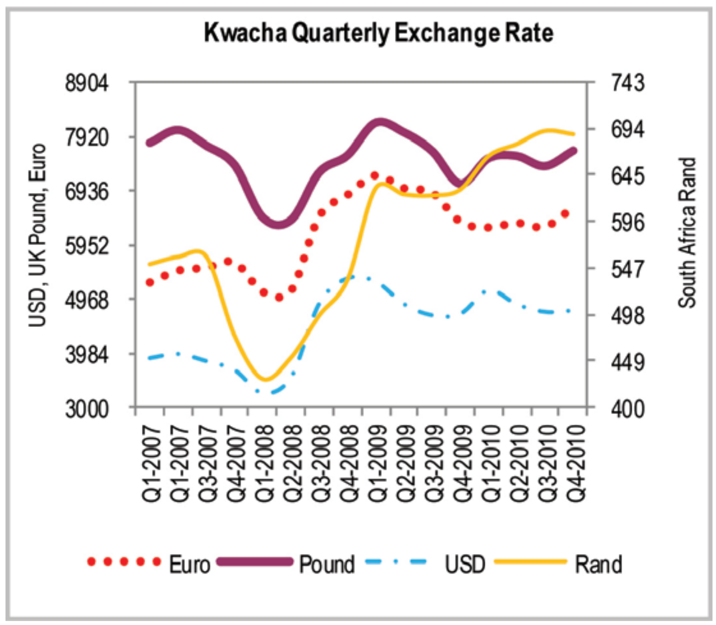
Macroeconomic Management Overview

Economic Growth: In 2010, real GDP growth out-turn was 7.6%, up from 6.3% in 2009.Zambia's growth continues to be driven, in large measure, by the huge mineral reserves, especially increasing copper output as new mining projects have come online. Agriculture is another key component of the economy, particularly in terms of employment and food production. Maize output is projected to increase by 8% to 3.02mn tonnes in 2011. Economic growth prospects remain strong in the outlook period, with growth projected to be 6.8% for 2011.



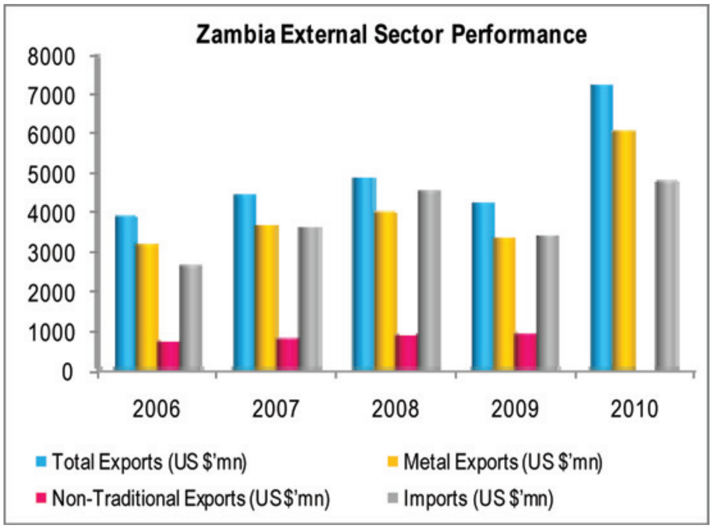
Monetary Policy and Banking System: Zambia's monetary policy objective continues to focus on achieving single digit inflation (2011 target being 7.0%). It is envisaged that in the second half of 2011, reserve and broad money growth rates may not exceed 4.0 % and 5.5 %, respectively. However, the Bank of Zambia faces challenges in fighting inflation due to: (i) higher production costs because if of the 25.5% upward adjustment in electricity tariffs effected in August 2010; (ii) increased transportation costs arising from higher fuel prices after the price adjustments made following the implementation of the Uniform Petroleum Pricing (UPP) mechanism, effective September 2010 and worsened by the increase in global oil prices; (iii) higher than programmed growth in reserve money and broad money on account of increased government borrowing and spending largely to finance maize purchases following the bumper harvest; and (iv) seasonal price increases of beef products, kapenta, fresh fish and fresh vegetables, due to low seasonal supply. However, the above challenges were partially mitigated by improved supply of maize and other foodstuffs in the second quarter of 2010 and the pass-through effects of the appreciation of the Kwacha against the US dollar during the second half of 2010.

Zambia continues to administer a floating exchange rate regime and its foreign reserves were recorded at US$2.1 billion at end of 2010. Copper continues to dominate foreign exchange earnings – 55% of total. The kwacha has also been remarkably stable over the course of the past few months and this trend is expected to continue in the short term. Between June and July 2011, the currency traded at an average of ZMK4, 775/ US$, a level at which it has lingered with relatively little deviation since the beginning of 2011. The kwacha will continue to be supported by increasing production of copper, and sustained high international prices. Major risks include; i) the processing and outcome of the forthcoming tripartite elections, and ii) economic developments in the world's largest metal consumers, particularly China.



Interest Rates have come down with average lending rates standing at 26.2% in March 2011 from 54.5% in 2001. But the overall reduction has not been in tandem with the fall in inflation and yield rates on government securities. Measures employed to reduce interest rates have included a reduction in the Statutory Reserve Ratios from 14% in 2007 to 8%in 2010, containing inflation to single digit levels, the establishment of the credit reference bureau, and Government prudent fiscal policy.

Fiscal Policy: Over the past few years, the budget deficit position has progressively declined, reaching 2.2% of GDP in 2010. The fiscal stance continues to be characterized by prudent budget execution, accompanied by higher government revenues. Government has increased investments in health, education and infrastructure development, gradually reducing dependence on donor funding and relative improvement in poverty and human capital development. However, there is a need for caution as the Government prepares to tap into the sovereign bond market to finance capital spending. Stronger debt and liquidity management capacity will be critical in this process. In addition, recent consecutive bumper crop harvests have revealed the limitations of the current maize pricing and marketing system.



External Sector: Improved external sector performance due to both increasing mining revenues and reduced import requirements in view of the maize bumper harvests is foreseen in the outlook period. Gross international reserves were equivalent to 4 months of import coverage in 2010 and the trade balance surplus was recorded at US$2 billion in 2010.

Institutional and Structural Reforms

Public Sector Management: Zambia has embarked on a number of key public sector management reforms including decentralization, Public Financial Management, and Pay and Pension Reforms. These reforms are at various levels of implementation. Other reforms include the Single Treasury account and a number of anti-corruption measures.

Private Sector Reforms: Within the framework of the Private Sector Development Strategy, Zambia recently passed and enacted a public-private sector law and it is also putting in place a special Public-Private-Partnerships Unit. Zambia's overall rating in the 2011 World Bank's "Doing Business" Report shows remarkable improvement, rising from 84 to 76 in overall ranking, signaling a better business climate for private sector development.

Donor Coordination Activities

The Bank is preparing to play a lead role in the Cooperating Partners Group (CPG), ii) the Agriculture, Livestock and Fisheries Cooperating Partners Working Group, iii) the Water Supply and Sanitation Cooperating Partners, and Transport Cooperating Partners working Group. The Bank is also preparing to sign onto the second Joint Assistance Strategy for Zambia (JASZ.II), covering the period 2011-2015, the Memorandum of Understanding for the Zambia Poverty Reduction Budget Support and that of the Public Expenditure Management and Financial Accountability Programme (PEMFA). In addition, the Bank has identified three lending operations for co-financing. These include i) Itezhi-Tezhi Hydro Power Project, ii) Kazungula Bridge construction, and the fourth Poverty Reduction Budget Support Programme. On the non-lending side, the Bank is collaborating with Norway, the IMF, and the World Bank on a key study- Zambia Domestic Resource Mobilization Potential.

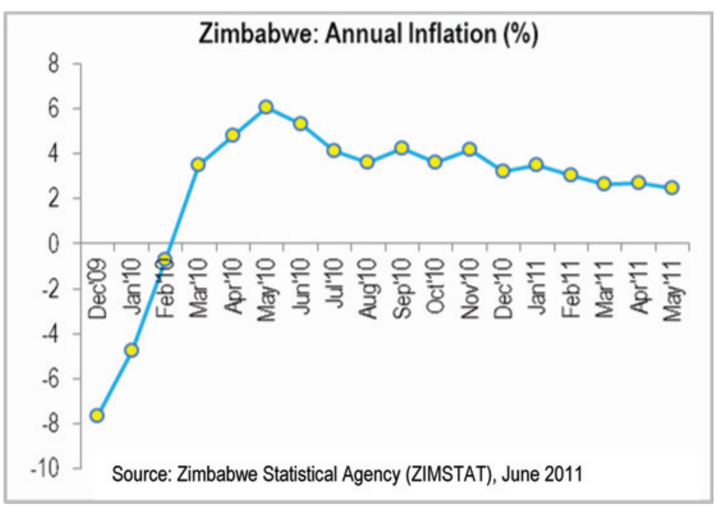
ZIMBABWE

Highlights

- The implementation of the Global Political Agreement (GPA) signed in 2008 continues to be slow and progress has been mixed. A recent Summit of the Organ Troika[8] on Politics, Defense and Security of SADC noted that the polarization of the political environment was characterized by the resurgence of violence, arrests and intimidation in the country. A new roadmap towards free and fair elections is being negotiated by the GPA principals and is scheduled to be presented to the next SADC Summit in August.
- While Macroeconomic stability has been restored and real GDP growth for 2011 is projected at some 7.8% in 2011, the medium term economic outlook for Zimbabwe will be largely determined by political developments and key reforms aimed at improving the investment climate, especially in the areas of property rights, indigenization, and land reform.
- In addition, external indebtedness remains challenging and the speed and determination with which the government addresses it will be vital, as this will unlock critical resources required for investment in various sectors of the economy, especially in the infrastructure sector.

Macroeconomic Management Overview

Economic Growth: The African Economic Outlook projects that the Zimbabwean economy will grow by 7.8% in 2011 underpinned by increased mineral and tobacco production. The mineral sector continues to benefit from favorable international commodity prices for gold, nickel, platinum, and chrome ore, on the back of expanding global commodity demand. Similarly, increased tobacco, cotton and sugar output is projected to spur agricultural sector recovery. Over January-June 2011, industrial capacity utilization averaged 47-50%, which is an improvement from an average of 40-45% by the end of 2010. Industry however continues to face challenges such as limited access to domestic and off-shore lines of credit to finance re-tooling, while frequent power outages and high costs of capital are among other constraints.

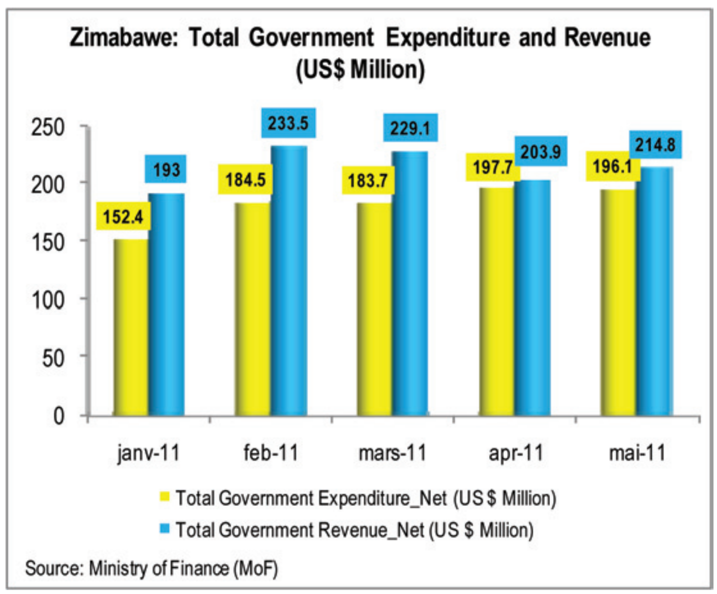


Source: Zimbabwe Statistical Agency (ZIMSTAT), June 2011

Monetary Policy and Banking System: Zimbabwe continues to operate a multi-currency regime (which was adopted following the hyperinflation of 2008), along with cash budgeting. The currency and the fiscal regime has helped to restore and maintain price stability as they have become agencies of restraint on government, ensuring discipline in budgetary execution—as there is no recourse to deficit financing.

Annual inflation marginally declined from 2.7% in April 2011 to 2.5% in May 2011. The decline in annual inflation was underpinned by low food and non-food inflation, which stood at 2.3% and 2.6%, respectively. At current levels, the country remains on course to achieve the 4.5% inflation rate targeted for the end of the year. On the other hand, month-on-month inflation remained constant at the 0.1% level achieved in April 2011.

Annual money supply (M3) growth, defined as total bank deposits increased by 49.2% in May 2011. On a monthly basis, M3 growth increased by 5.1% in May 2011, compared to 0.9% in April 2011. Money supply growth is underpinned by improved bank deposits and increased bank lending. Annual total banking sector deposits, net of inter-bank deposits, increased by US$0.9 billion (49.18%) from US$1.83 billion in May 2010 to US$2.73 billion in May 2011. The composition of the deposits, the bulk of which are demand and short-term deposits is, however, unfavorable for long-term investment.



Source: Ministry of Finance (MoF)

Fiscal Policy: Over the January-May 2011period, the government realized net revenues amounting to US$1,074.4 million, marginally surpassing the target of US$1,031.3 million. On the other hand, net expenditures of US$914.4 million, were contained within the planned target of US$956.7 million. Accordingly, a cumulative surplus of about US$160 million was registered. However, given subdued civil service salaries and wages and growing wage demands, the surplus realized over the January to April 2011period, is somewhat artificial. In view of outstanding obligations in the period of analysis, the surplus is likely to be wiped off during the remainder of the year. Of the net government revenue, tax revenue contributed US$985.7 million while non-tax

8 Namibia, Mozambique and Zambia

revenues contributedUS$88.6 million. On the expenditure side, current and capital outlays contributed US$836 million and US$55.2 million to net government expenditures, respectively. In this context, the recent increase in public sector wages, if not supported by a continuous transfer of diamond revenues to the tune of US$42 million a month, would place the country's finances in a precarious position.

Balance of Payments: Merchandise exports increased significantly by 56.3% from US$1,246.4 million over the January to June 2010 period, to US$1,948.5 million over the corresponding period in 2011. Improved export performance in the first six months of 2011 was spurred by favorable terms of trade and growing commodity demand from emerging market economies, particularly China and India. Similarly, imports increased by 11.5% from US$2,595.1 million over January-June 2010 to US$2,894.0 million over the comparable period in 2011. The rising import bill is attributed to attendant supply gaps in the Zimbabwean economy, which are currently being augmented by the importation of finished goods. The recovery in industrial production has also resulted in the concomitant absorption of intermediate inputs, machinery, raw materials as well as spare parts.

Institutional and Structural Reforms

A Country Integrated Fiduciary Assessment (CIFA) with assistance from development partners to provide an integrated and holistic assessment of the Public Financial Management System (PFMS) was recently conducted in Zimbabwe. In addition, a report on the Observance of Standards and Codes (ROSC) focusing on Accounting and Auditing Assessment (A&A) has also been undertaken. The main purpose of the ROSC assessment was to assist the Zimbabwean government in strengthening the private sector's accounting and auditing practices and in enhancing financial transparency in the corporate sector.

Zimbabwe has eased business start-up by reducing registration fees and initiated a process to speed up the *name search* process and company and tax registration. In addition, the corporate income tax rate was reduced from 30% to 25%, the capital gains tax was lowered from 20% to 5%, and the payment of corporate income tax was simplified by allowing quarterly payment through commercial banks.

Zimbabwe has made relative progress in a number of key MDGs such as universal primary education. Enrolment in primary schools has consistently been relatively high (with a net enrollment ratio of 91% in 2009 down from 98.5% in 2002). The rate of HIV infection has also seen an improvement with a decline from 16.1% in 2007 to 13.7% by 2009 due, in part, to public awareness programs and education. However, Zimbabwe has experienced a decline in areas such as access to safe drinking water. The rural population with safe drinking water declined from 70% in 1999 to 61% by 2009.

Issues Requiring Particular Attention

The key issues that require attention in Zimbabwe are (i) dealing with external debt arrears, improving the investment climate with regards to clarity on the issue of indigenization, property rights and rule of law, reining in wage expectations, improving transparency in the reporting of diamond revenues, and agreeing a roadmap for holding free and fair elections.

Donor Coordination Activities

The Bank is coordinating with other donors in various activities, including Public Financial Management, Debt Management, Statistics, the Zimbabwe Multi Donor Trust Fund (ZIMFUND), and Water and Sanitation.

III. SPECIAL THEME: ZIMBABWE-REFORMS FOR PRIVATE SECTOR PARTICIPATION IN INFRASTRUCTURE DEVELOPMENT

III. SPECIAL THEME: ZIMBABWE-REFORMS FOR PRIVATE SECTOR PARTICIPATION IN INFRASTRUCTURE DEVELOPMENT[9]

Rehabilitation of Infrastructure is Critical to Zimbabwe's Economic Take-off

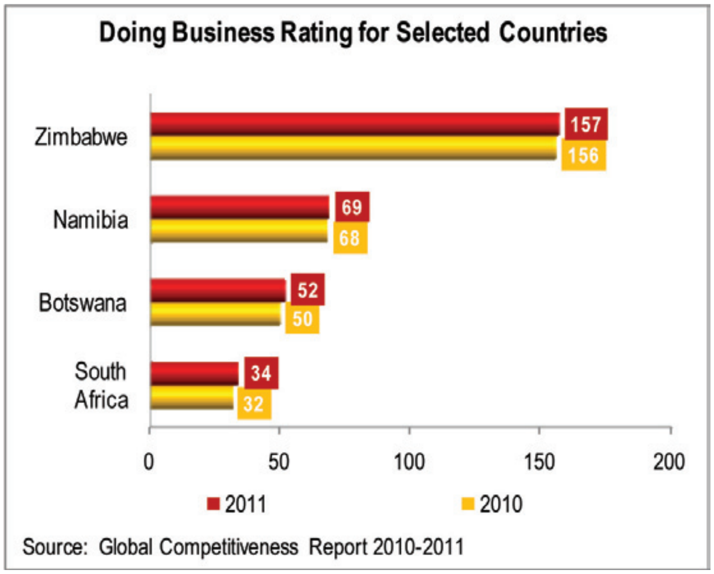
The large backlog of rehabilitation and periodic maintenance of infrastructure pose a serious constraint on economic take-off, especially given the limited public financial resources. Consequently, there has been a renewed interest in mobilizing private investment for this purpose. Sustaining and improving the quality and quantity of infrastructure services in the decade ahead will require a substantial increase in private investment in power, railways, roads, civil aviation, and information communications technology. The Bank's report, "Infrastructure and Growth in Zimbabwe, an Action Plan for Sustained Economic Growth", estimates the total amount of private investment in infrastructure at about US$4.6billion (at 2009 constant prices). However, the mobilization of this amount of private funding presents a major challenge for the country. Measures encompassing there structuring of parastatals and the adoption of key policy initiatives to improve the regulatory environment, including Public-Private Partnerships (PPPs), are prerequisite to a successful outcome in this regard.

The Mobilization of Private Investment Faces Major Challenges

According to the World Bank 2011— "Doing Business Survey" Zimbabwe ranked 157 out of 183 countries worldwide, two positions up compared with the 2009 ranking. Its ranking however is still well below those of neighboring countries. The legal and institutional framework for public enterprises continue to constraint their effectiveness, autonomy, and accountability.

Another area of concern relates to the Indigenization and Economic Empowerment Regulations that became effective on 1 March 2010. The law requires foreign firms with a value in excess of US$500 to have more than 50% of their equity held by indigenous persons within five years (that is, by 1 March 2015). This Regulation was met with some apprehension among local and international investors due to earlier experience with land reform. There are concerns within the private sector that foreign–owned businesses could be ceased without compensation under Zimbabwe's indigenization law. The Zimbabwe government, therefore, needs to rebuild its image and demonstrate a commitment to upholding the rule of law and respecting property rights, as well as avoiding to send out mixed signals to investors.

Despite the mixed signals, the government is taking steps to improve the business climate. Zimbabwe has eased business start-ups by reducing registration fees and initiated a process to speed up the name search process and company and tax registration. In addition, the corporate income tax rate was reduced from 30% to 25%, the capital gains tax was lowered from 20% to 5%, and the payment of corporate income tax was simplified by allowing quarterly payment through commercial banks. The reality however remains that the operating environment for infrastructure services is deficient.



Strengthening the Operating Environment for Private Infrastructure Investment

International experience since the 1970s suggests a significant increase in the role of the private sector in the provision of transport services and infrastructure. However, there is a need for a careful assessment of the regulatory environment within which these services could be provided in Zimbabwe, in view of the multiplicity of existing challenges. One of the important challenges in the medium-term is to strengthen the regulatory framework. In doing so, Zimbabwe can draw on a rich background of analysis and assessment of the regulatory experience of other countries. The World Bank (2010) reports that "The standard infrastructure reform and policy prescription package of the 1990s - market restructuring, private involvement up to and including privatization, establishing independent regulators, and enhanced competition- yielded positive results in Africa." Experience elsewhere in Africa further indicates that most African countries have undertaken preliminary institutional reforms, mainly the broader sectoral policy and legal measures, but regulatory and governance reforms have taken much more time to produce results. This process could be expedited as Zimbabwe is not entirely a new player in private sector provision of infrastructure investments. A good example is the 350 km railway line from Beitbridge to Bulawayo built in record time of 18 months ending in 2000. The construction was done on Build- Operate-Transfer basis by Bulawayo Beitbridge Private Limited through a PPP arrangement (85% held by New Limpopo Bridge Projects Limited and 15% by National Railways of Zimbabwe).

9 For more information please visit http://www.afdb.org/en/countries/southern-africa/zimbabwe/infrastructure-and-growth-in-zimbabwe-an-action-plan-for-strengthened-recovery/

However, the government has to ensure that policies are formulated and implemented in a consistent and predictable manner in order to address challenges in the operating environment and negative investor perceptions about the country. In particular, there are three closely related sets of concerns that will require early attention. These are:

- Strengthening the legal, regulatory, and administrative environment applicable to the provision of infrastructure services;
- Technical and financial restructuring, including privatization of state enterprises that are likely to enter into partnerships with potential equity investors, or that will need to go to the financial markets for long-term funding for infrastructure projects; and
- Strengthening the policy framework for private investment in infrastructure services under public-private partnership arrangements of one kind or another

Strengthening the Institutional and Regulatory Environment

An efficient operating environment for infrastructure development calls for important changes in institutions involved in the regulation and oversight of infrastructure services. These initiatives will include:

- Strengthening regulatory arrangements with the creation of an independent regulator for the oversight of management and the provision of related infrastructure services. The standard recommendations for the creation of such an agency are straightforward and revolve around the following three broad principles:
  - the regulator's sectoral breadth of authority;
  - the desirable qualities of a regulator; and
  - the division of labor between the regulator and the government.
- A new legislation to create the proposed independent regulatory authority. The essential element of an effective regulatory framework for related infrastructure and services is to place the responsibility for regulation in an agency with the required independence, autonomy, expertise, and accountability.
- The regulatory authorities should have access to their own funding sources and not be reliant on budgetary transfers from the national government. The most common approach could be to impose fees on the regulated industries or the consumers of regulated services in the form of user charges and other service fees.
- Consideration of issues that emerge from increased regional integration of economic activity. Regulatory and administrative hurdles continue to inflate costs and prolong delays for freight movements along the strategic road and rail routes used by Zimbabwe.

In the transport sector for example, the civil aviation is regulated by the Civil Aviation Authority of Zimbabwe, which is also the operator of airport and navigation services for the industry. In the case of road transport, there is no formal regulatory body. However, responsibility for technical standards for road construction and safety rests with the Department of Roads, while responsibility for overseeing the road transport industry is dispersed among several entities. Hence, the creation of a single regulatory agency for the entire transport sector, including roads, rail, civil and aviation, is necessary to substantially expand private sector participation in the decade ahead. The creation of a single regulatory authority for the transport sector is not uncommon. For example, countries such as Brazil, Argentina, Tanzania, and Singapore are served by authorities with broad sectoral responsibilities for regulation within the transport sector. Zimbabwe's Posts and Telecommunication Regulatory Authority covers different forms of communication. However, careful consideration of the degree of independence, autonomy, expertise, and accountability for the authority will be required under these circumstances. In addition, an integrated approach to the regulation of transport services, with due attention to inter-modal competition, would appear to best serve the country at this time.

Restructuring of State Enterprises

The restructuring of state enterprises has been identified in the Government's Medium Term Plan as one of the priorities for the medium-term. The need for reforming the public enterprise sector has long been raised, but progress is lacking. In addition to addressing the regulatory framework, state enterprises play important roles in the provision of infrastructure services and these should be candidates for restructuring. If there is to be sustained progress in rehabilitating and rebuilding the infrastructure assets and services of the country, there is a clear need for early action on the financial and technical restructuring of these enterprises. For instance, potential private investors in water storage and transport, power generation, railways, and airport concessions will require financially sound public partners for the types of PPP arrangements currently envisaged by the government. The restructuring process will have to be undertaken on a case-by-case basis, with close attention given to the full range of stakeholder interests, including, for example, the manner in which staff redundancies will be managed. In those cases where state enterprises are to be privatized, the design of the programs will need to take account of the earlier-mentioned indigenization law. A variety of techniques can be used to ensure compliance with the requirements of the indigenization law. These will center on the proportions of voting and non-voting stock to be issued by the privatized company and the extent to which government equity in the existing state enterprise can be converted into voting or non-voting stock at the time of privatization and then transferred to a nominal purchase price to mutual funds or other entities on behalf of indigenous Zimbabweans. Similar approaches could be used in other infrastructure sub-sectors.

Strengthening the Policy Framework for Public-Private Partnerships

There were a number of initiatives by the Zimbabwean government in the 1990s to expand the role of the private sector in providing infrastructure services. These were largely inconclusive. The initiatives failed to take off for a number of reasons, including investor perceptions of high political risk, lack of political commitment, lack of clear legal and policy frameworks, lack of financial resources within the government, currency risks, lack of expertise and capacity within the government, and lack of policy consistency. Following the formation of the Inclusive Government in early 2009, there has been renewed interest in the use of PPP arrangements for infrastructure services. The bulk of the private funding to be mobilized under PPP-type arrangements will be in four sectors: water storage and transport, power generation, concessions for railways, and concessions for airport services. This process will involve dealings with the parastatals that currently own these types of infrastructure assets. As already indicated, the current financial position of these parastatals is unsatisfactory. In their present financial condition, it is unlikely that they could form successful partnerships with private investors. From the perspective of potential private investors, the combination of the unsuitable legal framework, uncertainty about the regulatory environment, and the weak financial position of the public partners translate into a high degree of risk and uncertainty about the attractiveness of these PPP opportunities.

Some progress in this direction is already underway. The government has identified the need to consolidate existing legislation, drafting ofan act for PPPs and drawing up a specific set of regulations under the Procurement Act or the draft Public Finance Management Act.

It has also become clear that in making a final decision on PPP arrangements, several related concerns need to be taken into account. First, it is very unlikely that any major PPPs can move forward until after the formal launch of the debt arrears clearance process. The authorities have reached a consensus on the way forward for a Debt Resolution Strategy with the cabinet approving the Zimbabwe Accelerated Arrears Clearance, Debt and Development Strategy in 2010. However, the continued accumulation of arrears on public and private creditors' accounts will make it very difficult for interested private investors to mobilize the large amounts of debt financing that will be required, either on a corporate basis or with the use of non-recourse or limited recourse loans by the international banking community. Second, the introduction of a series of major PPP projects will create serious difficulties for new regulatory authorities, especially if the provisions of the PPPs are at odds with the regulatory structure on such matters as competition and/or pricing policy, or technical standards for service delivery by suppliers. The reality is that the proposed new regulatory regimes for infrastructure services will also require new legislation. The experience of the past two decades indicates clearly that there is no universal norm for the most appropriate design of PPP arrangements. Any analysis must be made on a country- by- country, sector-by-sector, and project- by- project basis with close attention given to the full range of stakeholder interests.

Third, the government may consider a number of other options to facilitate the mobilization of private finance for the proposed PPP program. These options may include some form of direct public support, particularly in the case of specific risks that private investors or lenders are not well placed to manage such as political risk and environmental risk. The government may also want to look to an intermediary to mobilize some local financing for PPP projects. The provision of such government support and, in particular, contingent liabilities created through such support mechanisms would have to be carefully managed.

Finally, a substantial amount of support will also be required for the development of stronger capacities within the various regulatory authorities already in place or that are proposed. The technical support will be for teams of specialists that include lawyers, financial specialists, and technicians to advise and assist the government in the design and negotiation of PPP-related contracts, including arrangements for take-or-pay contracts in water storage and transport and power generation, and concession agreements for the provision of railway and airport services. International experience indicates that successful PPP programs require good public sector management systems, and especially transparent tender processes and enforceable contracts, the use of transactional advisors, minimum political interference, and a relationship of trust between the public and private sectors. Zimbabwe could benefit from access to the experience of other countries and best international practices in private sector provisioning of infrastructure.

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