SOUTHERN AFRICA QUARTERLY OVERVIEW AND ANALYSIS

4TH QUARTER 2013

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ANGOLA
BOTSWANA
LESOTHO
MALAWI
MAURITIUS
MOZAMBIQUE
NAMIBIA
SÃO TOMÉ AND PRÍNCIPE
SOUTH AFRICA
SWAZILAND
ZAMBIA
ZIMBABWE

4TH QUARTER 2013 http://www.afdb.org/en/countries/southern-africa/

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PREFACE

The Southern African Resource Center (SARC) of the AfDB produces the Southern Africa Quarterly Overview and Analysis. The publication is part of the AfDB's surveillance of economic and policy developments in Southern African countries and Southern Africa as a region. It also attempts to draw some implications of quarterly developments for the outlook period. Individual country reports are prepared by the country economists and produced from information gathered through consultations, the review of country documents and other relevant sources.

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I. REGIONAL OVERVIEW

The Southern Africa region closed the year on an overall positive note, notwithstanding the downward revisions in growth projections seen in nearly half of the countries covered. Early indications show that the average growth rate for 2013 was 4.3 percent, only slightly lower than the 4.4 percent predicted in the third quarter. On a positive note, growth was strong in Mozambique, Zambia and Angola and picked up in Malawi and Swaziland. Mozambique continued on a strong growth path driven by growth in the mining sectors (coal) and in transport and communications. Zambia's growth performance in 2013 is predicted to have been slightly lower than observed in 2012, but remains among the highest for the region, driven mainly by expansion of output in the mining and quarrying sector, and relatively higher copper prices. In Malawi, growth was on the back of strong performance of the main export sector, tobacco, and a recovery of manufacturing and construction following subdued performance in 2012. In Angola, growth at the end of 2013 was predicted to have fallen below expectations due to volatile oil prices; but it was higher than observed elsewhere in the region thanks to robust growth in non-oil sectors such as energy, agriculture, fisheries, and manufacturing. Growth in Swaziland is expected to have rebound in 2013 from a very low base in 2012. This recovery is attributed mainly to the recovery of the manufacturing sector in response to a recovery in export demand and recovery in the construction sector in response to increased public capital expenditure.

However, the majority of countries experienced a deceleration of growth in 2013 compared to the growth levels achieved in 2012. In Botswana, weak global demand for diamonds and a severe drought significantly constrained fourth-quarter growth, placing overall performance in 2013 below 2012 growth. Lesotho was expected to have closed the year at a moderate growth rate, well below its 2012 growth rate, explained by weak external demand and the overall performance of the mining sector. Lesotho's economy rebounded in the last half of the year, following weak first and second quarter performance. This is attributed to the recovery of textiles exports in response to improving economic activity in the United States. Growth in Mauritius was also predicted to have slightly moderated in 2013, reflecting weak economic performance in Europe and a winding down of major public sector projects. In Namibia, a weaker external environment explaining the poor performance of the mining sector, and persistent drought, moderated growth to its lowest level in the past four years. In São Tomé and Principe growth was also moderate and slower than expected in 2013, owing to failure to secure funding for anticipated private sector projects, and disbursement delays in ongoing public and private sector projects. The South African economy closed the year on a depressed growth note due to contractions observed in the manufacturing sector, although positive trends were observed in mining and agriculture thanks to expansion in real output from these sectors. In Zimbabwe growth is predicted to have moderated in 2013 relative to 2012, with a further slowing of the economy reported in the fourth quarter of 2013. This is explained mostly by the poor performance of the agricultural and mining sectors, in addition to the chronic challenges associated with low liquidity and deindustrialization.

With the exception of São Tomé and Principe, regional member states are also members of the Southern African Development Community, SADC, and subscribe to a set of macroeconomic convergence targets. In 2013, performance with respect to inflation was positive in all countries except Malawi, which continued to experience high inflation rates, and a reversal of the disinflation trend that has commenced earlier in the year was observed. Nearly all countries met the convergence with respect to the size of public debt. Some notable developments in 2013 included an increase in public debt in Mauritius, to fund a rapidly widening fiscal deficit, which brought the total stock close to the legal ceiling and widened the gap between current debt levels and the 2018 target. Mozambique issued its first dollar-denominated bond amidst concerns of fiscal transparency and expenditure prioritization given the allocation of the funds raised toward military expenses, although the country remains well within the debt sustainability target. Slippage in fiscal policy was observed

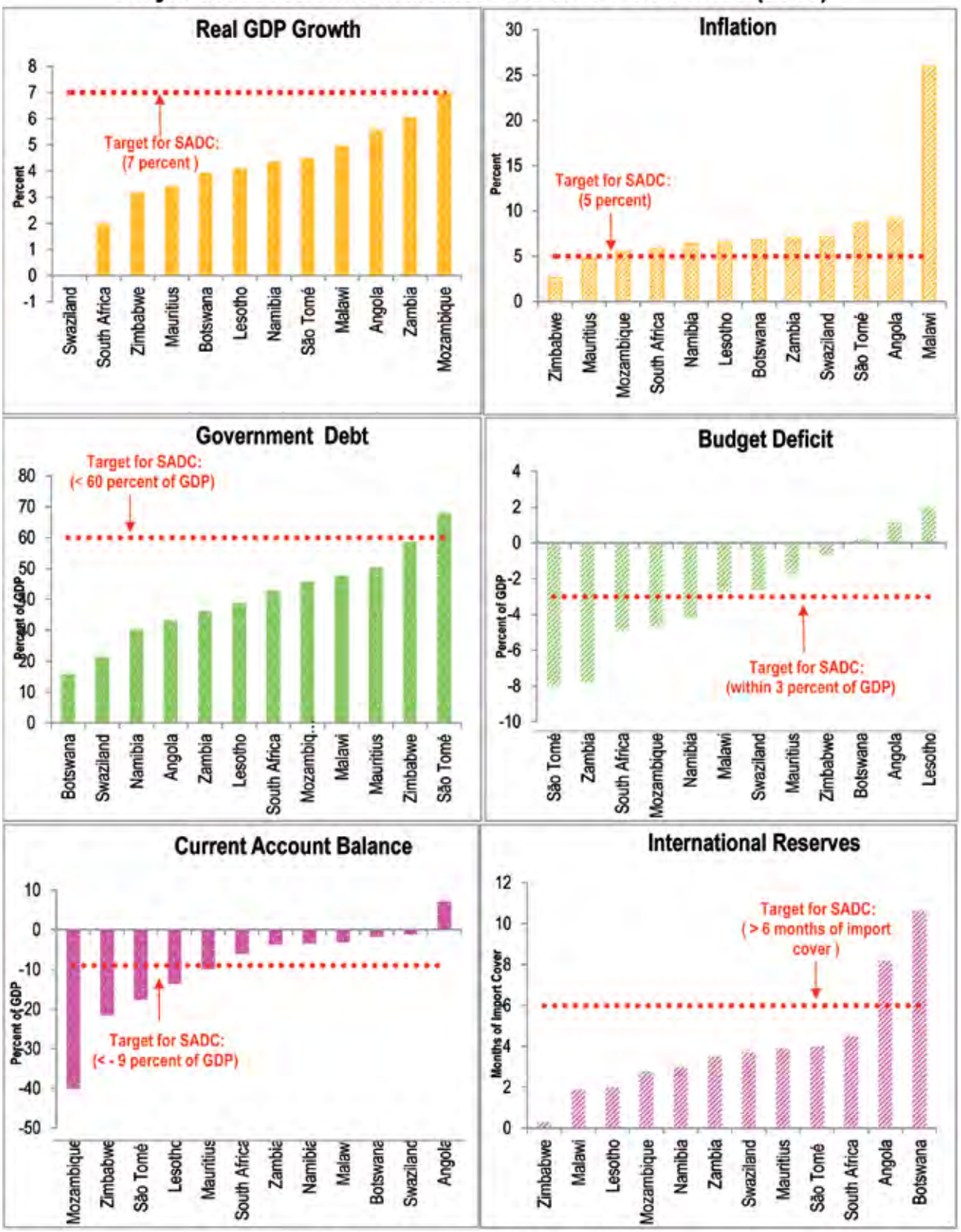
in Malawi, where the debt ceiling was breached to cover a larger than expected fiscal deficit, following a drastic withdrawal of external financing in the fourth quarter, which occurred in response to the Cashgate Scandal. In South Africa, the Government was able to lower external debt by paying off some of its rand-denominated debt, but overall debt increased by two percentage points as a result of the persistent fiscal deficit. In fact, two thirds of countries in the region are running budget deficits funded through debt. However, most are within the prudent targets on fiscal deficit as well as debt, reflecting efforts to diversify fiscal revenues observed in Angola, and fiscal consolidation in a number of countries including Lesotho and Namibia. The countries that recorded higher fiscal deficits mostly did so while funding expansionary fiscal policies to stimulate growth and jobs (Namibia, South Africa and Zambia).

The overall external balance of the region continues to be negatively affected by the weak performance of the global economy, which affects export earnings in oil and mineral-rich countries. However, improvements on the Unites States market had positive effects on textiles exports from Lesotho and Swaziland, while growth in tourist arrivals from Asia helped boost export earnings for Mauritius despite a decline in arrivals from Europe. Most countries are therefore failing to meet the SADC target on international reserves, with only Angola and Botswana surpassing the set floor of 6 months of import cover, while South Africa's position is boosted by large portfolio inflows, which fund part of the current account deficit.

Some key changes in the policy positions of member states observed on the fourth quarter include effort to migrate from use of short-term debt instruments to long-term debt in Swaziland. Angola has approved a customs policy, which aims to promote the domestic production of industrial goods and agricultural commodities. In Botswana, significant developments were observed in the diamond-mining sector, with the relocation from London to Gaborone of part of De Beer's value chain operations, and the new Okavango Diamond Company commencing full-scale operations, in the fourth quarter of 2013. In São Tomé and Principe, the Government modernized the customs systems by adopting the SYDONIA software in the fourth quarter of 2013. The Employment Tax Incentive Bill was signed into law in South Africa, paving the way for the implementation of the young worker tax incentive, which is meant to address youth unemployment in part. The Promotions and Protection Bill was also approved by Cabinet, and will facilitate the drafting of a uniform legal framework- governing investment, in place of the current fragmented framework based on individually negotiated bilateral treaties. Zambia launched its debut road-tolling program in the fourth quarter, which for now, focuses on heavy vehicles as one of the mechanisms to widen the tax base and support capital investments. A broadening of the program is expected in 2014 to cover other vehicle types. Finally in Zimbabwe, the recently elected Government passed Zim-ASSET, which outlines the national development plan for the period 2013 to 2018. However, implementation will depend in part on the outcome of the IMPF Staff Monitored Program review, which is now scheduled for March 2014, following an extension of the program's implementation into the fourth quarter of 2014.

The region's outlook is overall positive, with growth expectations for 2014 to pass predicted growth for 2013. A number of issues that will require policy attention in 2014 include: effective reengagement with lenders in Zimbabwe, the implementation of fiscal reforms to curb the widening deficit in Mauritius, the effective monitoring of Government spending in Zambia, the effective implementation of the youth employment incentive system in South Africa. Elements of fragility in public finance management and the political climate emerged in Malawi, São Tomé and Principe andMozambique. This needs to be carefully monitored and managed in 2014.

Key Macroeconomic Indicators for SADC Countries (2015)



Source: International Monetary Fund, World Economic Outlook Database, October 2013
Note: SADC targets do not apply to São Tomé and Príncipe

II. COUNTRY ANALYSES

HIGHLIGHTS

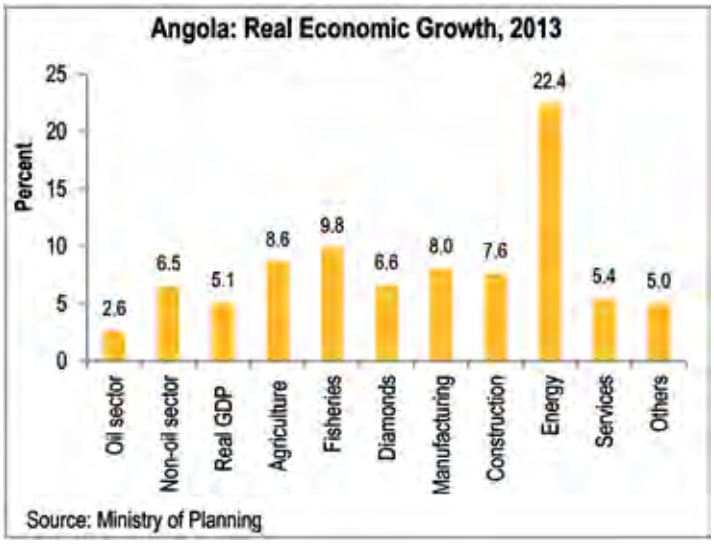
- Against a backdrop of weak budget implementation and volatile oil prices, real GDP grew by 5.1 percent in 2013, lower than the initially planned 7.1 percent.
- The country's economy has shown strong signs of stabilization but efforts must be made to further reduce the cost of living and adopt sound socio-economic management policies in order to drive development and lift many Angolans out of poverty.
- Investments to address the skills gap and modernize economic and social infrastructure are critical if the country is to continue its upward trajectory as one of fastest developing economies in the world.

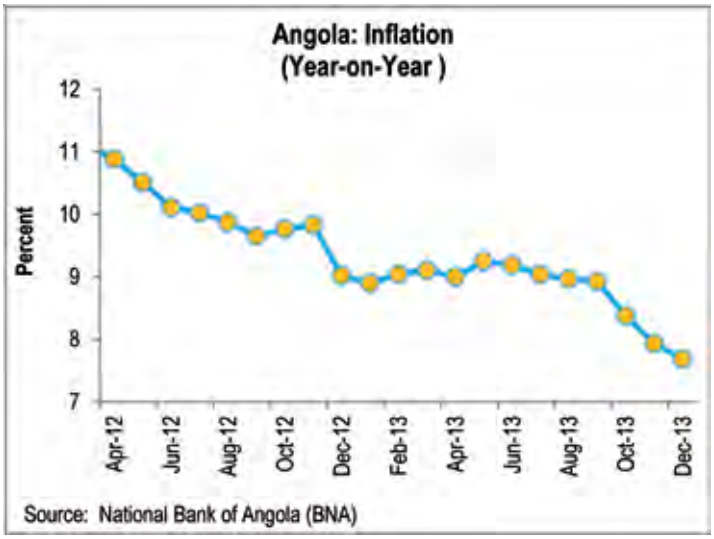
I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Angola's economic growth has remained positive despite the risky current global environment and the persistent risks from oil shocks. Growth was mostly driven by robust non-oil activity, notably in the energy, agriculture, fisheries, manufacturing and construction sectors. Against a backdrop of weak budget implementation and volatile oil prices, real GDP grew by 5.1 percent in 2013, lower than the initially planned 7.1 percent. The oil industry produced more than 1.7 million barrels per day (bpd) and total oil export revenues reached USD 32.5 billion in November 2013 against the USD 36.9 billion recorded in similar period of 2012. This oil revenue decline was mostly attributed to the wavering international commodity prices. Though indications of economic diversification are positive, oil production continues to account for approximately 47 percent of the country's GDP, 80 percent of Government revenues and 95 percent of its exports. Meanwhile, Government's investments in hydroelectric schemes, telecommunications and large-scale agricultural projects have demonstrated a long-term commitment to the reconstruction of the country and present new and growing opportunities to attract foreign investment.

Monetary Policy and Banking System: As the country's economy stabilized, monthly inflation measured by the Consumer Price Index (CPI) fell from 7.94 percent in November 2013 to 7.69 percent in December 2013, the lowest in more than two decades. Food and non-alcoholic beverages' price volatility remains one of the major drivers for inflation followed by goods and services, furniture, the costs of domestic appliances,, clothing and footwear. The significance of the CPI remains limited as it only covers the city of Luanda. In the short-term it is expected that inflation will remain benign and stay within the Central Bank's target range of 7-9 percent, and supported by a relatively strong domestic currency and prudent monetary policy. Angola's banking system also improved significantly in 2013. The framework for monetary policy management was modernized with the introduction of a reference rate by the Central Bank. The foreign exchange market and de-dollarization were enhanced with the implementation of the new oil foreign exchange law since July 2013. The banking sector's capital adequacy ratio remained strong at 18.3 percent in December 2013, well above the minimum requirement of 10 percent. Consistent with the accommodating monetary policy, the monetary accounts from the Central Bank of Angola indicate a significant expansion of broad money supply (M3) by 4.03percent in November 2013, which reached AKZ 4.389.831,46 million (equivalent to USD 43.9 billion) and corresponding to an annual variation of 13.26 percent.

The favorable monetary policy trends also led to an annual expansion of total credit-to-the-economy, which averaged 21.13 percent on annual basis, though in a downward trend as compared to the 2012 level of 30 percent. Credit growth was mostly supported by rising demand for social and individual activities' financing (22.6 percent), private sector (19.4 percent), wholesale and retail trade (16.5 percent), construction (10.2 percent) and real estate (9.2 percent). In contrast with strong money supply growth, the reference domestic interest rates for the period of 181 days to one year increased slightly from 12.81 percent in August to 13.6 percent in November 2013. As a result, the average spread between lending and deposit rates also saw an increase of 0.54 percentage points during the last quarter of 2013 closing the year at 8.39 percent. This inconsistency in the monetary policy transmission mechanism can be attributed to the prevalence of structural and operational risks and the shortage of capital for long-term investment in the banking sector.



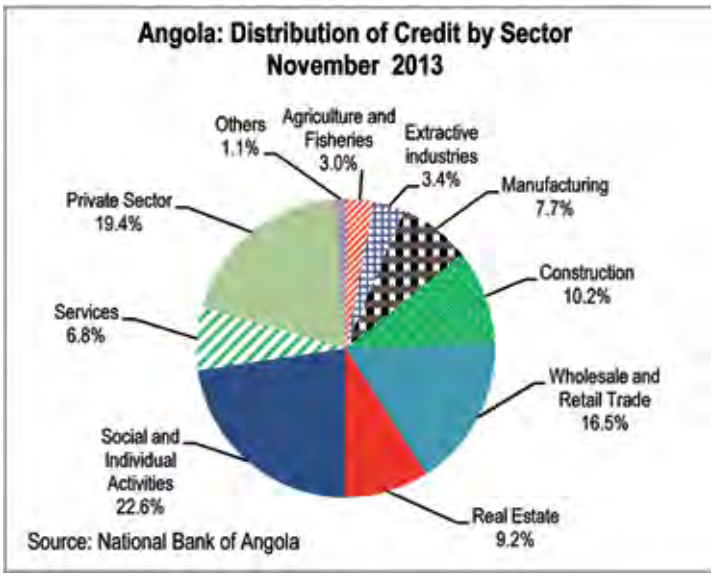


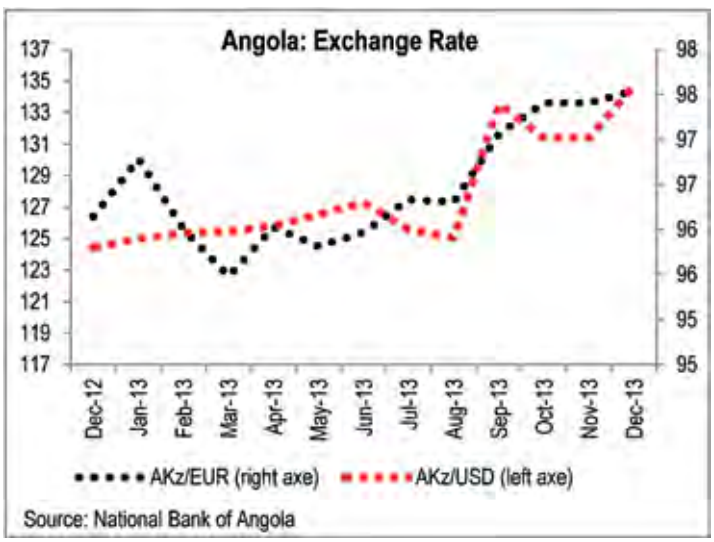
ANGOLA

During the last quarter of 2013, the domestic currency (kwanza) experienced a nominal depreciation of 0.21 percent against the American dollar (USD) and 2.1 percent to the euro (EUR), having closed the year at AKz/USD 97.6 and AKz/EUR 134.4, respectively. These, combined with declining inflation, have contributed to reducing the domestic exchange rate overvaluation and consequently improve the country's competitiveness. Data from the Central Bank of Angola also indicate that the executive has intervened in the foreign exchange market by selling an equivalent to USD 1.905 million in October 2013 in an attempt to stabilize the domestic currency and meet the increased demand for foreign currency associated with the imports of goods and services during the festive season.

Fiscal Policy: Despite the significant increase in capital expenditure from USD 13 billion in 2012 to USD 18 billion in 2013, as well as the slight reduction in the oil price from the realized level of USD 111 per barrel (pb) in 2012 to the projected USD 96 pb in 2013, the budget did not move into a deficit. Instead, it recorded a primary balance surplus of 0.3 percent of GDP by the end of 2013. The Government's fiscal anchor, measured by the non-oil current primary balance deficit, has shown signs of improvement as it declined from 36.1 percent of non-oil GDP in 2012 to less than 31.7 percent in 2013. Nonetheless, the anticipated increase in Government spending on infrastructure, which is expected to be largely financed with foreign borrowing, poses significant risks to the economy if sustained without adequate growth. According to estimates by the Ministry of Finance, total fiscal revenue, as a percentage of GDP, decreased from 43.3 percent in 2012 to 38.2 percent in 2013, due to reduced growth on oil revenues. In contrast, non-oil fiscal revenues have increased from 6.4 percent of GDP in 2012 to 9.4 percent of GDP in 2013. This was due to increased efforts to improve efficiency in tax collection as a result of the implementation of the Executive Program for Tax Reform (PERT). On the expenditure side, by November 2013, the execution rate stood at 81 percent of the total annual budget, which represents a significant improvement as compared to the 53.9 percent level that was registered in the similar period in 2012. Fiscal expenditure was mostly driven by the strong annual expenditure of execution of goods and services (128 percent), interest payments (142 percent), and wages and salaries (93 percent). Consistent with the previous fiscal years, capital expenditure execution in 2013 stood low at 67.7 percent reflecting delays in external funding, contracting and the weak implementation of public procurement processes. Despite this, Angola's total public debt appeared sustainable at 30.6 percent of the GDP in 2013, according to the IMF's debt sustainability analysis. External debt still accounts for the larger share of total public debt (20.4 percent of the GDP), while domestic debt accounts for 10.2 percent of the GDP.

External Sector: External sector developments were favorable in 2013. Despite the continued improvements in the terms of trade, the current account surplus trended down from 7.3 percent in 2012 to less than 4.4 percent in 2013, according to preliminary data from the IMF. This decline was a result of large investment in public infrastructure and a lower than expected growth in oil revenues. Against this backdrop, Angola's trade balance improved significantly from USD 8.8 billion in the second quarter of 2013 to USD 10.8 billion in the third quarter of the year, according to data from the National Institute of Statistics. This positive performance was largely attributed to the sharp increase of oil exports (8.31 percent) and a significant decline in imports associated to slow performance of vital sectors such as construction and transports. The major import categories that experience a decline over the third quarter of the year include: vehicles and transport equipment (27.85 percent), clothing (26.68 percent), minerals and including other mining products (16.65 percent), wood (12.24 percent), and metal equipment and materials (12.91 percent).





The Central Bank of Angola continued with its policy of accumulation of foreign reserves as a way of insulating the economy from external shocks. As of November 2013, net international reserves stood at 32.9 billion, that is, 2.5 percent lower than the level registered in September 2013. This slight decline in foreign reserves was driven by the Central Bank's decision to inject an estimated USD 1.9 billion into the foreign exchange market in a bid to reduce a chronic spread between the informal and formal exchange rate. As a result, the spread, which widened in early 2013 to near 10 percent because of anxieties relating to the new oil foreign exchange law and excess liquidity has since narrowed to about 4 percent by the end of the year. Angola's foreign reserves remain

strong with an estimated capacity to cover approximately eight months of imports. Balance of payments data from the Central Bank indicate that foreign direct investment (FDI) inflows increased from USD 14.12 billion in 2011 to USD 15.07 billion in 2012. Preliminary estimates for 2013 indicate that FDI stood at USD 15.54, mainly channeled into pre-salt, oil fields, real estate, construction, hotels and tourism.

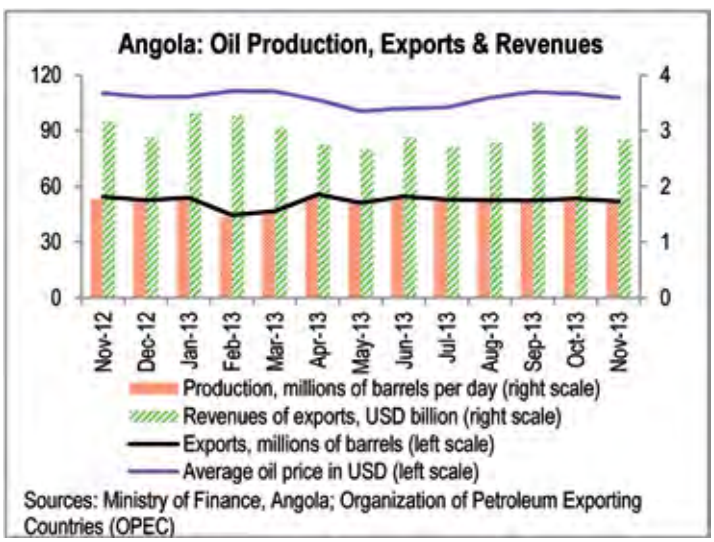
II. INSTITUTIONAL AND STRUCTURAL REFORMS

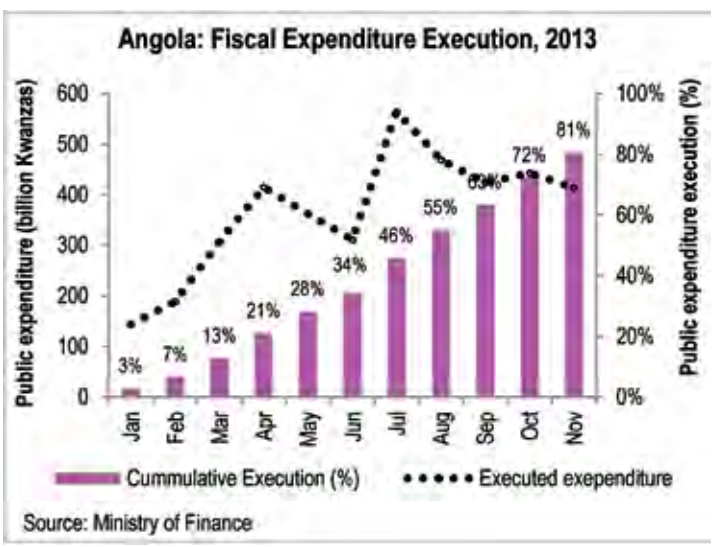
The Government of Angola is currently investing in constructing various kinds of power generation and transmission infrastructure in a bid to improve the quantity and quality of energy supplied. This is part of a broader reform aimed at modernizing the power sector for the period 2013-2025. The transformation of the power sector includes an increase in generation infrastructure from the present capacity of 1,000 MW to 9,000 MW in 2025, based on water resources and natural gas. The reform also envisages the strengthening of the role of renewable energy technologies, especially for wind and solar plants. It is worth noting that the Angolan power infrastructure is in very poor state of repair at present. In particular, the distribution system is plagued by frequent outages and shortages, and over 65 percent of the energy injected into the system cannot be accounted for. Therefore, the power sector reform is a response to the urgent need to modernize the country's power infrastructure and ensure adequate long-term growth. It is expected that this will contribute to improving energy supply and reliability, as well as scale-up access to electricity from the current 30 percent to 50-60 percent by 2025. The implementation of the reform requires massive intervention of various entities, including the private sector and development partners. In this context, the African Development Bank is committed to supporting Government's efforts to modernize the power sector by implementing an integrated investment program and including a capacity-building program for skills development.

In November 2013 the Government of Angola approved a new customs tax policy through Presidential Decree No 10/13 of 22 November. The decree revised major taxes for imports and exports of goods, as well as reduced and liberalized certain taxes on consumable goods. The main objective of this policy reform is to promote national investment in sectors where the country possesses competitive advantages and the capacity to increase industrial and agricultural production and compete with the external market. More specifically, the new policy adopted significant measures to protect the local industry, in particular, through the introduction of a 30 percent import duty, with an additional 10 percent consumption tax on imports of finished manufactured products for domestic consumption. The new decree also simplified the imports of goods that serve as main inputs for national production, including those that are part of the food basket. According to the new customs tax policy, this category of goods will be exempt from payment of customs duties, as well as consumption tax.

III. DONOR COORDINATION

The African Development Bank Office in Angola has continued to play its catalytic role as a knowledge generator and Government's partner of choice for policy advisory services and institutional reforms. As part of these efforts, on 14 November 2013, the Bank Office made a presentation on the 2012 Public Investment Program execution report, as well as the status of implementation of the 2013 state budget to the development partners represented in Angola. During the meeting, the Resident Representative highlighted the importance of the Institutional Capacity Building for Public Investment Program (ICBPIP) in assisting the Ministry of Planning to strengthen the execution, monitoring and impact evaluation of the Public Investment Program on its beneficiaries. The successful implementation of the ICBPIP project would also contribute to create the basis for moving towards the second generation of Public Financial Management systems. Overall, development partners commended the work currently being developed by the Bank Office in Angola and suggested further investigation into the connection between investment expenditure and economic growth through enhanced analysis of the growth drivers.





IV ISSUES NEEDING PARTICULAR ATTENTION

Angola's GDP has remained positive despite the risky current global environment and perennial risks from oil price shocks. The strong dominance of oil revenues on Government's public accounts, exports and GDP call for the need to speed up reforms to bring about economic diversification. Angola also needs to address the skills gap and modernize the economic and social infrastructure (e.g. power) if it is to continue its upward trajectory as one of the fastest developing economies in the world. As the macro economy stabilized and fiscal and monetary policies improved, inflation has fallen significantly, reaching historic single digits over a decade although it still remains high. Therefore, efforts must be made to further reduce the cost of living and adopt sound socio-economic management policies in order to drive development and lift many Angolans out of poverty.

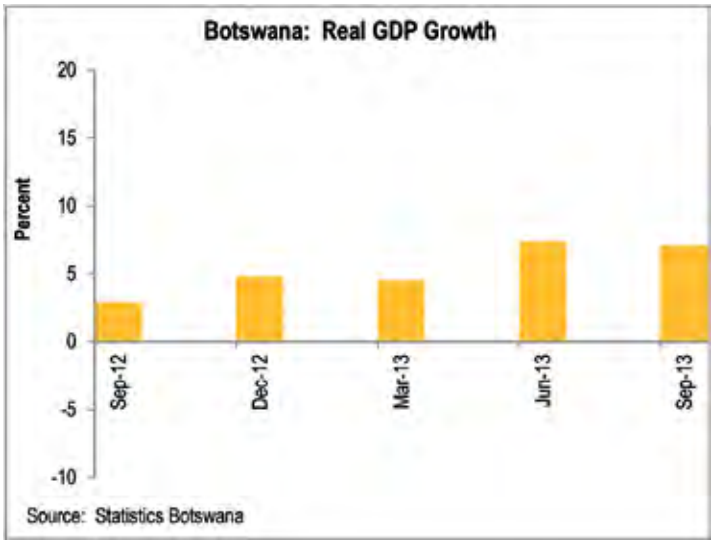
HIGHLIGHTS

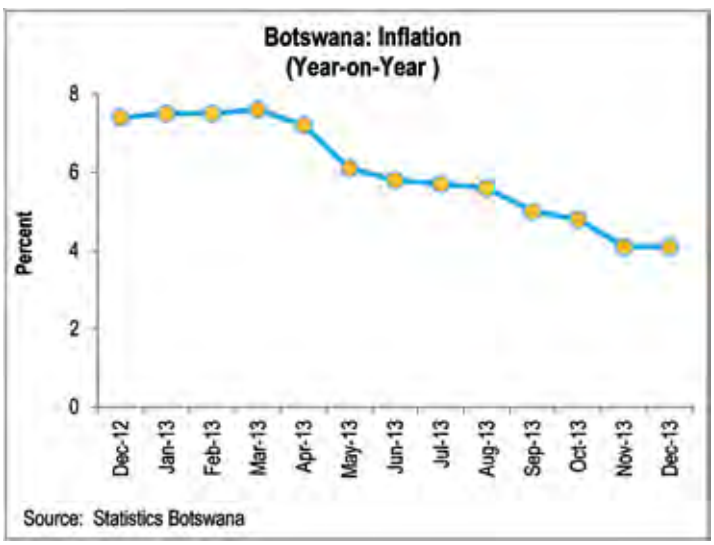
- Real GDP growth rebounded to 7.1 percent in the third quarter of 2013 from 2.9 percent in the similar quarter of 2012, mainly due to a recovery in the water and electricity subsector and sound performance in the mining sector.
- Inflation continued to decline during the fourth quarter of 2013, reaching 4.1 percent in December, thus remaining within the 3-6 percent medium-term objective target range for the seventh consecutive month in 2013.
- The country's diamond industry achieved a remarkable milestone in November 2013 when De Beers relocated its Diamond Trading Company's aggregation, quality-assurance and sight-preparation operations from London to Gaborone ahead of schedule and also successfully conducted its first sight sale.

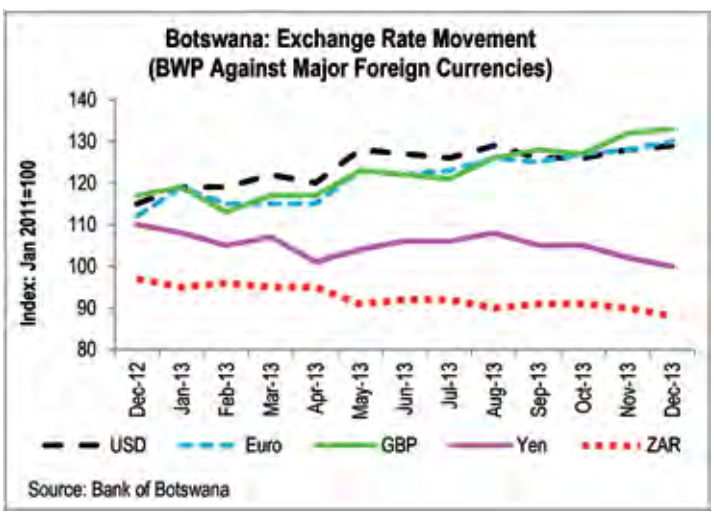
I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Botswana's economic performance rebounded strongly in the third quarter of 2013, with the real GDP growth rate estimated to have increased substantially to 7.1 percent from 2.9 percent in the corresponding quarter in 2012. This outcome mainly reflected a substantial growth of 68.2 percent in the water and electricity sector in contrast to a decline of 31.4 percent in the same period in 2012, as well as a sound performance by the mining sector, which recorded a growth of 21.2 percent. The recovery of the water and electricity sector impacted positively on all other sectors, which recorded growth rates of more than 3.0 percent over the period. While the country continued to suffer from a severe drought, the recovery in the utilities sector emanated from a substantial increase in local electricity generation recorded in the third quarter of 2013 that led to a decline in the importation of electricity. With regard to the mining sector, the better performance was mainly due to a 23.8 percent increase in diamond production compared to a decrease of 36.7 percent realized in the same quarter of 2012. As a result, in the third quarter of 2013, the mining sector's contribution to GDP stood at 22.7 percent. Data for the fourth quarter are not yet available but it is estimated that the sound performance continued during the quarter, thereby leading to an increase in real GDP growth rate in 2013 to 5.0 percent from 4.2 percent in 2012.

Monetary Policy and Banking System: The annual rate of inflation continued with the declining trend that began in March 2013 and fell to 4.1 percent in December 2013. Notably, for the seventh consecutive month, inflation remained within the Bank of Botswana's objective target range of 3-6 percent. The lower rate of inflation mainly reflects declines in food and transport prices. In reaction to the continued decline in inflation, the Bank of Botswana decided to maintain its lending rate unchanged at the level of 8.0 percent that had been put into effect in August 2013. A declining trend was also recorded in core inflation, with the rate falling from 7.2 percent in December 2012 to 4.0 percent in December 2013. The reduction in inflation is expected to continue in the short term due to weak domestic demand and a moderation in external price developments. However, the monetary authorities have indicated that a further relaxation in the monetary policy could be considered based on the evolvement of fuel and food prices.







Fiscal Policy: Government operations during the first quarter of FY 2013/14 (April-June 2013) resulted in a surplus estimated at BWP 2,643 million (about 7.6 percent of GDP). This was higher than the surplus of BWP 1,933 million (about 7.1 percent of GDP) recorded in the corresponding quarter of FY 2012/13. The surplus arose from a significant increase of 40 percent in revenue, which offset a rise in expenditure of 29 percent. This outcome augurs well for the realization of the projected modest surplus of 0.6 percent in 2013/14 that is premised on the challenges emanating from the persistent uncertainty in the global economy and the associated adverse effect on revenues. Public debt is projected to decline to 13.5 percent of GDP in 2013/14 from 14.9 percent in 2012/13; of which 10.2 percent will be external public debt (including publicly guaranteed debt).

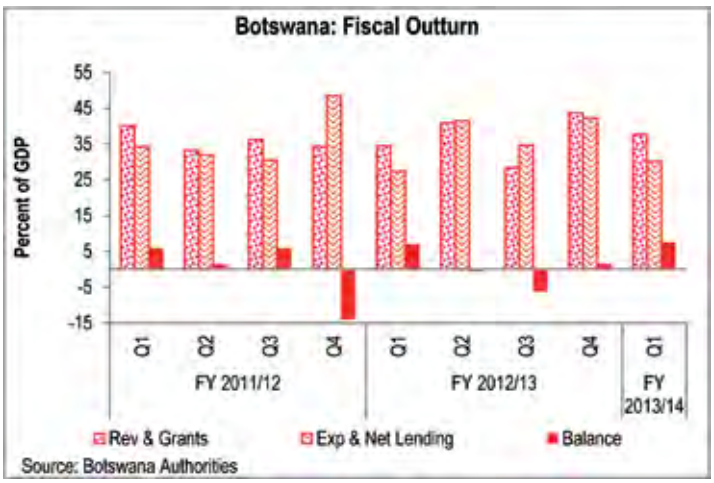
External Sector: During the third quarter of 2013, Botswana's trade balance turned around to a surplus of BWP 1,376 million from a deficit of BWP 6,437 million recorded in a similar period of 2012. The outcome reflected an increase in exports of 45.5 percent, as well as a decline in imports of 8.6 percent. The increase in exports was mainly due to mineral products, particularly diamonds, which increased by 50 percent while the decline in imports mainly emanated from a decrease of 40 percent in imported food items. The recovery in diamond exports suggests renewed prospects for the economy although it may be too early to ascertain the sustainability in view of the global economic prospects that continue to be fragile. The higher exports have contributed to an increase in gross foreign reserves from USD 7.65 billion at the end of June 2013 to USD 8.13 billion as at end October 2013 (equivalent to 13.1 months' of imports). The nominal value of the pula exhibited mixed performance against major foreign currencies during the fourth quarter of 2013. The pula held depreciated against the euro (by 4.0 percent), the pound sterling (by 3.9 percent) and the USD (by 2.4 percent). However, the local currency appreciated against the yen by 4.8 percent and against the rand by 3.3 percent, mainly reflecting a weakening of the rand against major currencies and its large weight in the basket.

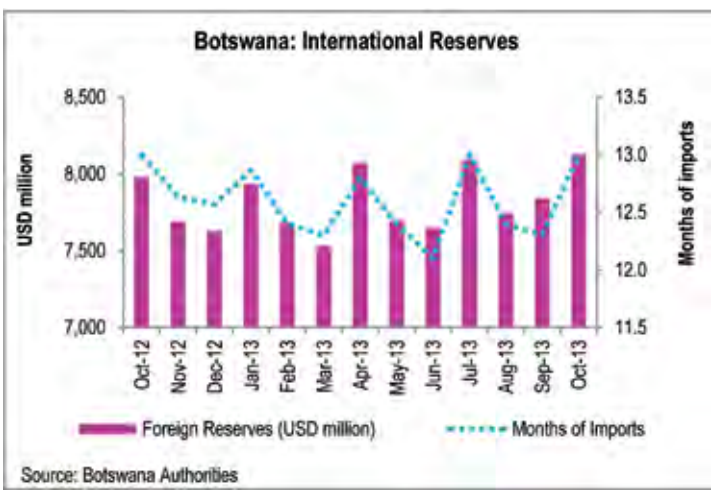
II. INSTITUTIONAL AND STRUCTURAL REFORMS

Botswana's diamond industry received a boost in October 2013 when the Okavango Diamond Company conducted its first full-scale sale, in which 76 companies from the world's major diamond centers participated and in the course of which over 220 000 carats were sold. The diamond cutting and polishing sector has continued to grow, with the licensing of eleven additional companies, bringing the total number to 27. Sales to the local polishing industry are expected to grow from USD 618 million in 2012 to USD 770 million in 2013. However, the most remarkable milestone was achieved in November 2013 when De Beers relocated its Diamond Trading Company's aggregation, quality-assurance and sight-preparation operations from London to Gaborone ahead of schedule. In the same month, the company successfully conducted the first sight sale in Botswana.

III. DONOR COORDINATION

The Ministry of Finance and Development Planning (MFDP) convened the second bi-annual Development Partners' Forum in November 2013. The Forum was well attended by a diverse number of Development Partners resident in the country, including the World Bank, the European Union, various UN agencies, USAID, and other bilateral donors including GIZ, JICA, Japan, France and Brazil. The Bank's participation was particularly appreciated, being the only non-residential development partner in the meeting. The meeting continues to be the key forum for exchange of information on areas of collaboration by the development partners.





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LESOTHO

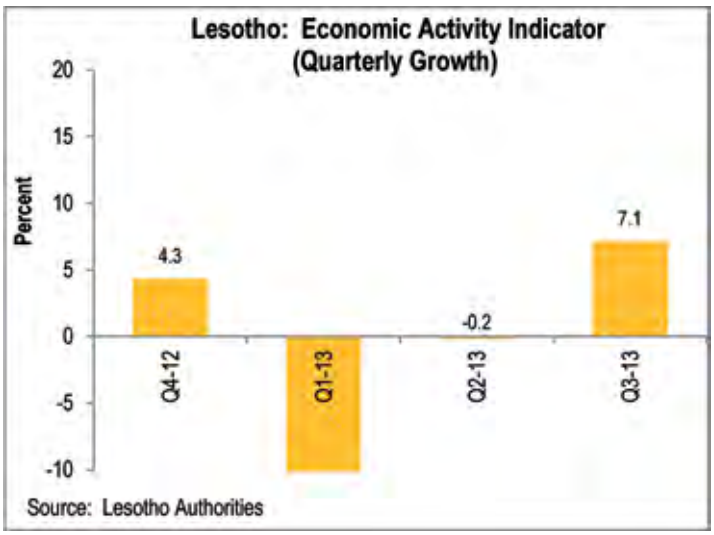
HIGHLIGHTS

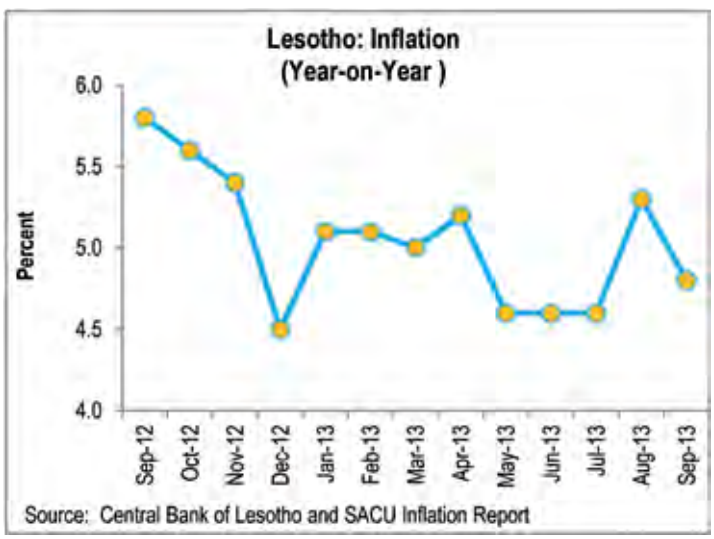
- The economy attained modest growth during the third quarter of 2013 largely on the back of improved performance of mining, financial sector and other services.
- The fiscal balance continues to show a surplus position largely underpinned by faster growth of revenues over expenditure.
- Inflation continues to be below 5 percent and is largely driven by the non-food prices.

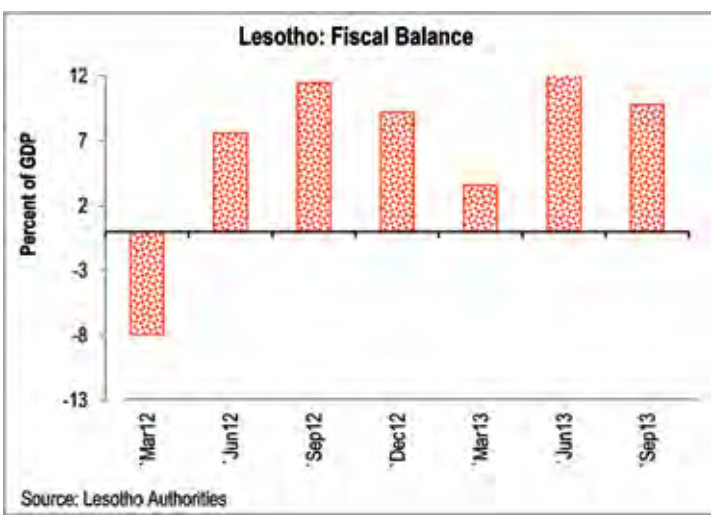
I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Based on the Economic Activity Indicator produced by the Central Bank of Lesotho, the economy attained modest quarterly growth of 7.1 percent in the quarter ending September 2013. This was mainly driven by strong growth in the mining (23 percent) and financial sector (14 percent); other services (13.2); manufacturing (13.0 percent), water (10.1 percent) and electricity (8.6 percent). While construction continued with the slump experienced in the previous quarter, trade and communications registered positive growth of 2.9 and 0.2 percent respectively. Growth was widespread and cut across most of the sectors of the economy. Moving forward, the prospects for the fourth quarter ending December 2013 appeared good, largely premised on continuation of good performance in the key sectors, in particular, the manufacturing of textiles and clothing in response to improving economic activity in the United States of America. Given the close positive relationship between this sector and water subsector as well as electricity, these sectors are also expected to experience high growth. Additionally, the services sector is expected to increase in response to the increased demand during the Christmas season, thereby boosting overall economic growth in the fourth quarter.

Monetary Policy and Banking System: The authorities pursued an expansionary monetary policy stance in response to weak economic conditions and a lower inflationary environment. However, monetary policy continued to be guided by the need to maintain parity between the loti and the rand. The accumulation of gross international reserves in the range of 5.4 months of import of goods and services supported the parity in the third quarter. Although the reserves were lower compared to the second quarter, this favorably compares with the reserves of below 4 months in the same quarter in 2012. Interest rates (91 Treasury Bill rates) showed a downward trend and settled at 5 percent by the end of the quarter, reflecting the need for liquidity to support the economy. The year-on-year inflation slightly rose to 4.8 percent during the quarter ending September from 4.6 percent in the previous quarter but was much lower than the rate of 5.8 percent experienced during the same period in 2012. The year-on-year inflation during the quarter of September was mainly driven by the non-food component (largely housing and utilities; education and tobacco). Inflation, however, remained within the 3-6 range required by the Common Monetary Area. Lesotho's inflation is also influenced by developments in South Africa from where the bulk of the consumer goods are imported. The pass-through from the depreciation in the exchange rate of the rand to domestic inflation remained muted in the quarter ending September, partly on the account of excess capacity in the economy.







Fiscal Policy: The fiscal position continued to show a non-cumulative surplus equivalent to 9.8 percent of GDP in the third quarter although this unfavorably compares with the surplus of 12.7 percent of GDP attained in the previous quarter. The surplus was underpinned by faster growth in Government revenues (largely SACU) than in expenditures (largely recurrent dominated by compensation of employees) during the quarter. The policy of reducing non-productive spending and limiting the spending to core non-SACU receipts has helped to bolster the surplus position through fiscal savings. The surpluses were used to boost the country's reserves, which are required as a cushion for unexpected external shocks. Lesotho's public debt remains low and sustainable although it has shown a slight increase between 2012 and 2013. As of 2013, total public debt as a proportion of GDP was 39.0 percent up from 38 percent in 2012. The bulk of the debt is (92 percent) is foreign and the residual is domestic. The increase in total public debt in 2013 was driven by the rise in the foreign component largely influenced by exchange rate depreciation, although increases in public debt (in a bid to facilitate the capital market development) also contributed.

External Sector: The external current account position showed a surplus of 7.7 percent of GDP in the third quarter of 2013, which was a major shift from the deficit position experienced in the three quarters. The current account balance shifted to a surplus of 7.7 percent of GDP from a deficit of 6.7 percent in the second quarter. The surplus arose from increased merchandise exports and increased net incomes, which surpassed imports. The gross international reserve position was recorded at 5.4 months of import of goods and services. The depreciation of the nominal effective exchange rate to 92 in the quarter ending September from 91 in the previous quarter ending June also bolstered the competitiveness of the country's exports. The external sector is expected to continue with the surplus position through to the next quarter, given the continued depreciation of the exchange rate and the improved economic activity of the United States, a key trading partner for textiles and clothing. There are also indications of increased FDI (estimated at close to 0.7 percent of GDP in 2013 up from 0.4 percent of GDP in 2012).

II. INSTITUTIONAL AND STRUCTURAL REFORMS

The Bank Group has approved the Institutional Support for the Enhancement of Public Financial Management and e-Government Project, which should be operational once the Government signs loan agreements in the course of February 2014. The two projects will expeditiously support the public finance management action plan already approved by Government. Additionally, they will support Government data portals, which will support the implementation of the National Strategic Development Plan. The Government has already produced a monitoring and evaluation framework for its new development plan.

III. DONOR COORDINATION

The development partners continued to share portfolio information through the Development Partners Consultative Forum (DPCF). During the quarter under review, there was some sharing of information on recent economic developments, including the consumer price index from the Ministry of Economic Planning.

IV ISSUES NEEDING PARTICULAR ATTENTION

Sustaining the surplus in the external sector remains a challenge in view of the weakening growth in the Euro Zone, which is already constraining some of the key sectors of the economy. This calls for deepening of drastic actions to widen the production base and to diversify the export markets.

MALAWI

HIGHLIGHTS

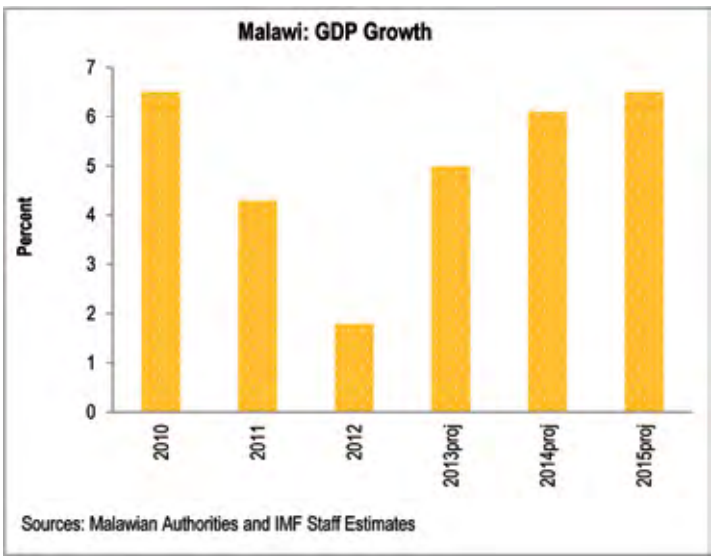
- The Common Approach to Budget Support (CABS) Donors suspended funding to Malawi in response to the massive fraud of public funds (Cashgate).
- The Reserve Bank of Malawi (RBM) further tightens monetary policy, as the Malawi kwacha (MK) continues to weaken against major trading currencies and the risks to inflation are elevated.

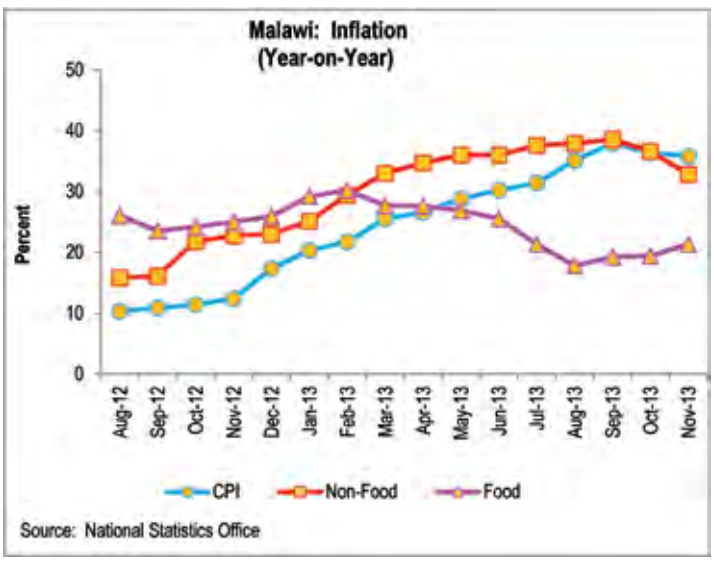
I. MACROECONOMIC MANAGEMENT OVERVIEW

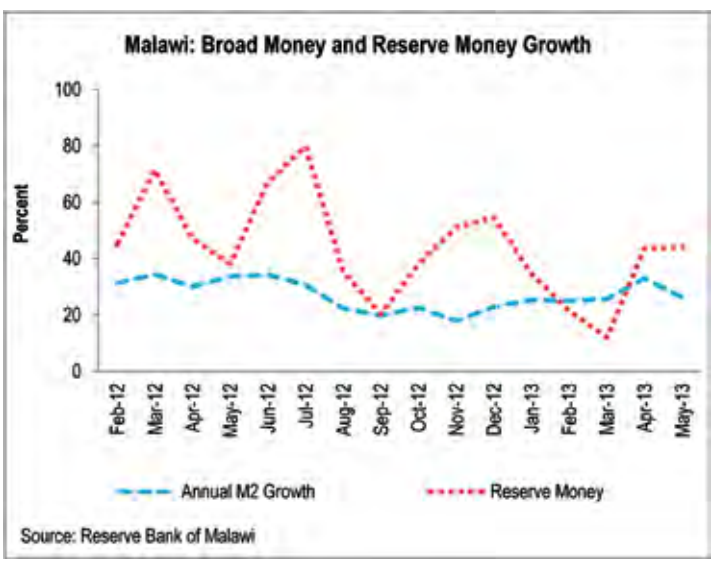
Economic Growth: Despite the macro challenges, Malawi's growth prospects are favorable. This is premised on improvement in the supply response to economic reforms, investor confidence and high prices of tobacco. The main export crop – tobacco – performed strongly in the 2013 season, almost doubling in volume from 78 million kg to 162 million kg. Strong growth in other export crops such as tea is also expected. Manufacturing activities continue to revive after contracting in 2012. Firms are now operating at more than 50 percent of capacity owing to an improved supply of imported raw materials. The pick-up in industrial capacity utilization is likely to be sustained during the lean season. RBM has accumulated adequate foreign exchange reserves to ensure that supply lines for fuel, drugs and other critical imports are not disrupted. The manufacturing sector is forecasted to rebound with growth of 6.3 percent. Construction activities are picking up, a sign of economic recovery. The sector is expected to grow by 7.1 percent. Services, Retail and Wholesale and Mining are also projected to register rapid growth. The economy is projected to grow at .5 percent in 2013, slightly less than the target of 5.5 percent. Growth in 2014 is projected to further increase to 6.1 percent.

There are several risks to Malawi's growth prospects. These are (i) uncertainty in donor inflows – mainly due to Cashgate- (ii) adverse weather conditions; (iii) high interest rates and inflation, which would constrain private-sector investment and hinder growth. The political uncertainty surrounding the 2014 Tripartite Elections is also a risk to the growth outlook for 2014. Private investors are adopting a wait-and-see stance until the political landscape is clearer. Some of the risks reflect the structural weaknesses of the economy. Hence, there is a need to extend structural reforms in order to build a more competitive and diversified economy

Monetary Policy and Banking System: The inflation rate has started picking up, reversing the disinflation trend observed since April, 2013. Year-to-year headline inflation increased to 22.2 percent in October from 21.7 in September. The urban and rural rates stood at 31.6 percent and 17.5 percent respectively in October, 2013. Food inflation increased to 19.4 percent from 18.2 percent while non-food inflation fell to 23.90 percent from 24.2 percent. Inflation accelerated further in November, 2013. Headline inflation rate edged slightly upwards, from 22.2 percent to 22.9 percent. The resurgence in inflation has been driven largely by rising food prices and an adjustment in fuel and utility prices. The increase in food prices is attributed to emerging pressure on maize stocks, as this is a lean season. Further maize price shocks are likely in the coming months unless the strategic maize reserves are restocked.







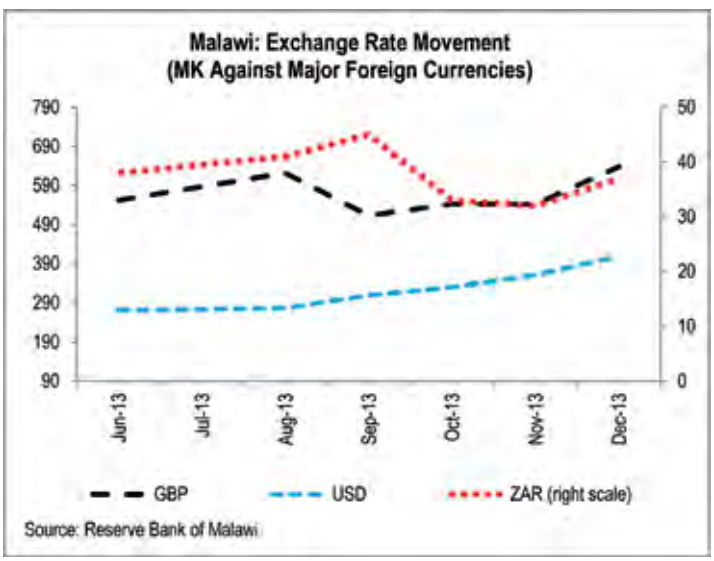
Continued depreciation of the MK against the USD and other major trading currencies is another factor driving inflation. The MK depreciated to MK430 against the USD in December, 2013 from MK330 against the USD in June, 2013. The weakening of the MK necessitated further adjustment in the price of fuel during the quarter. The price of petrol was increased by 3.2 percent in November, 2013. The risks to inflation increased significantly during the quarter under review. In view of the risks, the authorities have had to revise upwards the end December 2013 target. The Government is now targeting an inflation rate of 23.1 percent, end December 2013, which is significantly higher than the original target of 14 percent.

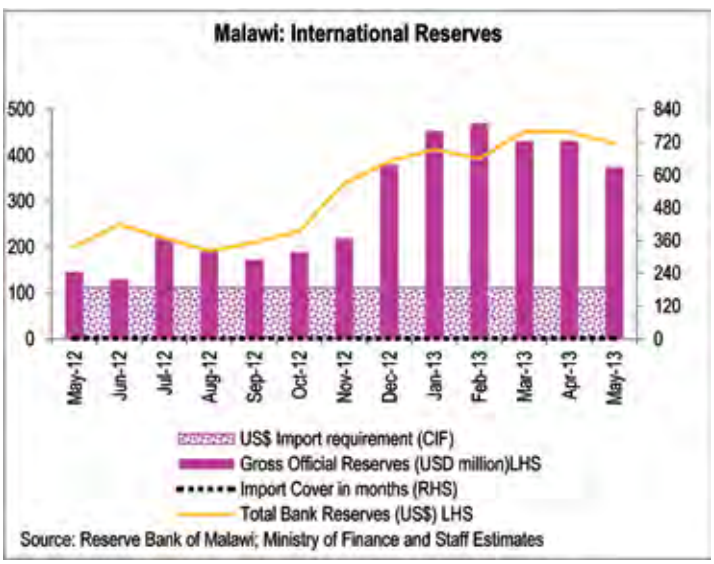
The RBM has resolved to continue with tight monetary policy stance in the light of emerging concerns: notably inflation, exchange rate pressures, and the Cashgate financial scandal. The Cashgate triggered the suspension of donor budget support to Malawi, exacerbating the macropolicy challenges that Malawi faces. The Central Bank has maintained the benchmark bank rate at 25 percent in this Quarter in order to contain inflation, stabilize the exchange rate, and protect foreign exchange reserves. RBM has at the same time instituted additional measures to strengthen monetary policy management with a view to improving liquidity management and further tighten monetary policy. In this regard, the Liquidity Reserve Ratio (LRR) has been modified. Vault cash will no longer count as part of the LRR. Additionally, eligible financial institutions will be required to maintain with the Central Bank a minimum of 12 percent of the revised composition of the LRR. The Central Bank has also introduced a Lombard Facility to facilitate liquidity management by commercial banks and provide access to funds at a spread of two percentage points above the bank rate.

Liquidity conditions during the quarter reflected fiscal trends and developments in money and foreign exchange markets. During the quarter under review, money market liquidity was tight reflecting, contractionary monetary operations in October, 2013. Reflecting tight liquidity conditions, the interbank rate rose to 24.83 percent in November from 19.27 percent in September 2013. Similarly, the all-type Treasury Bill Rate increased to 31.15 percent from 18.74 percent in September 2013. During the quarter bank lending rates ranged from 35 to 38 percent. Market interest rates are not expected to fall significantly until inflation decelerates. The yields on TBs are likely to moderate when measures to restrain expenditure take effect and domestic borrowing requirements are reduced.

During the quarter, broad money supply grew rapidly. Broad money supply expanded by 31.8 percent and 35 percent in October and November respectively. Similarly, reserve money grew by 33 percent and 24.4 percent in October and November respectively. The rapid expansion in money supply during the quarter was attributed mainly to the increase in Government's Net Domestic Borrowing Requirements. Private sector credit growth increased by 11 percent compared to the previous quarter.

Fiscal Policy: Fiscal performance during the first quarter of the 2013/14 fiscal year deteriorated. The weak performance reflected a serious slippage in fiscal policy. Total expenditure were above the target by MK 25.5 billion. While domestic revenue ove-rperformed by MK 20 million, this was not sufficient to compensate for the drastic fall in external financing. Grants underperformed by MK 22 billion, leaving a net shortfall in resources of MK2.0 billion. To cover the shortfall, Government resorted to domestic financing. As a result, the IMF Extended Credit Facility (ECF) ceilings for Net Domestic Financing were breached in the first quarter. The fiscal pressures have intensified following the Cashgate scandal. At the November CABS Review the donors affirmed the suspension of budget support due to the loss of confidence in the Government's Public Finance Management System. Completion of the Third IMF ECF Review was deferred pending assessment of the impact of the Cashgate on the macroeconomic framework and the adequacy of the actions taken by Government to investigate the fraud and rectify the underlying weaknesses in the PFM system. A Special IMF ECF review mission, which visited Malawi in November, 2013 noted the risks to the macro framework posed by Cashgate and urged the Government to vigorously implement the action plan in order to restore donor confidence. The fiscal framework for 2013/14 has been adjusted substantially in view of the increased fiscal gap. The Government has committed to undertake strict expenditure controls and more stringent austerity measures. CABS donors and the IMF are closely monitoring the implementation of the Action Plan. Completion of the Third ECF Review, which hinges on the Action Plan, was rescheduled to January 2014.





The fiscal framework will remain tight in the absence of donor financing of the budget. The Government therefore needs to effectively implement the Action Plan and convince DPs that it is serious in tackling the underlying governance weaknesses.

External Sector: Malawi's external position in 2013 is expected to improve on account of the strong rebound in tobacco exports. Total earnings from tobacco during the 2013 season surged to USD 361 million from USD 177 million in 2012. Export growth in 2014 is projected to further increase by 9 percent, as measures to boost production of other export commodities take effect. Import growth will be lower (4 percent), reflecting the high cost of imports due to local currency appreciation. These trends will result in an overall improvement in the trade deficit. The increase in tobacco earnings has boosted Malawi's international reserves position. As at November 2013, gross official foreign exchange reserves stood at USD 396.2 million, or 2.1 months import cover, compared to USD 431 million (2.3 months import cover) in September. While the level of international reserves provides an adequate cushion, the suspension of donor financing has exerted pressure on the exchange rate. The weakening of the MK is therefore likely to continue. The Central Bank has assured the country that the reserves are sufficient until the peak season starts in March. The RBM will manage the reserves carefully and ensure an uninterrupted supply of fuel and other essential imports.

II. INSTITUTIONAL AND STRUCTURAL REFORMS

The 2014 World Bank Ease of Doing Business released during the quarter shows that Malawi's ranking dropped from 161 to 171 out of 189 countries. This trend underscores the importance of deepening private sector reforms to enhance competitiveness and foster job-creating growth. The Government has committed itself to intensifying private-sector reforms focusing on all the key impediments to a vibrant private sector. These include infrastructure, which is a key constraint to competitiveness. The Government is moving ahead with plans to improve the reliability of energy supply. Currently, the Government is reviewing the Energy Sector Policy in order to create an enabling environment for private-sector participation in the sector.

The cost of trade in Malawi is very high, partly the result of the high prevalence of non-tariff barriers to trade. Therefore, reforms to reduce trade barriers are essential to lower trade costs and enhance Malawi's competitiveness. The Government has passed new business laws in order to improve an enabling environment for private investment. Furthermore, the Government is promoting private investment in strategic sectors such as energy. A number of foreign investors have shown interest in investing in the energy sector projects through the PPP arrangements. Going forward, the challenge will be to ensure that public institutions supporting the private sector function effectively. Therefore, reform of the public sector would contribute significantly to private-sector development efforts.

III. ISSUES NEEDING PARTICULAR ATTENTION

The Cashgate poses a risk to the economic progress made as a result of reforms. The looting of public resources has undermined donor confidence and also has the potential to weaken investor confidence. The Government has to work hard to rectify the weaknesses in the PFM system in order to he restore donor confidence. The steps taken by Government in response to the Action Gate are encouraging but the efforts need to be sustained. Cashgate has provided an opportunity to strengthen the implementation of the Public Finance Management Reform Program. In the longer run, broader public sector reforms will be needed to strengthen accountability and transparency.

High inflation continues to pose a challenge; hence the macro adjustment efforts to achieve price stability need to be sustained. The authorities have further tightened monetary policy, which should reduce inflationary pressures and ease the pressure on the exchange rate. However, the high lending rates pose a threat to private sector growth. The expectation is that interest rates will start falling once inflation comes down. The expansion in the productive base would in the longer run help contain inflation. The Government should exercise fiscal restraint as this will, in the short run, bring down interest rates by minimizing recourse to domestic borrowing.

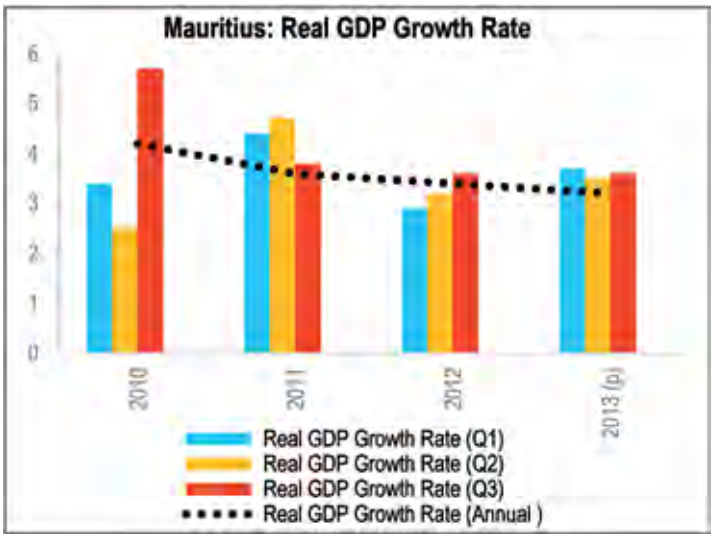
HIGHLIGHTS

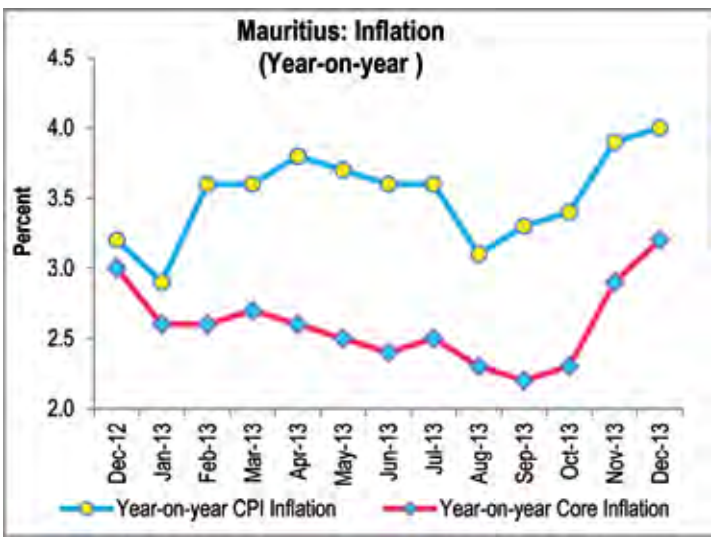
- Against the backdrop of weak external demand, growth was estimated at 3.5 percent in the third quarter of 2013, the same as the revised growth for the second quarter.
- The repo rate remained unchanged at 4.65 percent amidst concerns about excess liquidity and the impact of prolonged negative real interest rates on domestic savings and the banking sector.
- Fiscal space continued to narrow as growth in spending outpaced the increase in revenues**.** The budget deficit at MUR8.04 billion during the period under review had more than quadrupled compared to the corresponding period in 2012.
- The external sector position remained tenuous with the current account deficit in the third quarter of 2013 widening by 8 percent.
- The fight against corruption needs momentum. Mauritius' ranking on the Transparency International's Corruption Perception Index (CPI) declined from 43 in 2012 to 52 among 148 countries in 2013.

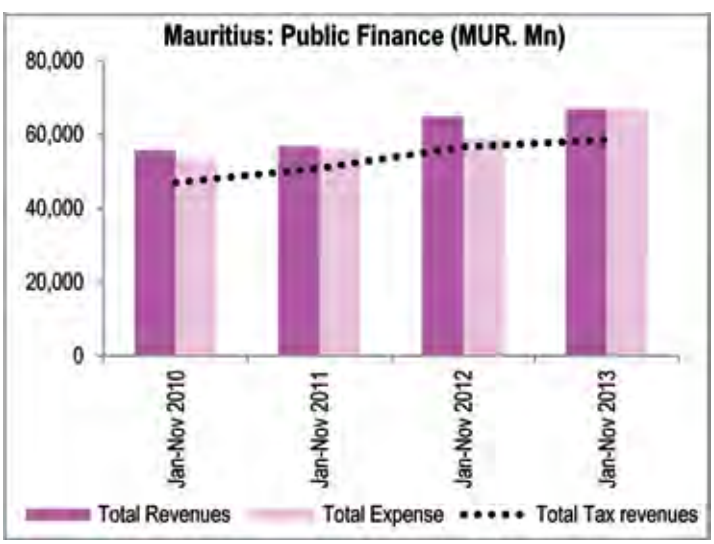
I. MACROECONOMIC MANAGEMENT

Economic Growth: Economic growth in the third quarter of 2013 was estimated at 3.5 percent, the same as the revised growth rate for the second quarter as external demand remained sluggish. Growth was anchored by a strong quarterly performance in accommodation and food services, which grew at 6.9 percent compared to 0.3 percent in the second quarter and a strong performance in financial intermediation, information and communication technology and wholesale and retail trade. Tourist arrivals at 694,443 for period January to September 2013 showed a 2.8 percent increase over the corresponding period in 2012. Arrivals from Europe (374,540) decreased by 2.3 percent, driven by a 6.3 percent fall in arrivals from France, the main market for Mauritius. Arrivals from Asia partly compensated for the weak performance in the European market, as they grew by 29 percent to reach 99,550. On the completion of major projects and a slowdown in public sector investment projects due to capacity constraints to implementation, construction continued to perform below par with growth contracting by 11.7 percent after a decline of 2.9 percent in the second quarter. Against this background, Statistics Mauritius forecasted a growth rate of 3.2 percent in 2013 down from 3.4 percent in 2012. Growth is expected to rebound in 2014 to reach 3.7 percent.

Monetary Policy and Banking System: Bank of Mauritius (BoM) maintained the repo rate unchanged at 4.65 percent per annum amidst concerns about excess liquidity and the impact of prolonged negative real interest rates on domestic savings and the banking sector. Year-on-year CPI inflation increased from 3.3 percent in September 2013 to 4.0 percent in December 2013 against the backdrop of public-sector wage increases. In tandem, year-on-year core inflation rate steadily picked up pace during the period from 2.2 percent to 3.2 percent (Figure 2). Excess liquidity in the money market remained high with all auctions of Government of Mauritius Treasury Bills (GMTB) between end October and end November 2013 oversubscribed. The overall weighted yield increased from 3.29 percent to 3.52 percent during the period. Broad money liabilities increased by 5.4 percent over the corresponding period. Correspondingly, private sector credit accelerated by 0.8 percent to reach MUR403.33 billion in November 2013.







MAURITIUS

Fiscal Policy Fiscal space continues to narrow as growth in spending outpaces the increase in revenues. From January to November 2013 total revenues registered a 2.8 percent nominal increase over the corresponding period in 2012 to reach MUR66.77 billion, with tax revenues representing 87.69 percent. Total spending increased by 13.7 percent to reach MUR66.97 billion with a notable increase of 20.4 percent in compensation to employees. Subsidies and transfers increased by 26.7 percent and 21.4 percent respectively compared to the corresponding period in 2012. The budget deficit at MUR8.04 billion more than quadrupled compared to the corresponding period in 2012. The Government is using domestic debt to finance the deficit. In this regard the debt to GDP ratio at 59.1 percent of GDP as at end September 2013 from 58.1 percent as at end June 2013 had accelerated close to the legal limit of 60 percent, raising concern about the Government's ability to achieve the fiscal target of 50 percent by 2018. The 2014 budget passed by Parliament in November 2013 aims at invigorating investment and growth. However, the authorities appeared to have slowed down on bold reforms, as reflected by a notable absence in the budget statement of earlier plans to secure a private-sector operator to bolster efficiency in the water sector. The budget deficit is expected to widen to 3.7 percent of GDP in 2013, more than double the size in 2012, but should slightly narrow to 3.2 percent of GDP in 2014.

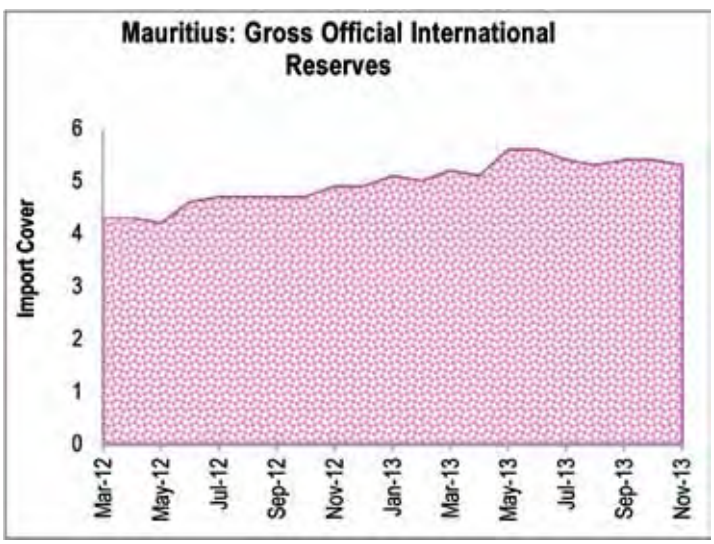
Balance of payments: The external sector position remains tenuous due to weak external demand. The current account deficit in the third quarter of 2013 widened by 8 percent over the corresponding quarter of 2012 to reach MUR11.92 billion (about 3.7 percent of GDP), driven by worsening merchandise trade balance and a significant fall in services surplus. The trade deficit during the quarter widened by 1.4 percent over the corresponding period in 2012 to reach MUR17.45 billion. Furthermore, at MUR1.92 billion, the services account generated a much lower surplus compared to MUR4.48 in the corresponding period in 2012 driven by a 38 percent fall in net travel receipts The capital and financial account registered a surplus in the third quarter with non-residents' direct investments in Mauritius, excluding cross-border transactions of Global Business Companies and net of repatriation, registering a net inflow of MUR1.29 while residents' direct investments abroad net of repatriation amounted to MUR1.15 billion. The overall balance of payments posted a deficit of MUR3.43 billion compared to a surplus of MUR3.0 billion over the corresponding period in 2012. The Bank of Mauritius (BoM) continued to intervene in the foreign exchange market to bolster reserves and smooth volatility. During the period under review, the reserves import cover as at end November 2013 remained at 5.3 months as at end August 2013, while the dealt rupee exchange rate had appreciated by about 1.9 percent against the USD and had depreciated by 1.7 percent against the euro.

II DONOR COORDINATION

During the period under review Agence Française de Développement (AFD) signed a loan agreement of around 50 million euros, as a sectoral budget support for the financing of sustainable development projects in the energy sector. The budget support framework constitutes the main modality of financial support to Mauritius and presents the main platform of collaboration for development partners. A bank's infrastructure investment specialist is present in Mauritius to enhance policy dialogue with the Government and coordination with other development partners. Discussions for bank support in the energy and water sector are ongoing.

III ISSUES NEEDING PARTICULAR ATTENTION

- Plans to strengthen public sector implementation capacity and improve the regulatory framework for Public Private Partnerships need fast tracking to help accelerate the implementation of public sector investment programs.
- Fiscal consolidation needs to accelerate in line with the medium-term macroeconomic framework so as to achieve efficiency gains in budget execution and help attain a more sustainable current account balance. A reduction in Transfer and Subsidies, as achieved in 2012, would help improve the fiscal position.
- Mauritius remains the best performing country in sub-Saharan Africa on governance. However, the latest comparative assessments show the country may be losing ground in some areas, particularly on corruption. A report by Transparency International published during the quarter under review shows that Mauritius's ranking on the Corruption Perception Index (CPI) declined from 43 in 2012 to 52 among 148 countries in 2013, raising the need for further strengthening institutional reforms to curb the emerging problem of corruption in the country.



MAURITIUS

MOZAMBIQUE

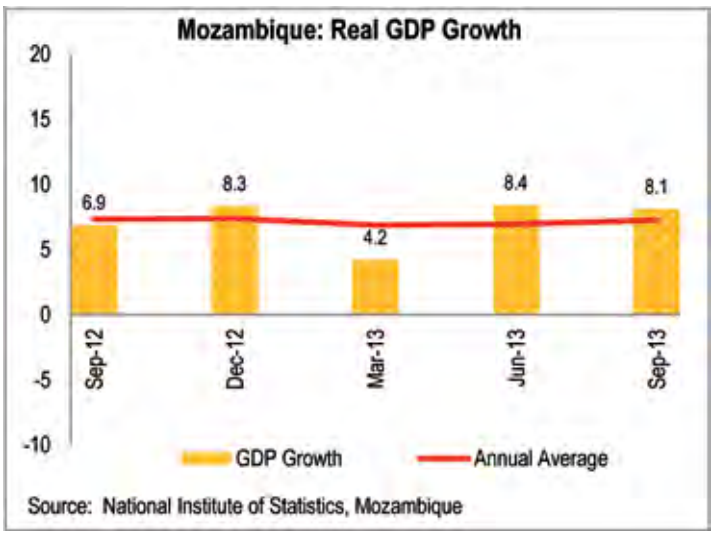
HIGHLIGHTS

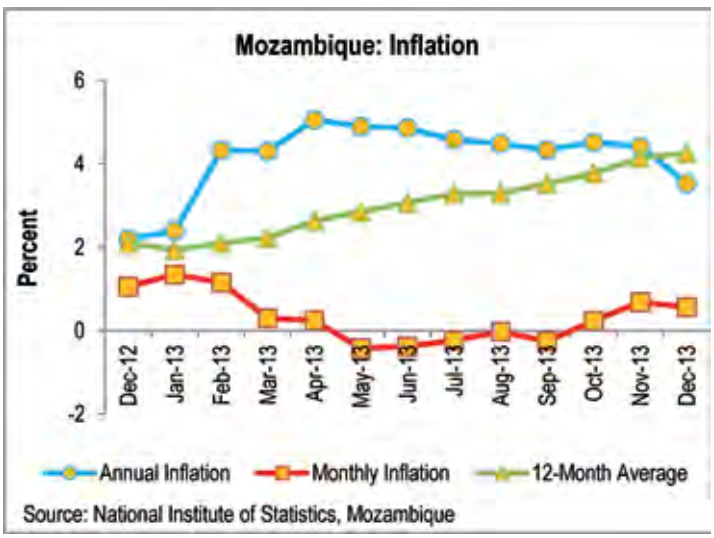
- Despite the negative effects of the flood in the first quarter, economic activity is performing well and on track to achieve the 10-year average annual real GDP growth of 7.2 percent.
- Cabinet approved the action plan for implementing the Green Economy Roadmap, which intends to transform Mozambique's development into a comprehensive process that includes economic, social and environmental dimensions.
- A fishing company, owned by public entities, issued USD 850 million in sovereign-guaranteed bonds on international markets, marking the country's debut issue in dollar-denominated debt. However, issues of public spending prioritization and transparency raised concerns.

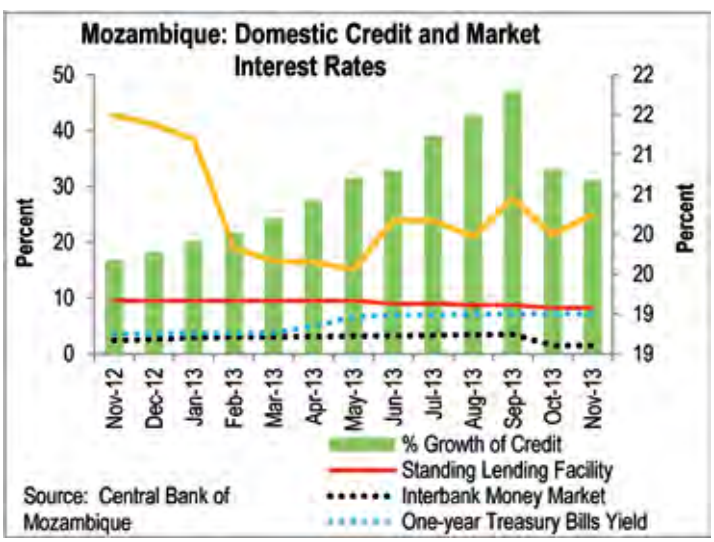
I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Economic performance remained strong in the third quarter of 2013 with a GDP growth of 8.1 percent, although this was 0.3 percent lower than the previous quarter. Growth was driven by the extractive sector, with coal production quickly expanding (21.4 percent), and benefiting from upgrades and improvements in the main rail line and port facilities' shipping capacity. Other fast-growing sectors were Transport and Communication (15.5 percent) and Water and Electricity (11.5 percent). Continued investments in infrastructure and credit expansion are fuelling robust growth in Construction (7.8 percent) and Retail (75 percent). In relative terms the country's industrial sector remains lethargic, with 1.6 percent growth. Agricultural production, still contributing 23 percent to overall GDP, continued its pick-up from the first quarter flooding, with 5.8 percent growth. The Economic Climate Sentiment Index closed the quarter with an up-tick, although Demand, Employment and Inflation sentiments were negative, and on a downward trend since June 2013.

Monetary Policy and Banking System: After 5 months of deflation, between May and September 2013, the fourth quarter brought back price increases correlated with the festivities season and the closure of the vegetables season. Even so, 2013 ended with yearly inflation at 3.54 percent, 200 bps below the official annual target of 5.6 percent. The 12-month average inflation is still rising, and now stands at 4.26 percent. The extended harvest season for vegetables and decreases in the world commodity prices provided a favourable framework. A crucial factor for inflation containment was the continued depreciation of the rand during the year, with an additional 3.37 percent devaluation in the fourth quarter. South Africa remains the main source of food and goods imports. In future these factors will continue to constrain inflation, offsetting the effects of credit expansion to the private sector. In October the Central Bank decreased the Lending Standing Facility (LSF), now at 8.25 percent, by 50 bps. Since the first rate cut of 2013 in May, the LSF was reduced in total by 125 bps on the back of positive inflation figures and with the objective of fostering lower credit rates to small and medium enterprises. However, in the same period, the average one-year lending rate from commercial banks diverged by gaining 69 bps and revealing strong distortions in the credit market.





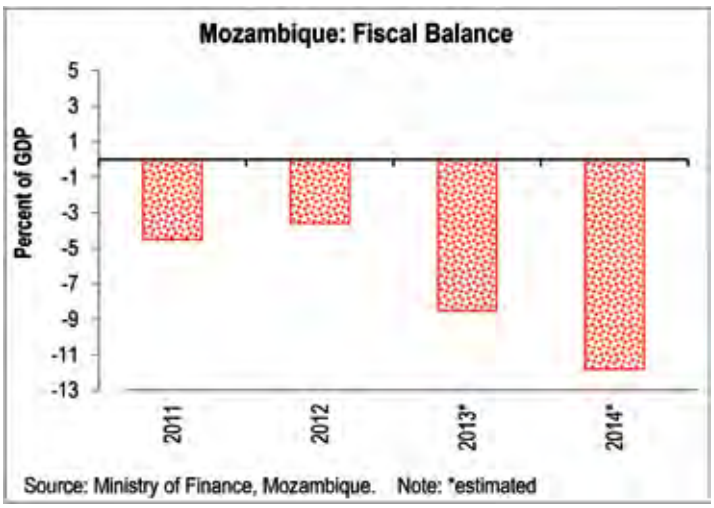


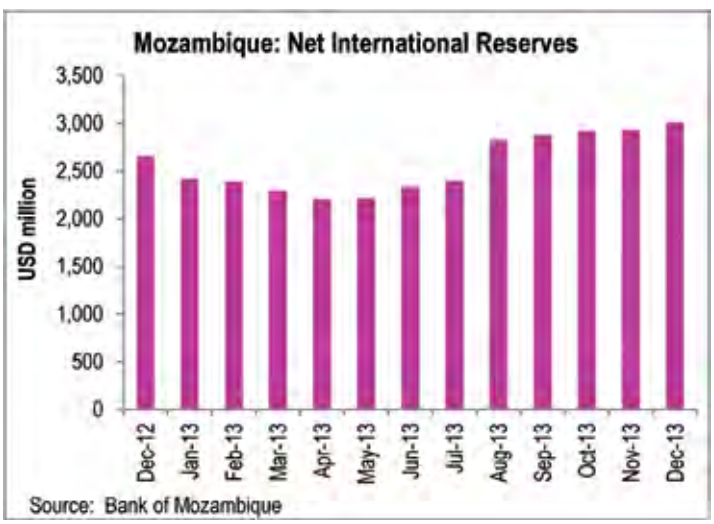
Fiscal Policy: Fiscal execution during the third quarter progressed well, with revenue collection reaching MZN 88.303 billion, 73 percent of the annual target and 22 percent above the same period in 2012. The greatest contribution came from income tax, which reached 83.6 percent of the annual target, profiting from windfall capital gains tax revenues. On the other hand, budgetary expenditure in the same period reached just 61.7 percent, with current expenditure at 67.7 percent of execution. Capital expenditure underperformance was 1.5 percent lower than during the same period of 2012, with 45 percent of the programmed expenditure executed. The delays in project execution due to the floods worsened the country's perennial low absorption capacity. Notwithstanding, the 2014 budget approved by Parliament in December contemplates an increase in capital expenditure to 18.8 percent of GDP. Overall expenditure will expand from 40.2 percent in 2013 to 45 percent of GDP. The extra expenditure includes a nominal increase in the wage bill, special provisions for the presidential elections and the partial inclusion of the EMATUM bond, reclassified as defense expenses. In September 2013, EMATUM, a privately incorporated company fully owned by the state, issued a USD 850 million bond yielding 8.5 percent a year with a 7-year maturity in a non-publicized quasi-fiscal operation., The proceeds will finance a fleet of 24 fishing boats and 6 patrol vessels. The bond benefits from a sovereign guarantee, in practice turning the issue into Mozambique's first sovereign dollar bond issue. On the revenue side, fiscal revenues are estimated to grow by 1.8 percent of GDP. Even so, fiscal revenues will only cover 60 percent of expenditure. Donor funding levels are estimated to level off at 30 percent of the budget. The decrease in direct budgetary support will be completely offset by an increased in donor-funded projects. The remaining financing will come from non-concessional loans. The fiscal deficit is expected to reach 11.8 percent of GDP in 2014.

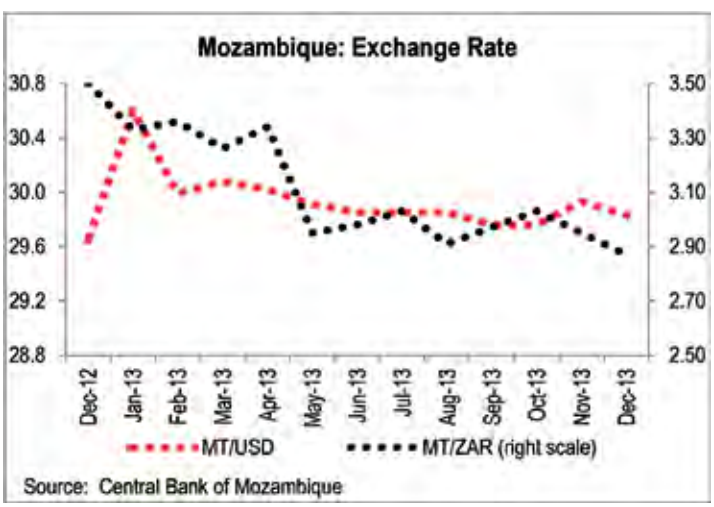
External Position: During the third quarter of 2013 the current account deficit reached USD 3.59 billion (29 percent of GDP), which represents a year-on-year reduction of 15.2 percent, benefiting from a decrease in import of services. As several megaprojects are still at first inception phase, the current account deficit is expected to remain high. FDI – which accumulated to USD 4.5 billion at the end of the third quarter, USD 700 million above the same period in 2012 – largely financed the deficit. On the FOREX market, during the fourth quarter, the Metical (MZN) remained stable against the USD (-0.61 percent), but performed well against the South African rand (ZAR), with a 3.37 percent gain. Overall in 2013 the MZN gained 18 percent against the ZAR, the main currency of imports, contributing largely to contain inflationary pressures, but hindering Mozambique's competitiveness in the region. Net foreign currency reserves have progressively accumulated since beginning of the second Quarter, benefiting from a collection of windfall revenues from capital gains tax associated with gas consortium transactions. The fourth quarter ended with USD 3 billion in reserves, meeting the official annual target. The existing level of gross foreign currency reserves covers 5.1 months of imports.

II. INSTITUTIONAL AND STRUCTURAL REFORMS

Mozambique's Cabinet approved the Green Economy Action Plan (GEAP). The GEAP was prepared to implement the Roadmap for a Green Economy in Mozambique, launched during the RIO+20 conference. The GEAP's strategic objective is to build a model of economic development that is competitive, diverse, and socially inclusive and that efficiently and rationally uses natural resources. It is in line with the country's poverty and development strategies, and it is intended to shape the forthcoming Government's 5-year plan and provide the basis for greening the new National Development Strategy.







III. DONOR COORDINATION ACTIVITIES

Development partners have taken a joint position regarding the EMATUM case, raising concerns with the Government over the operation's impact on debt levels and fiscal sustainability, budgetary and fiscal transparency and expenditure prioritization. Some partners have suspended pending disbursements and new commitments for next year are being reconsidered on the basis of the Government's reaction to the political dialogue and the future course of action to regularize/minimize the issues arising from the deal.

IV. ISSUESS NEEDING PARTICULAR ATTENTION

The EMATUM case has highlighted a number of public finance management framework weaknesses that are symptomatic of broader issues of governance and public policy options. The case should also be framed within the country's current politico-military situation. Additionally, the costly interest service and the fiscal regularization of the operation will further pressure the already large 2014 fiscal deficit. The strengthening of PFM and Public Investment framework is crucial for attaining sound public accounts and prioritizing expenditure on poverty alleviation.

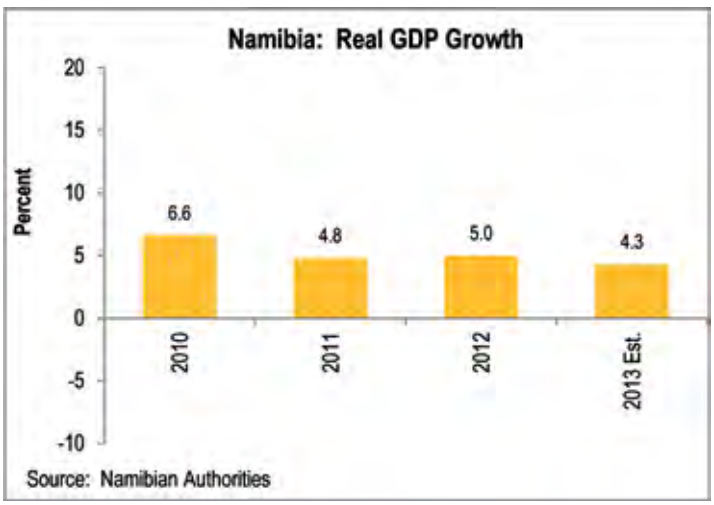
HIGHLIGHTS

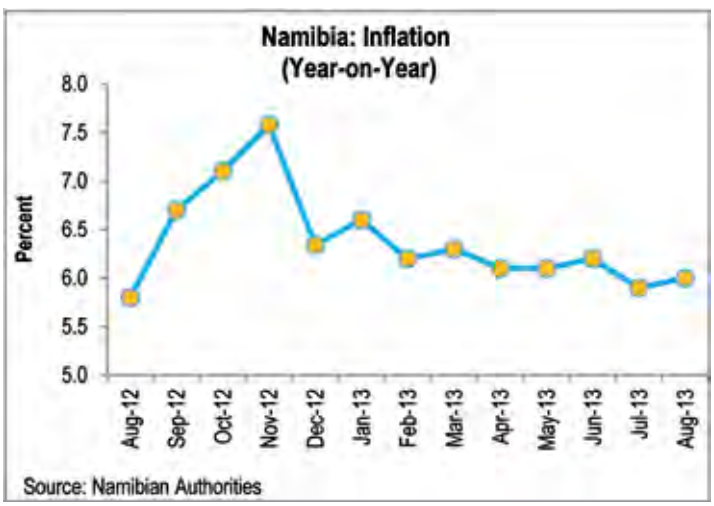
- Real GDP growth was revised downwards from 4.7 percent to 4.3 percent in 2013, reflecting the effects of the severe drought on crop production and a slowdown in mining activities.
- Inflationary pressures continued to ease mainly on account of the decelerating costs of food, non-alcoholic beverages, alcoholic beverages and tobacco.
- The fiscal deficit is expected to narrow substantially on account of lower spending than budgeted, large Southern African Customs Union (SACU) receipts and increased revenue collection.
- Gross reserves declined significantly on account of large increases in the import bill mainly relating to the construction activities in the mining sector.

I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: The Namibian authorities modestly revised down the GDP growth outlook for 2013, from 4.7 percent to 4.3 percent. A weaker external environment than originally expected and prolonged drought conditions are expected to depress growth in mining activities and crop production by the end of 2013. The Namibian economy recovered in the third quarter of 2013, growing strongly by 5.3 percent compared to 2.7 percent registered in the second quarter of 2013. The strong performance was mainly driven by agricultural output reflecting a sustained sharp increase in livestock marketed due to persistent drought and manufacturing output, which expanded strongly by 31.9 percent and 15.2 percent, respectively. During the third quarter, domestic economic growth was held back by the weak performance of the mining sector, which grew at 3.9 percent and the construction sector, which registered a slow growth of 1.4 percent. Downside risks to Namibia's economic outlook associated with the global and South African economic outlook remain elevated. Key risks include weak global recovery for mineral exports that would result in lower export earnings, low international commodity prices, prolonged drought conditions beyond 2013, which could weaken annual growth in agriculture, delays in construction projects, lower SACU receipts due to the economic slowdown in South Africa, and a depreciating exchange rate.

Monetary Policy and Banking System: Inflationary pressures continued to ease, as has been the trend since the beginning of 2013. Year-on-year inflation slowed down to 4.4 percent in November 2013 from 4.9 percent in October 2013, lower than the annual inflation of 6.5 percent for 2012. The slowdown is mainly attributed to decelerating costs of food, non-alcoholic beverages, alcoholic beverages and tobacco. On the other hand, transport and housing inflation increased slightly. Namibia's inflation tracks that of South Africa because of the currency peg and the strong trade ties between the two countries. Annual inflation is expected to hover at the top of the target range of the South African Reserve Bank (SARB) of 3 to 6 percent in 2013 and 2014. The annual credit extended to the private sector remained strong, growing by 13.7 percent at the end of October 2013, compared to 13.3 percent at the end of the preceding month. Credit to individuals rose by 14.9 percent at the end of October 2013, implying that they continued to respond positively to favorable conditions that prevailed in the economy, while credit extended to the corporate sector remained much lower at 11.9 percent. The authorities were, therefore, concerned that bank funding for productive economic sectors might be crowded out. Against the background of a slowing pace in economic recovery, a supportive policy regime was maintained. The Bank of Namibia kept the repo rate unchanged at 5.5 percent.





Fiscal Policy: The lack of an independent monetary policy tool has led to the active use of fiscal policy as a major countercyclical tool to sustain economic growth in the aftermath of the global economic crisis. Reflecting the continuation of increased spending to accommodate the program launched in 2011/12 aimed at stimulating growth and creating jobs, total expenditure is projected to increase to 40.9 percent of GDP in 2013/14, leaving the overall fiscal deficit at 6.4 percent of GDP, from 2.8 percent in 2012/13. A much narrower fiscal deficit is, however, now expected in 2013/14 on account of lower spending than budgeted, the recovery in SACU revenues and increased revenue collection associated with higher domestic economic growth and initiatives to improve the tax administration regime, all of which is driven by higher domestic economic growth. Total public debt increased to 23.1 percent of GDP at the end of the third quarter of 2013 from 22.3 percent at the end of the previous quarter, reflecting

the issuance of Internal Registered Stocks by the Government. Although public debt remains sustainable and significantly below Namibia's fiscal benchmark of 35 percent of GDP, the authorities intend to gradually start unwinding the fiscal stimulus at the end of the 2013/14 with the objective of reaching a balanced budget by 2016/17 in order to ensure fiscal sustainability and to build fiscal buffers. Accompanying measures being pursued to achieve fiscal consolidation include expenditure prioritization, restraining the size of the wage bill (which is over 14 percent of GDP), and strengthening domestic revenue collection and administration.

External Sector: The current account deteriorated, recording a deficit of ND 3.9 billion during the third quarter of 2013, compared with a surplus of ND 3.4 billion during the previous quarter. The deterioration reflects the widening of a merchandized trade deficit by ND 2.2 billion and large net investment income outflows. The net investment income recorded a net payment of ND 2.4 billion during the third quarter, compared to inflows of ND 2.1 billion, mainly due to increased payments to foreign direct investors largely in the form of retained earnings. Given that the recorded surplus in the capital and financial account was not enough to offset the huge outflows in the current account, the overall balance of payments deteriorated significantly, recording a deficit of ND 1.7 billion during the third quarter of 2013, compared to a surplus of ND 1.1 billion during the previous quarter. Namibia's gross reserves declined to 9.19 weeks of import cover during the third quarter of 2013 from 14.35 weeks during the previous quarter on account of large increases in the import bill mainly relating to the construction activities in the mining sector. This development is considered transitory. The stock of international reserves remained sufficient to maintain the currency peg as they were seven times higher than the currency in circulation during the third quarter of 2013. The local currency, the Namibian dollar (pegged to the ZAR) continued to depreciate against all major currencies. By end-December 2013, it had weakened by 21.7 percent, year-on-year, against the USD.

II. DONOR COORDINATION

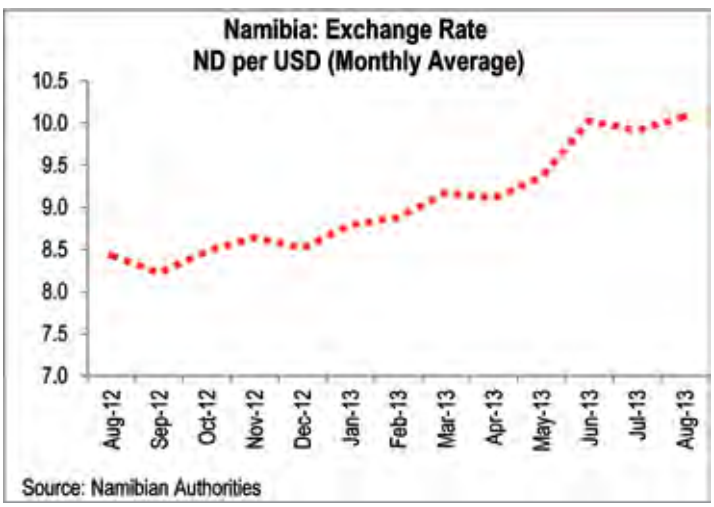
The African Development Bank, the Government of the Republic of Namibia and Namibia Ports Authority (Namport) signed a ZAR 2.9 billion (USD 338 million) sovereign guaranteed loan to Namport to finance the construction of a container terminal at Walvis Bay New Port on 8 November 2013. In accordance with the Bank's Strategy 2013-2022 and focus on infrastructure development and regional integration, the Bank approved the construction of the New Port of the Walvis Bay Container Terminal Project in July 2013. The project is expected to enable Namport to triple the container-handling capacity at the Port of Walvis Bay from 350,000 TEUs to 1,050,000 TEUs per annum. It will also finance the purchase of up-to-date port equipment and the training of pilots and operators for the new terminal. The Bank also provided a UA 1.5 million grant (USD 2.3 million) to the Government of Namibia, which will fund the preparation of the National Logistics Master Plan study, technical support and capacity-building for the Walvis Bay Corridor Group and the training of freight forwarders.

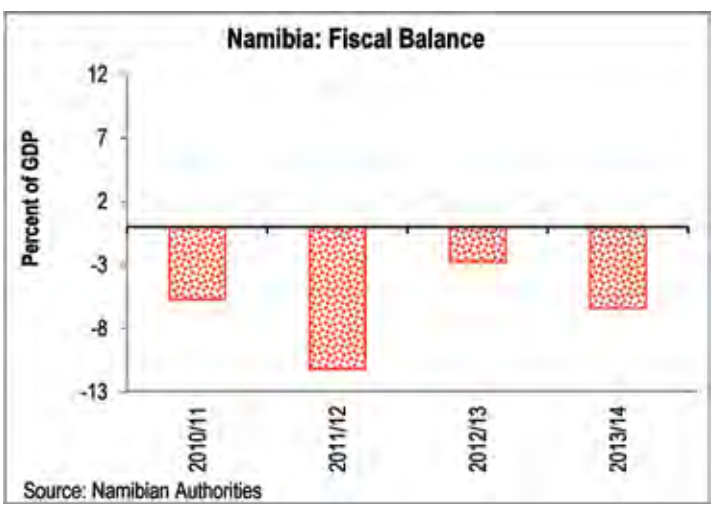
III. INSTITUTIONAL AND STRUCTURAL REFORMS

The draft Public Procurement Bill, which was tabled in Parliament by the Minister of Finance, was withdrawn in October 2013 after members of the public and some parliamentarians expressed reservations about certain aspects of the Bill. The Bill, if enacted, will modernize Namibia's public procurement system by strengthening the legal and regulatory framework for procurement and establishing an independent procurement oversight body, among other things.

IV. ISSUES NEEDING PARTICULAR ATTENTION

Namibia's medium-term growth prospects remain vulnerable to various endogenous and exogenous shocks, as demonstrated by the recent downgrading of GDP growth expectations for 2014 by the authorities. The risks underscore the need for Namibia to intensify efforts to diversify the economy in order to promote economic transformation that will enhance the resilience of its medium-term growth prospects.





SÃO TOMÉ AND PRÍNCIPE

HIGHLIGHTS

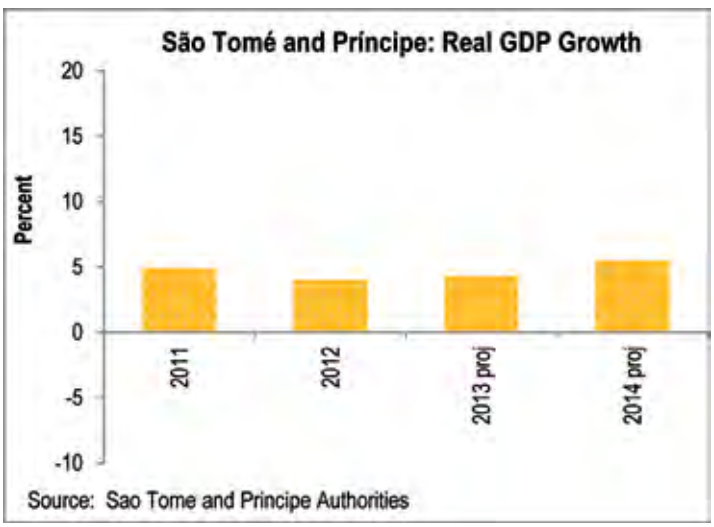
- Parliament approved the 2014 State Budget estimated at USD 159 million.
- Government received USD 5 million in oil signature bonus from bloc 2 of its Exclusive Economic Zone (EEZ).
- Inflation hits its record low of 6 percent in more than twenty years.

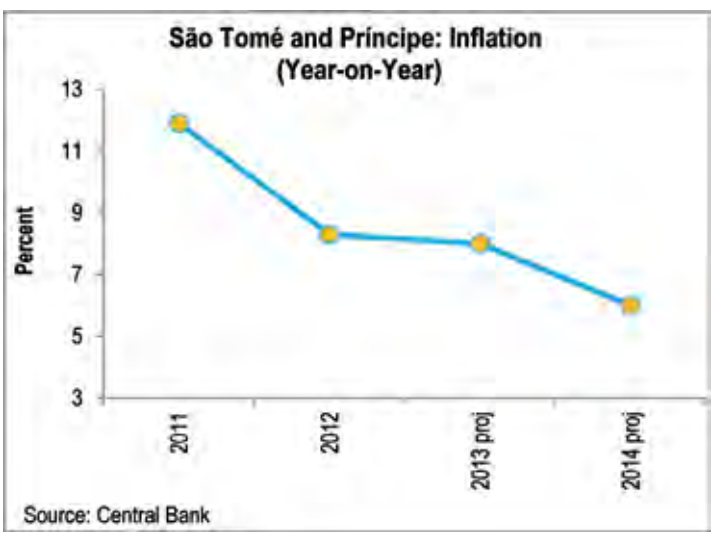
I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Growth forecast in São Tomé for 2013 has been adjusted downward to 4 percent for 2014 from 5.2 percent due to delays in disbursements for project execution and weak financing prospects for both private and public-sector projects. The negative projection is also linked to some extent to the announcement by TOTAL to abandon oil exploration in block 1 of the Joint Development Zone (JDZ) with Nigeria, due to exploration costs and the size of the oil reserves. Following the announcement of Total, the National Petroleum Agency (ANP) has confirmed the existence of oil reserve in block 1 with production capacity of 19,000 barrels per day for a period of 15 years. In addition, the Government also announced receipt of USD 5 million in an oil signature bonus from Sinoangola, a consortium of Chinese and Angola Company, from block 2 of its Exclusive Economic Zone (EEZ). The consortium group is expected to invest USD 154 million on environmental impact studies, seismic surveys in block 2, drilling block and evaluation of existing resource. The service sector continues to be an engine of growth followed by agriculture.

Monetary Policy and Banking System: The ongoing fixed exchange rate agreement signed with the Government of Portugal in January 2010 helped to sustain the inflation trends over the years. In December 2013 the Central Bank announced that inflation hit its record low to 6 percent in more than twenty years, compared to 11 percent registered in the same period in 2012, representing a monthly percentage change of 1 percent impacted by the following products;:medical expenses – 2.2 percent; clothes and shoes – 1.4 percent; and food, drinks and cigarettes – 1.4 percent, among other things. In November 2013, the money in circulation and the commercial banks deposit in the Central Bank (CB) contracted by 0.08 percent and 0.42 percent respectively mainly linked to a decrease in foreign currency deposit by 4.37 percent. The increase in credit to the Government (2.26 percent), and the slight recovery of credit to the economy (0.34 percent) was among the factors that contributed to money growth (2.66 percent in November 2013 against 1.11 percent recorded in October 2013). While the credit to economy is expected to reach 9.4 percent in 2013 against the 7.6 percent initially projected, the Central Bank (CB) kept its requirements for unprofitable banks and maintained the capital adequacy ratio to above 10 percent.

Fiscal Policy: Contrary to the 2013 budget (estimated at USD 150 million), the approved 2014 State Budget estimated at USD 159 million is more ambitious within the context of the global economic challenge and the country´s high dependence on external aid. The social sector and infrastructure remained the Government´s priority in the public investment plan. Despite the positive economic performance acknowledged during the second review held in September 2013 under the extended credit facility (ECF) program of 2012 to 2015 with the IMF, the decrease of the tax revenue to 13 percent of GDP in 2013 from 14 percent recorded in 2012 affected the fiscal performance. The domestic primary deficit is estimated at 6.5 percent in 2013 against 10.1 percent of GDP reported in 2012. High concessional loans, given the country's weak debt position, from multilateral institutions and bilateral will continue to be the Government´s main avenue to finance the budgetary gap. According to the IMF and WB Debt Sustainability Analysis (DSA) undertaken for low and medium-income countries, STP is at high risk of debt distress. Under the non-oil baseline scenario and fiscal adjustment, the public debt (both NPV of debt-to GDP and the NPV of debt-to revenue ratios) will rapidly increase. After benefiting from Highly Indebted Poor Countries (HIPC)[1] initiative, the country stock of debt at the end of June 2013 was estimated at USD 222.4 million, of which USD 40.4 million was owed to multilateral donors and USD 182 million to bilateral creditors. Portugal remains the lead bilateral creditor (USD 41.8 million), followed by Angola (USD 23 million).





1 Prior to qualifying for the HIPC, the stock of debt was anchored at USD360 million in 2006.

SÃO TOMÉ AND PRÍNCIPE

External Sector: Despite the projected improvement in the trade balance deficit (35.5 percent in 2013 compared to 39 percent in 2012), the current account deficit, including transfers, is projected to improve to 16.6 percent of GDP in 2013 from 21.4 percent in 2012, reflecting an improvement in current transfers. In November 2013, the level of foreign reserves declined to 5.68 month of imports (at around USD 37.7 million) from 5. 92 registered in previous month, which is still above the minimum requirement of 3 months of imports. In 2013, the net foreign reserve is estimated at USD 45.8 million. Remittance, which is a major source of private consumption, is expected to remain low in 2013 due to the ongoing fiscal crisis in Portugal where many São Toméans are based and work. In spite of the poor performance in recent years, FDI is expected to recover to USD 26 million from 2013 to 2015. Over the years, there has been a decline in FDI inflows to the country to 9.1 percent in 2013, from 43.1 percent registered in 2008. Furthermore, in the third quarter of 2013 the average FDI inflow to the country stood at USD 8.7 million against USD 47.5 million reported in Q2 2013 reflecting the negative impact of the global economic turmoil.

II. INSTITUTIONAL AND STRUCTURAL REFORMS

The new Government, appointed in December 2012, is set to continue implementing key reforms to enhance transparency and accountability in the management of public funds. The 2013 budget was managed and executed through the SAFE public finance management system. Other key measures included the participation of civil society in policy dialogue and project implementation. Key Government reforms undertaken included enforcing compliance with tax laws, simplifying customs procedures, and controlling current expenditure. Enforcement of a macro-fiscal unit towards the implementation of the medium-term fiscal framework was also a key measure. In addition, the Government will be instituting an IT system, scheduled for the first quarter of 2014, to monitor arrears from the water and energy company (EMAE).

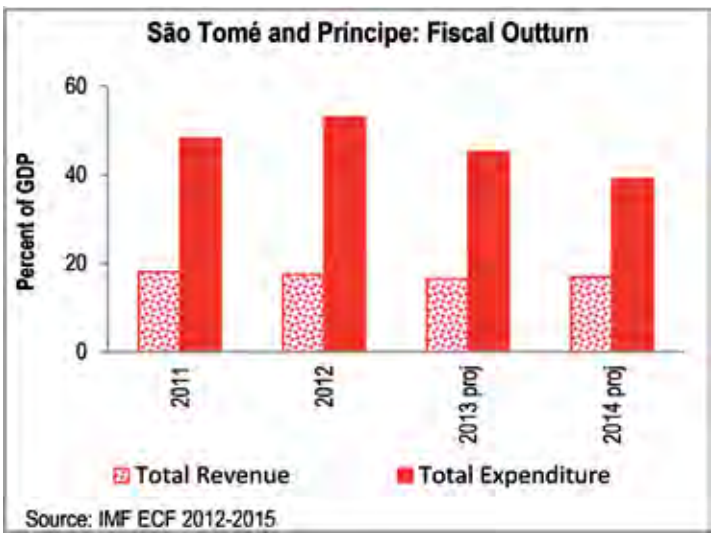
The private sector is undeveloped and in need of improvement. Conscious of the challenges, the Government is making progress in unleashing the country's potential. To this effect, an operating license has been awarded to the Angola giant telecommunication company, UNITEL. In September 2013, the Government with the support of the IFC and ICF launched the single window for the external sector by introducing the SYDONIA software system at the customs department. The system will help to, (i) harmonize policy and procedures; (ii) reduce transport cost on the import and export of goods; (iii) improve coordination between line Ministries; and, (iv) provide incentives for exports. More importantly, it will help improve transparency and modernize the customs department.

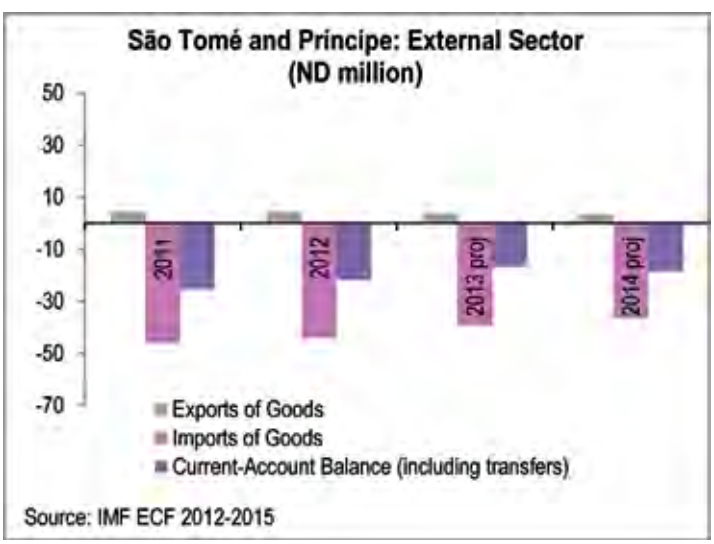
III. DONOR COORDINATION

As coordination among donor partners is weak, significant efforts are required to develop joint initiatives. Nevertheless, the Government is making progress in mobilizing additional resources from bilateral donors and seeks opportunities to further enhance relations with external communities. In this connection, in December 2013, the Government organized a meeting with its development partners under the theme – Economic Diplomacy and the Opportunities for the country. The need for the country to strengthen south-south cooperation and development of key infrastructure was thought to be to country´s key avenue for economic transformation. To complement the Government efforts, donors with representation in STP held a meeting and discussed the implementation progress of the Donor Coordination Unit (UCA), which is to be set up at the Ministry of Foreign Affairs.

IV. ISSUES NEEDING PARTICULAR ATTENTION

The fragile political outlook due to the new ruling coalition, a divided political scene and prospects of an early election might delay the implementation of key reforms and lead donors to withhold pledged funds. Other issues include: (i) developments in the oil sector as a result of Total's unexpected withdrawal from block 1 of JDZ, and (ii) close attention to political developments. Efficient expenditure control, as well as caution in implementing the 2014 budget, is imperative amidst the upcoming legislative and municipalities elections scheduled for August 2014.





SÃO TOMÉ AND PRÍNCIPE

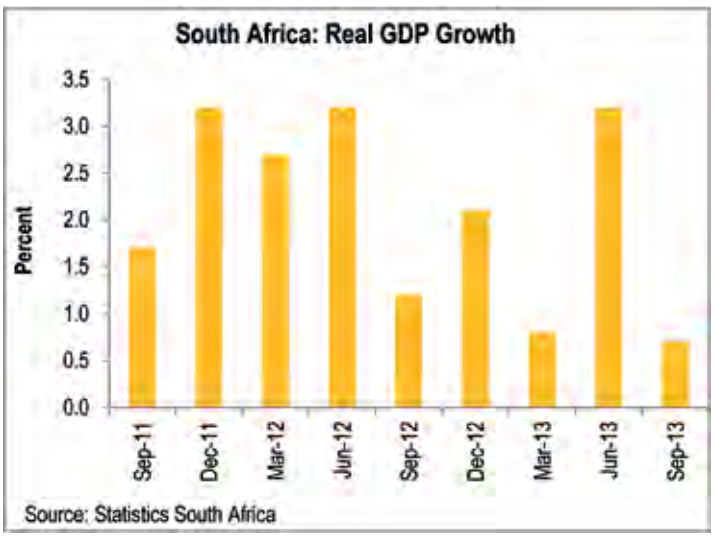
SOUTH AFRICA

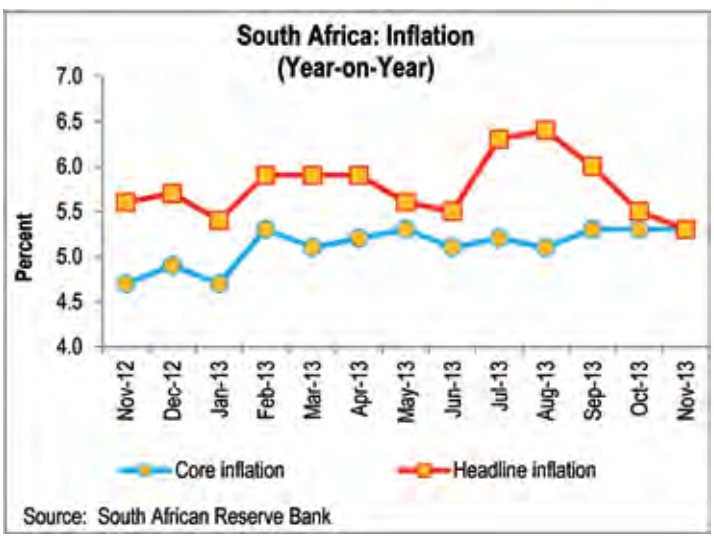
HIGHLIGHTS

- Due to contraction in manufacturing production, economic activities decelerated during the third quarter, registering a real GDP growth of just 0.7 percent, compared to 3.2 percent during the preceding quarter.
- The unemployment rate fell to 24.7 percent in the third quarter from 25.6 percent in the second quarter.
- The enactment into law of the Employment Tax Incentive Bill will go a long way towards addressing the chronic high level of youth unemployment facing the country, if effectively implemented.

I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Economic growth decelerated during the third quarter to 0.7 percent from 3.2 percent in the second quarter. As a result, the economy grew by about 1.9 percent during the first 9 months of 2013 compared to the corresponding period in 2012. This remains significantly below the estimated potential growth rate of 3.5 percent, indicating the widening negative output gap. The decline in economic growth during the third quarter was due mainly to the contraction in manufacturing activities by 6.6 percent. The contraction in the manufacturing sector was due to lower production in motor vehicles, parts and accessories and other transport equipment as a result of a prolonged strike in the sector. On the other hand, mining output expanded by 11.4 percent, contributing 0.6 of a percentage point to growth. The expansion in the mining sector was due largely to higher production in the mining of platinum and related metals, as well as higher diamond mining production. Moreover, real output in the agricultural sector expanded by 3.6 percent in the third quarter, from a negative growth of 3 percent during the previous quarter due mainly to improved horticultural and animal production. On the other hand, growth in the tertiary sector fell to 1.3 percent in the third quarter from 2.2 percent in the second quarter. The unemployment rate decreased to 24.7 percent in the third quarter of 2013 from 25.6 percent in the second quarter while the absorption rate and labour force participation rate increased by 0.8 and 0.4 of a percentage point to 41.9 and 55.7 respectively in the quarter. The economy created 308,000 jobs between the second and third quarters. On the demand side, growth in real gross domestic expenditure decelerated to 1.9 percent in the third quarter from 2.7 percent in the second quarter. Likewise, growth in real gross domestic final demand declined to 2.2 percent in the third quarter from 2.5 percent during the second quarter, mainly due to the moderation in real final consumption expenditure by households and general government. Nevertheless, final consumption expenditure by households was the largest contributor to GDP growth with 1.5 of a percentage point while real net exports subtracted 1.3 of a percentage point from growth in the third quarter of 2013. Consumer spending slowed due to sustained weak employment growth and restrictive credit conditions. Consistent with the slower rate of increase in household spending, the ratio of household debt to disposable income decreased from 75.8 percent to 75.5 percent in the third quarter while the cost of servicing debt as a percentage of disposable income remained at 7.7 percent from the first to the third quarter of 2013. Real gross fixed investment by private business enterprises declined to 2.6 percent in the third quarter, from 3 percent in the second quarter. This was mainly due to moderation in capital outlays in most sectors except mining and transport. Real fixed investment by public enterprises increased by 0.1 percent in the third quarter from a negative growth of 0.8 percent recorded in the preceding quarter. Economic growth was held back by supply-related constraints during the previous quarters and as a result real output is likely to remain subdued for 2013 as a whole.





Monetary Policy and Banking System: After breaching the upper bound of the monetary policy target range in July and August 2013, consumer price inflation fell back within the policy range in the third quarter of 2013, reaching 5.5 and 5.3 percent in October and November respectively. The slowdown in inflation was due to moderation in food inflation and an increase in petrol prices. Food inflation fell to 4.3 percent in October from 6 percent in September while petrol prices increased by 9.3 percent on an annual basis in October compared to 12.8 percent in September. The upside risk to inflation still remained elevated, due mainly to the continued depreciation of the rand against major currencies, and the tapering of the US bond-purchasing program. Core inflation remained unchanged at 5.3 percent for three consecutive months ending in November 2013. Total

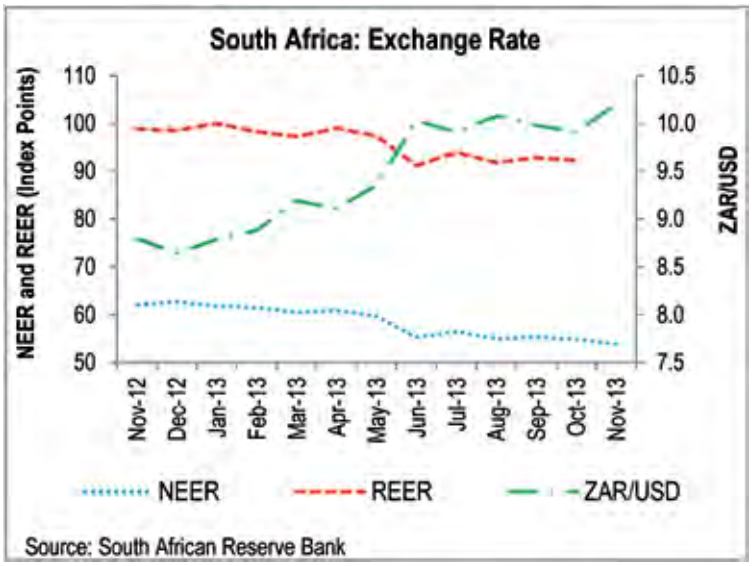
inflation of both regulated and non-regulated administered prices also declined to 7.3 percent in November from 7.8 percent in October 2013, reaching its slowest level since June 2013. Inflation is expected to average 5.8 percent in 2013. The South African Reserve Bank nevertheless left the discount rate unchanged at 5 percent at its November Monetary Policy Committee meeting. Weak demand conditions in the economy, continued supply disruptions, low business and consumer confidence, as well as slower bank credit to households all underpinned the Monetary Policy Committee's decision. Twelve-month growth in general loans to households, mostly unsecured lending, declined to 14.2 percent in September 2013, the lowest rate since February 2010.

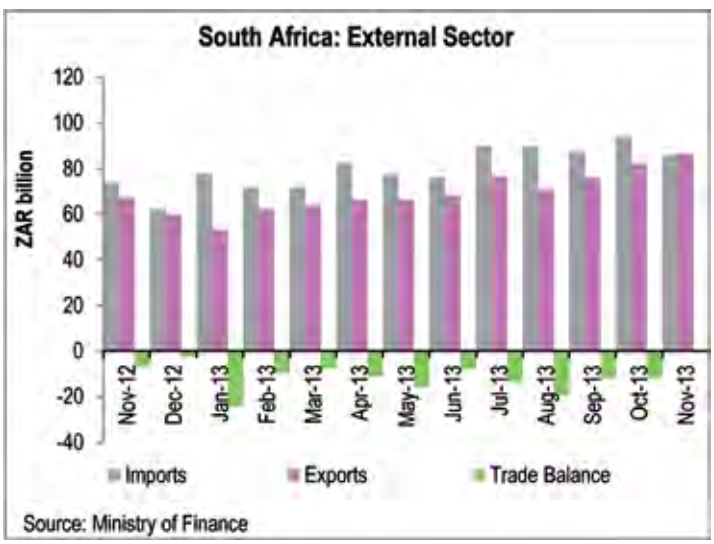
Stock Exchanges: The analysis of five-year (2009-2013) performance and volatility of the FSTE/Johannesburg Stock Exchange (JSE) All-Share Index and the FTSE/JSE Top 40 Index reveals that the bourse has performed well despite global and domestic economic weaknesses. The one-year return in rand for the All-Share index was 21.4 percent, compared to 22.8 percent for the Top 40 Index at the end of December 2013. The Top 40 Index remained more volatile than the All-Share Index with volatility reaching 15.8 percent for one year and 16.3 percent for 5 years compared to 14.4 percent for one year and 14.9 percent for five years for the All-Share Index. The market capitalization for the entire bourse was ZAR 10,518 billion at the end of December 2013.

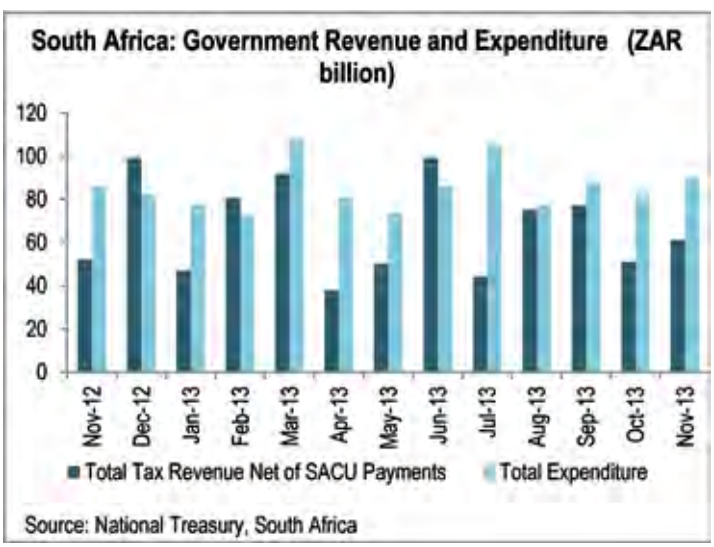
Fiscal Policy: From April to September 2013 the national Government revenue net of SACU payments increased by 10.1 percent and reached ZAR 398.5 billion (23.4 percent of GDP), mainly due to higher income tax collections. On the other hand, spending by the national Government amounted to ZAR 504 billion (29.6 percent of GDP) during the period under review, leading to a deficit of 6.2 percent. However, the primary deficit declined to 3.3 percent between April and September 2013 compared to 3.7 percent during the same period the previous year. Despite the less expansionary fiscal policy stance to rein in the deficit, Government spending continues to outstrip Government revenue with persistent month-on-month fiscal deficits.

South Africa's total outstanding external debt declined markedly from USD 140.6 billion at the end of March 2013 to USD 130.4 billion at the end of June due mainly to the decline in the rand-denominated debt. Total foreign debt was 35.4 percent of GDP and 111.5 percent of export earnings at the end of the second quarter of 2013. Total gross loan debt, comprising domestic and foreign debt, increased from ZAR 1.366 billion to ZAR 1.487 billion between March and September 2013, rising from 42.7 percent to 44.7 percent during the period under review.

External Sector: South Africa registered a trade surplus of ZAR 0.8 billion in November 2013 from a deficit of ZAR 11.8 billion in October 2013 for the first time in a decade, following the inclusion of trade data from the SACU countries in the calculation of the balance of payments. The trade balance had been in deficit for 22 consecutive months since January 2012. Nonetheless, in spite of the revision of balance of payments calculation methodology, the deficit on the current account widened from 5.9 percent in the second quarter of 2013 to 6.8 percent of GDP in the third quarter. This was mainly due to strong import demands for manufactured goods and mineral products amid slower growth for the demand of South Africa's exports and weaker rand.





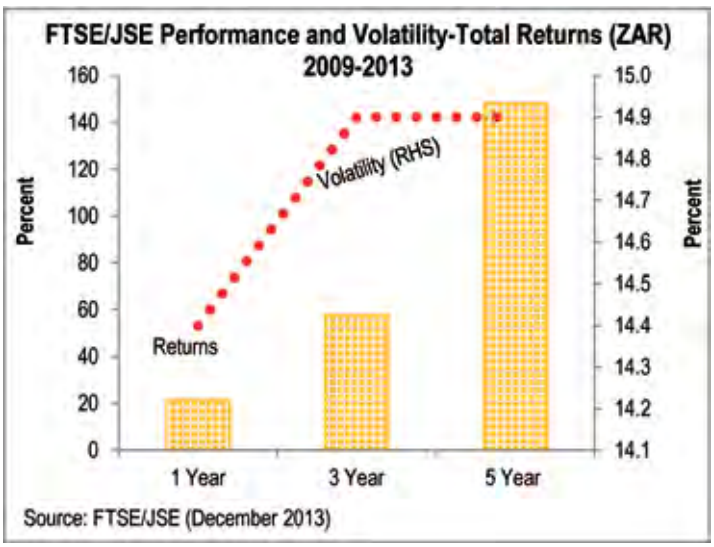


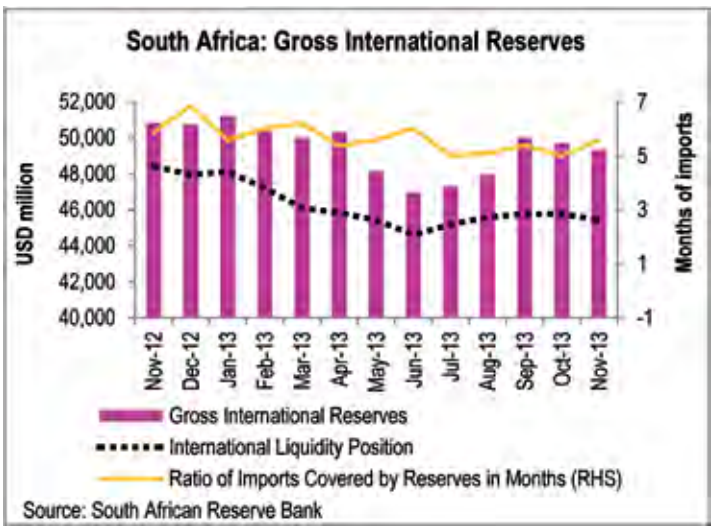
The current account deficit was fully financed by capital inflows. In spite of the country's subdued economic growth performance and continued labor market tensions, the net capital inflows reached ZAR 81.8 billion in the third quarter of 2013 from ZAR 34.7 billion in the second quarter. Inward FDI reached ZAR 47.4 billion in the third quarter of 2013 from ZAR 16.6 billion in the second quarter. Portfolio investment surged to ZAR 48.8 billion during the third quarter of 2013 from an outflow of ZAR 5.2 billion in the second quarter. The balance on the financial account therefore reached 9.5 percent of GDP during the third quarter of 2013, up from 4.1 percent in the previous quarter.

Between September and November 2013 the rand depreciated by 1.9 percent against the euro, 1.2 percent against the USD and 3.1 percent against the yen, while the nominal effective exchange rate depreciated by 3.5 percent in the third quarter of 2013. In November 2013, the rand weakened further as the USD strengthened on the back of stronger GDP growth data. On the other hand, the real effective exchange rate of the rand declined by 15.2 percent from March 2012 to September 2013, leading to a significant improvement in the external price competitiveness of South African exports. Widening annual current and fiscal account deficits, lower commodity prices, weak economic growth, and lingering labor unrest also contributed to the continued weakening of the rand. Gross international reserves continue to increase, reaching USD 49.3 billion in November 2013 from USD 46.9 billion in June, covering about 5.8 months of imports.

II. INSTITUTIONAL AND STRUCTURAL REFORMS

The Government signed the Employment Tax Incentive Bill into law in December 2013. The Act will encourage private employers to employ young workers by providing a tax incentive to the former, with Government sharing the costs of such employment for a maximum of two years. More specifically, the Bill involves a 50-percent subsidy for the employment of the first-time workers between the ages of 19 and 29, earning between ZAR 2,000 and ZAR 6,000 per month, including workers who have completed high school and those employed in Special Economic Zones. The incentive involves deductions in the amount of pay-as-you-earn tax that is payable to the South African Revenue Authority for every qualifying employee that is hired by the employer. The Government contends that this incentive will allow many unemployed young people to gain work experience and develop their skills, thereby improving their prospects for better employment opportunities. The incentive is available to all private-sector employers in all sectors of the economy who are registered with the tax authority. South Africa is currently facing a major challenge of high and rising unemployment with youth unemployment above 50 percent. The Government's previous attempts to address the challenge of youth unemployment were stalled due to strong opposition from the ANC's ruling Alliance partner, COSATU, which argued that the youth wage subsidy would lead to businesses replaced its older members by the new recruits. The Act will become effective on 1 January 2014.





South Africa's new Promotion and Protection of Investment Bill approved by the Cabinet in November 2013 caused considerable consternation among South Africa's largest trading partner, the EU member states, and investors. The Bill intends to replace about 13 bilateral investment treaties with EU member states with a comprehensive and uniform legal framework to govern investment. The Government states that the Bilateral Investment Treaties (BITs), which were signed after 1994 had loopholes that were exploited by the legal and business community to challenge regulatory changes, which the Government considered to be in the public interest. In particular, the Government believes that these treaties hindered the achievement of Black Economic Empowerment (BEE) goals and therefore failed to facilitate economic transformation. Following the adoption of the Bill, the Government canceled BITs with Germany, Luxemburg, Belgium, Spain and Switzerland. The proposed law will exclude any recourse to international arbitration to ensure that foreign investors will not challenge South African laws and measures through international arbitration in the future. Investors fear that the new law would

allow the Government to provide less than market-value compensation in cases of expropriation. However, the Government assured the investors that the unified investment law will protect any rights in the South African Constitution and protect investors from arbitrary decision-making by the authorities.

III. ISSUES NEEDING PARTICULAR ATTENTION

Structural unemployment remains South Africa's single most important development challenge. Youth unemployment of above 50 percent remains the third largest in the world while the labour force absorption rate of 41 percent is one of the lowest globally. The employment tax incentive reform enacted into law at the end of 2013 is an important step in the right direction to address the scourge. Nonetheless, the Government needs to ensure that the incentive system is implemented effectively by ensuring higher uptake and avoiding undue abuses by the private sector.

SWAZILAND

HIGHLIGHTS

- The windfall SACU receipts pushed economic growth in 2012 to 1.7 percent and estimations put growth at about 3 percent in 2013.
- Despite an improved fiscal position, total debt increased by slightly more than 2 percentage points, rising from about 16 percent to 18 percent of GDP during the second half of the year.

I. MACROECONOMIC MANAGEMENT OVERVIEW

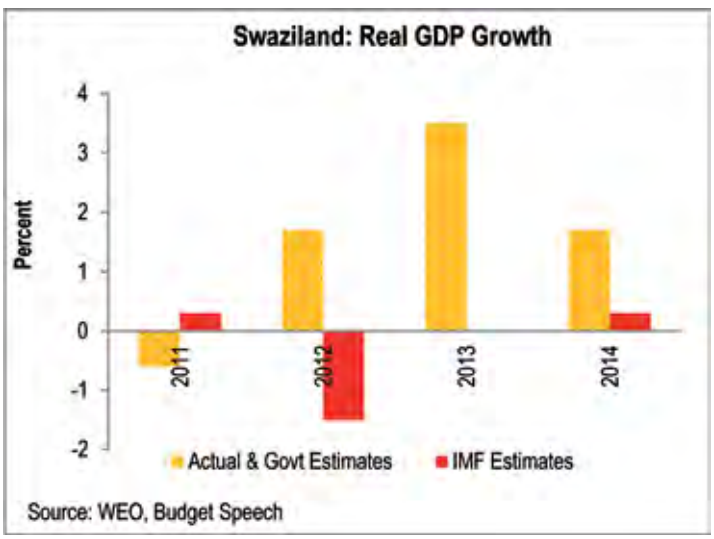
Economic Growth: The latest revision of economic data put growth in 2012 at 1.7 percent, significantly higher than the projected decline in economic activity of 0.3 percent, and a reversal of the economic contraction of 0.6 percent in 2011. The higher-than-expected recovery in the tertiary sector helped compensate for the slowing growth in the primary sector and the continued decline in the secondary sector. The tertiary sector decline of 1.2 percent in 2011 was reversed to a positive growth of 2.5 percent in 2012. The transport, storage and communications sector experienced the largest growth at 19.3 percent in 2012, compared to 2.7 percent the previous year. In 2013, growth was estimated to be about 3.5 percent as all sectors of the economy recorded positive growth.

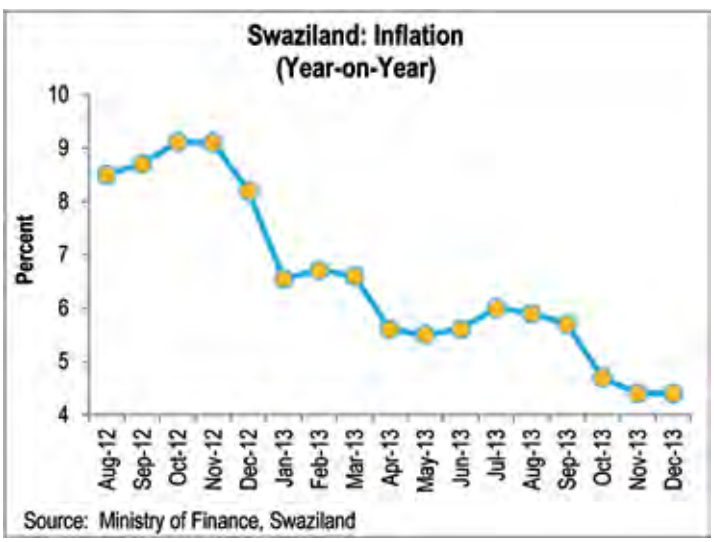
The supply side of the economy saw manufacturing output increase in response to the recovery in export demand. The soft drink concentrates, sugar and sugar-related products, timber and textiles subsectors registered positive growth of above 2 percent. Similarly, electricity, gas and water supply recovered from a contraction of 20.9 percent in 2012 to positive growth in 2013 on account of favorable rains in the 2012/13 summer season. On the other hand, higher public capital expenditure supported continued recovery in the construction sector. The services sectors, especially communications, could have seen higher growth had the expected reforms in the sector been implemented to boost demand and investment.

Monetary Policy and Banking System: Monetary policy has largely been accommodative and tracks that of the South African Reserve Bank. The discount rate has been maintained at 5 percent since July 2012 and the prime lending rates are at 8.5 percent. An improving macroeconomic environment and the stability of the financial sector have helped in rebuilding confidence in the economy, with interests on treasury bills falling from a peak of about 8 percent during early 2012 to about 6 percent by end-2013.

Reflecting the positive macroeconomic environment and the growth of the economy, key monetary aggregates recorded positive growth in 2013. Annualized private-sector credit grew by 6.5 percent as of end-November 2013 while public-sector credit contracted. On a month-on-month basis, private-sector credit increased by 21.6 percent in November, the largest recorded for the year. The healthier fiscal position allowed gross foreign reserves to increase from SWZ 6.9 billion in January to SWZ 8.2 billion in November 2013. Average foreign reserves for the final quarter of the year stood at 4.7 months of import cover. The large inflow of SACU receipts also largely accounted for the improved foreign reserves position of the country. The growth in foreign reserves also had an impact on money supply growth. After peaking at more than 25 percent in February 2013 broad money supply (M2) growth slowed to 11.5 percent in June before picking up to about 18 percent in July. By the end of the year broad money supply had grown by 16.1 percent. The depreciation of the lilangeni/rand exchange rate against major currencies also influenced the growth in money supply, given the rising foreign reserves.

Price pressures continued to wane, with headline inflation declining from a peak of 5.7 percent in September 2013 to 4.4 percent in December, driven mainly by decreases in the price of food and non-alcoholic beverages, which constitute about 29 percent of the CPI basket. Government, for the greater part of 2013, controlled fuel prices, thereby reducing the inflationary impact of the transport sector.





Fiscal Policy: The absence of an institutionalized framework to manage SACU receipts, upon, which Swaziland depends for 55 percent of its total revenue in 2013/14, increases the medium-term fiscal and debt risks for the country. Intermittent cash flow challenges in 2013/14 resulted in the temporary accumulation of domestic arrears. Overall, the fiscal position

is now estimated to be in surplus of almost one percent. Despite an improved fiscal position, debt has risen from about 15 percent at the beginning of the year to 18 percent by end-2013. External debt increased from 7.7 percent to 9.7 percent of GDP over the same period. Short-term debt as a proportion of total debt rose rapidly from 16 percent in 2009/10 to 30 percent in 2012/13 and Government is making efforts to reduce short-term borrowing by issuing long-term paper – in August 2013 a 5-year bond was issued at a fixed coupon rate of 8.5 percent. Since the establishment of the Swaziland Revenue Authority, domestic tax collections have increased. Domestic tax revenue has, however, remained at less than 15 percent of GDP over the last two years. Overall, total revenue is expected to continue dropping from the current 33 percent of GDP to 31 percent in 2014/15; total expenditure is also expected to drop from 36 percent to 34 percent of GDP over the same period. The fiscal position is therefore not expected to be impacted significantly.

External Sector: Swaziland recorded an overall balance-of-payments (BOP) surplus of E82.3 million during the third quarter of 2013, compared to a surplus of E629.4 million in the previous quarter. As opposed to 2012 when economic activity was depressed, growth in 2013 has been accompanied with higher import levels. The current account, although boosted by current transfers, has not avoided the decline in the balance of payments as the financial account was persistently in deficit. Net FDI and portfolio flows and net incomes have been largely negative during the year, hence the smaller surplus on the balance of payments. Investment enquiries in the forestry sector and the property market could result in net inflows on the investment account in 2014. Net FDI was positive, at more than E750 million, both in 2011 and 2012 compared to almost E1 billion in 2010, while the net portfolio was largely negative. As a result, in 2013, the Government had to impose a minimum capital investment of 30 percent for locally based financial institutions.

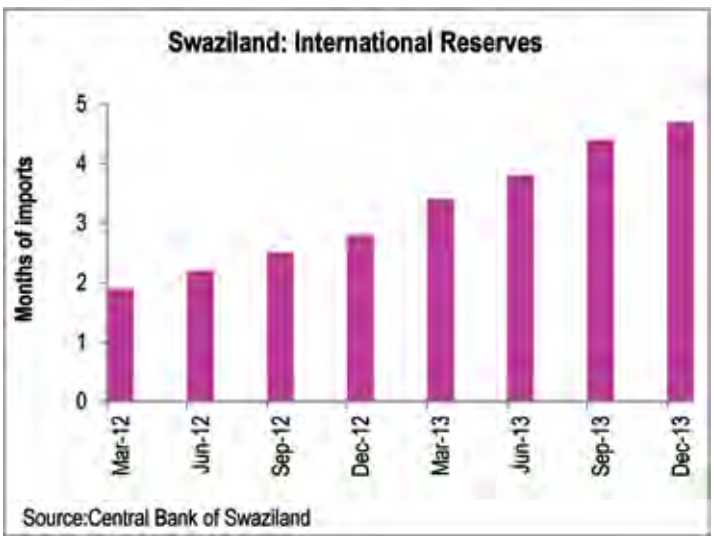
II. INSTITUTIONAL AND STRUCTURAL REFORMS

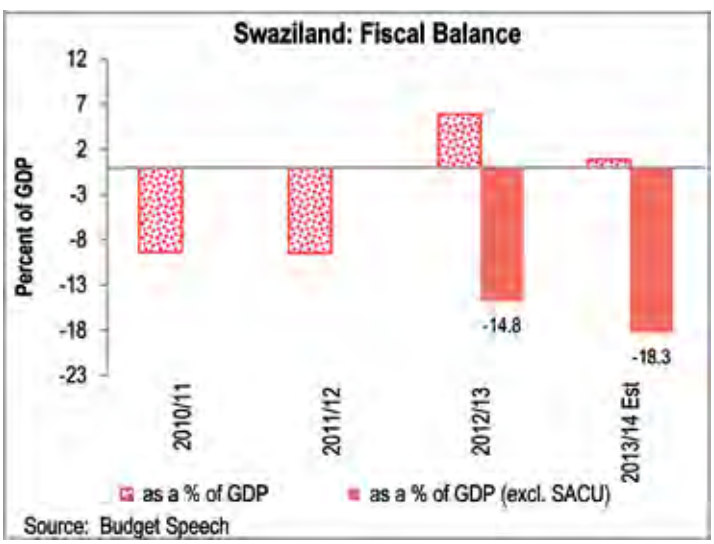
Swaziland held its parliamentary elections in September 2013 and the voter turnout was 65 percent. The election of women in Parliament, however, was disappointing. Only one out of the 22 women won her seat. His Majesty the King and the Parliament nominated 9 women, bringing the representation of women to 15.4 percent. Women representation at the community levels showed a similar pattern with some regions registering an even smaller female representation. By end-2013, the drafting of the National Legal Aid Policy and the Legal Aid Bill, which seeks to promote access to justice for marginalized groups in particular, had been completed. The Government, as part of strengthening the Commission on Human Rights and Public Administration, is also in the process of setting up the Commission's secretariat, which is envisaged to be operational by March 2014.

Attempts at improving the business environment are continuing, especially as the task force monitoring the implementation of the Investor Road Map has remained active and committed. Some progress has been noted, with regard to competitiveness and Ease of Doing Business. Swaziland rose one rank up, from 124 in 2012/13 to 123 in 2013/14 in the Ease of Doing Business rankings. The Global Competitiveness Report ranked Swaziland 11 places higher in 2013/14, from 135 to 124 out of 148 countries. Most of the improvement was recorded in the macroeconomic environment and in financial market development.

III. DONOR COORDINATION ACTIVITIES

Activities surrounding the election process left no space for planned donor meetings in the second half of the year. The annual Donors' Retreat was postponed to the first quarter of 2014. To promote coordination of the Bank's activities, the SARC hosted the United Nation Country Team at its offices on 13 November 2013. The purpose of the meeting was to enhance strategic partnerships geared towards more effective and harmonized delivery of interventions in support of the attainment of Swaziland's national development priorities. In this context, the meeting was in line with the Paris Declaration and the 2011 Bussan Outcomes.





IV. ISSUES NEEDING PARTICULAR ATTENTION

Whereas the fiscal policy should be focused on consolidating the fiscal position, reducing wastage and improving efficiency in resource allocations, there is evidence that the Government is adopting an expansionary fiscal stance, with the objective of supporting growth. Development partners should therefore be geared to accelerate their assistance in public financial management reforms so as to reduce wastage of resources.

HIGHLIGHTS

- Fitch downgrades sovereign credit rating one step to B, while S&P downgrades outlook to negative.
- Government revises estimates for real economic growth to 6.5 percent for 2013. Real growth projected at 7.3 percent in 2014.
- Budget deficit in 2013 estimated at 9 billion (8.5 percent of GDP), almost double the planned deficit.

I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: The Ministry of Finance released a revised estimate for 2013 real economic growth in the fourth quarter, raising annual GDP growth to 6.5 percent from the 6.0 percent that was announced in the third quarter. The four sectors driving the economy include mining and quarrying; transport and communications; construction; and the hospitality sector, i.e. hotels, bars and the restaurant sector.

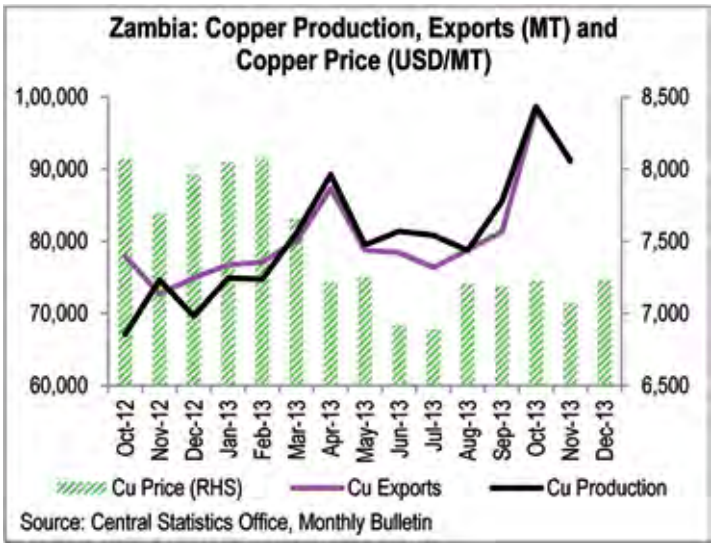
Mining, the most important sector for foreign currency earnings, continued to expand as new investments increased production capacity. According to the Central Bank fourth quarter production increased by more than 10 percent compared to the previous quarter. For the first 11 months of 2013 total production increased by 21 percent relative to the same period in 2012. Year-end total production is estimated to reach more than 980,000 MT (metric tons).

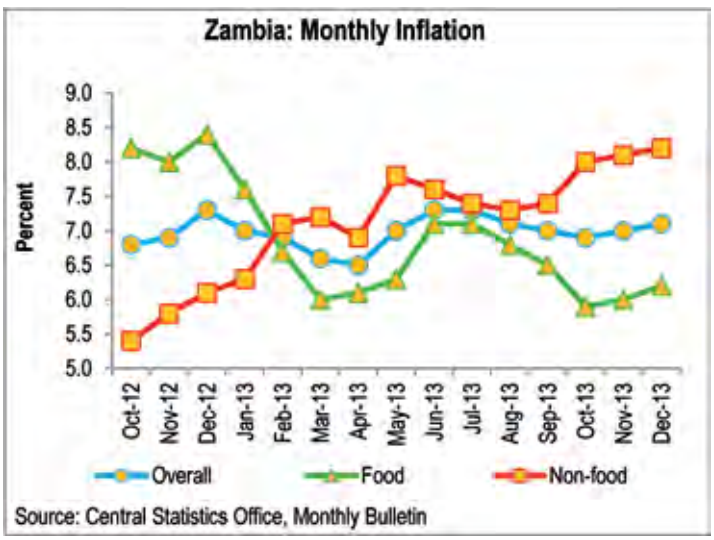
Copper prices during the fourth quarter have on average been higher than in the previous quarter. The average price per metric ton in December was USD 7,229, up from USD 7187 in September.

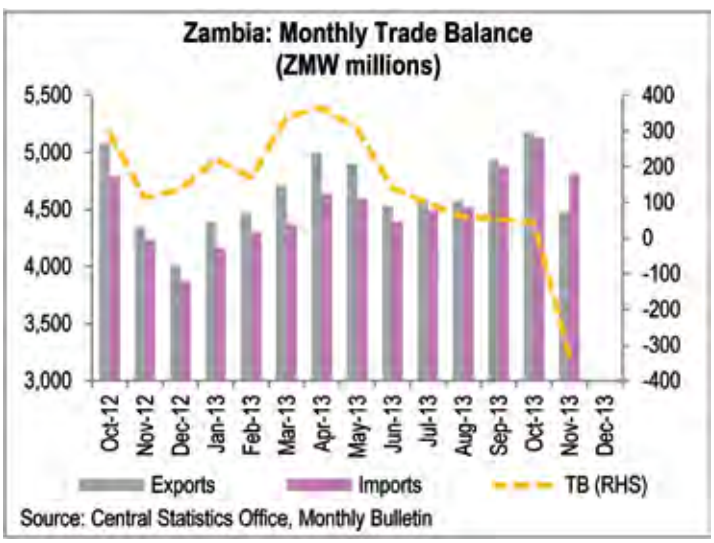
Agricultural production fell due to a reduction in maize and cotton output by 10 percent and 50 percent, respectively, as reported in the previous quarter. This is estimated to reduce total agriculture value added by 7.4 percent for 2013.

Monetary Policy and Banking System: Inflation during the fourth quarter continued to stabilize from the third quarter. Annual inflation reached 7.1 percent, slightly lower than the 7.3 percent in 2012. Food inflation was on average lower in the fourth quarter than in the previous quarter. Food inflation by the end of the quarter reached 6.2 percent compared to 6.5 percent by the end of the third quarter. Most food items showed moderate increases throughout the year with the exception of maize and cassava meal, which increased by more than 20 percent and 34 percent, respectively. This was attributed to the decreased supply of maize grain on the market during this time of the year. Non-food item inflation accelerated slightly compared to the previous quarter. At the end of December non-food inflation reached 8.2 percent compared to 7.4 percent in September. Throughout the year the price of firewood for cooking increased by almost 90 percent, adding to the costs of poorer households while cement increased by more than 17 percent.

The Central Bank maintained the policy rate at 9.75 percent for the fourth quarter. It stated that the relatively tight monetary policy was adequate to mitigate against any upward pressure from food price inflation, as well as exchange rate depreciation pass-through. The policy rate remained unchanged for six consecutive months.







ZAMBIA

The cost of finance and foreign exchange rates was affected by the Fitch downgrade of the sovereign credit rating from B+ to B – five levels below investment grade – in October. S&P followed suit, downgrading their outlook from stable to negative, increasing the risk of a full downgrade in the medium term.

The Zambian kwacha (ZK) slightly accelerated depreciation against the USD and the pound, following the credit rating downgrade, but otherwise depreciated moderately throughout the year. The total ZK depreciation against the USD reached 6.3 percent for the full year while the pound depreciated by 7.3 percent. The ZK to ZAR remained stable in the fourth quarter, though appreciating by 11 percent over the past 12 months.

Broad Money (M2) growth remained largely stable in 2013. In November, however, broad money growth fell below the year average to 18.0 percent (year-on-year) compared to 18.3 percent (year-on-year) for November 2012.

The cost of Treasury bills and bonds increased in the fourth quarter, following the downgrade. The 1-year T-bill rate increased to 15.7 percent in December compared to 13.6 percent in September. The 10-year T-bond increased by 85 basis points, amounting to 18.2 percent. The 2022 EuroBond, issued at 5.6 percent, was trading at above 7.0 percent towards the end of the year.

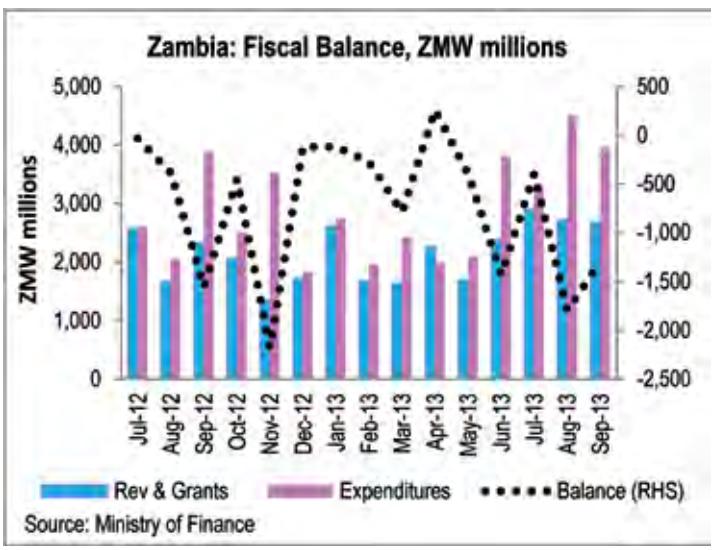
Average bank lending rates continued to stabilize around the year average of 16.3 percent. Lending rates are down from the average lending rates of 19 percent in 2012 with rates exceeding 23 percent in the first quarter of 2012. Current account deposit rates increased slightly in the fourth quarter to 1.3 percent in December, compared to 1.1 percent in September. Fourth quarter rates were still below the rates of the first quarter of 2013 at 3.8 percent.

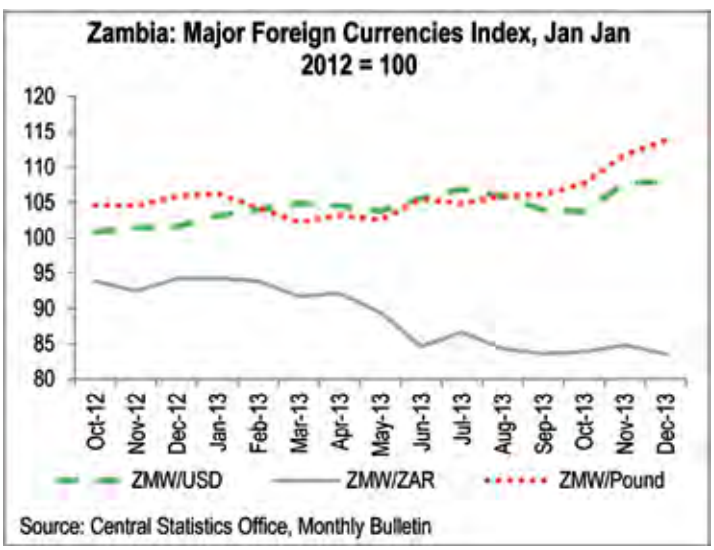
Loans and advances by commercial banks rose strongly throughout the year. By November loans and advances had grown by 16 percent on a year-on-year basis, totaling ZK 19.4 billion. The private sector holds 89 percent of these loans with the remaining held by parastatals, statutory bodies, non-residents and other financial institutions. In terms of sector distribution agriculture and forestry took up almost 20 percent of loans and advances.

Fiscal Policy: The Ministry of Finance continues to pursue an expansionary fiscal policy prioritizing expenditure on infrastructure, fuel, farmer input subsidies and the strategic food reserve. The first 10 months of 2013 saw expenditure amount to ZK 26.1 billion compared to ZK 20.2 billion during the same period the previous year, corresponding to 29 percent. Revenues including grants collected during the first 10 months amounted to ZK 20.2 billion compared to ZK 19.1 billion in 2012, corresponding to almost a six percent increase. By year-end total expenditure is expected to reach ZK 34.6 billion or ZK 2.4 billion more than the initial budget. The fiscal deficit is projected to reach 8.5 percent of GDP by the end of the year, which is almost double the planned deficit.

The Ministry of Finance released the 2014 State Budget in October, increasing the total spending framework to ZK 42.7 billion. Revenues and grants are projected to reach ZK 32.3 billion with the deficit – 6.6 percent of GDP – expected to be financed through internal and external sources, including a new sovereign bond issue. The expenditure framework has increased by 32 percent in order to accommodate higher spending on personal emoluments and increased capital spending, including the Government's flagship road project, Link 8000. The main spending item is personal emoluments amounting to 52 percent of total expenditure. Government has proposed to increase the taxable monthly salary threshold from ZMW2200 to 3000, which implies a reduction of ZK 1 billion in potential income tax. In addition, a wage moratorium is proposed for the next two years and deferment of any new recruitment to 2015. In order to increase revenue the Government is proposing changes to various excise taxes, withholding taxes, and rationalizing tax incentives, while also increasing collection efforts.

At the end of 2012, total public guaranteed debt (external and internal) was estimated at about 30.8 percent of GDP. In 2013 debt increased to 34.1 percent of GDP, with external debt amounting to 16.5 percent of GDP.





External Sector: The trade balance in the fourth quarter continued to deteriorate from the previous quarter with the first trade deficit recorded in 3 years in November. Estimates for the full quarter are not yet available.

The trade balance in October reached ZK 43 million and continued a downward slide in November, reaching a deficit of ZK 327 million. During the same months in 2012 the trade balance recorded a surplus of 291 million and ZK 113 million, respectively. The deterioration is mainly attributed to a fall in the exports of copper-derived intermediate goods, which recorded a decrease of more than ZK 500 million in November.

Total exports recorded in October and November amounted to ZK 9.7 billion, corresponding to a 2.1 percent increase compared to the same period in 2012. For the first 11 months of 2013 total exports increased by more than 17 percent compared to the same period the year before. In October and November imports amounted to ZK 9.9 billion, corresponding to a 10.1 percent increase compared to the same period in 2012. For the first 11 months of 2013 imports increased by more than 21 percent compared to the same period the year before. Non-traditional exports have performed strongly since 2005, growing at an average annual rate of 26 percent. Since May 2013, however, non-traditional exports have been declining on a monthly basis. The total 2013 non-traditional exports are still expected to surpass the level in 2012. In November, Switzerland and China were the main export destinations, accounting for 65.1 percent of exports. The two main sources of Zambia's imports were South Africa and the Democratic Republic of the Congo, accounting for 46.6 percent of imports in November.

Gross international reserves decreased due to stabilization of the ZK and once-off payments for accrued fuel bills, reducing reserves by close to USD 600 million during the first 4 months of the year. Foreign reserve accumulation has since improved with the current level amounting to USD 2.7 billion, corresponding to 2.8 months of imports (Government target is 3 months). According to the Ministry of Finance, FDI increased to just under USD 2.0 billion in 2013, up from USD 1.6 billion in 2012.

II. INSTITUTIONAL AND STRUCTURAL REFORMS

According to the 2014 Doing Business Report by the World Bank, Zambia's overall business environment improved in 2013. Zambia moved up 7 places in the ranking to 83rd position, globally, and is the 7th highest in Africa. This was mainly attributed to improvements in starting a business, resolving insolvency issues and obtaining credit. Within the Southern African region only Botswana and South Africa are doing better than Zambia.

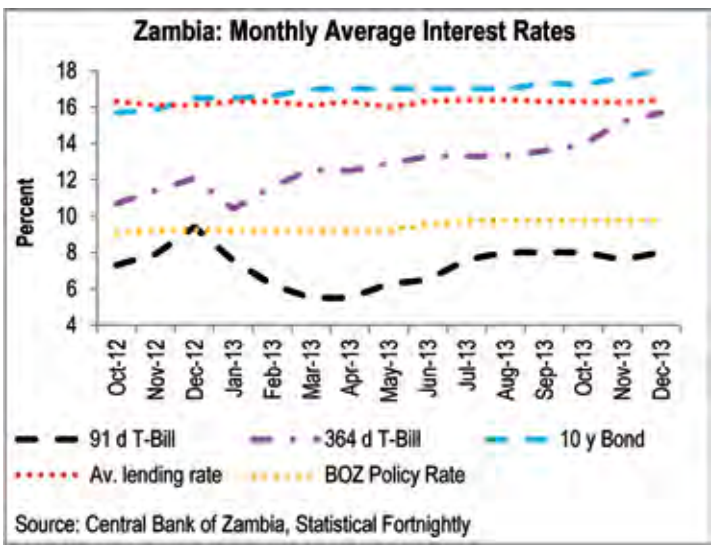
Zambia's national road-tolling program started on 1 November, focusing on heavier vehicles that will be required to pay road toll at 17 ports of entry. The second phase of the program, which will target light vehicles, will only be able to start once toll gates have been constructed around the main trunk road system on the Great North and the Great East Roads.

III. DONOR COORDINATION ACTIVITIES

As reported in the third quarter, the first 2013 Poverty Reduction Budget Support review meeting was held in July to assess the Government's progress for the 2012 Performance Assessment Framework. The main issues raised were the concerns about sound macroeconomic management and the growing risks of substantially increasing public expenditure. As the review was only concluded in November, it has been agreed that the second review meeting will be postponed to February 2014.

IV. ISSUES NEEDING PARTICULAR ATTENTION

The 2013 end-of-year budget deficit reached 8.5 percent of GDP, exceeding the planned deficit of 4.3 percent of GDP. There will be a need for Government to strengthen budget control to avoid similar overruns in 2014. The 2014 budget deficit is targeted at 6.6 percent of GDP. In the past years the costs for the Farmer Input Support Program and the purchase of strategic maize reserve has overrun the budget. It will be important to monitor spending on these items in the coming year.



ZIMBABWE

HIGHLIGHTS

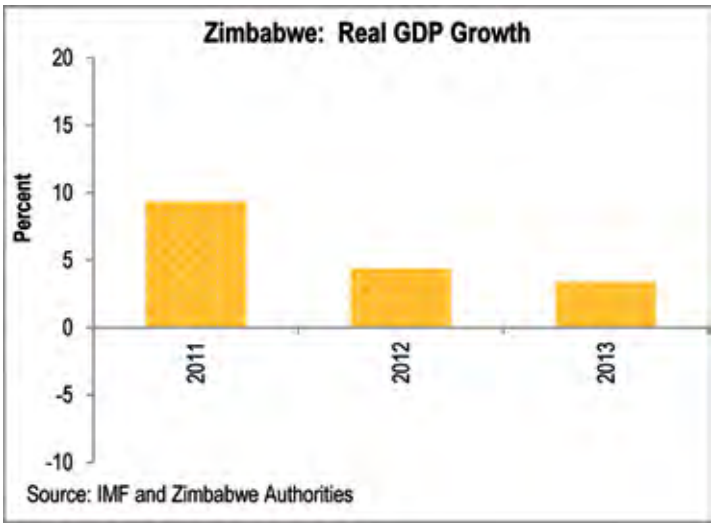
- Economic data for the fourth quarter indicate an economy that is slowing down further. GDP growth is projected to register 3.4 percent in 2013 against the initial projection of 5.0 percent, following poor performance in agriculture and weakening global commodity prices.
- The balance of payments position continued to deteriorate. The economy is struggling to generate exports at a time when economic agents are importing heavily.
- The fiscus remains severely constrained due to the poor performance of domestic revenue inflow against the background of rising recurrent expenditure and huge debts.
- The annual rate of inflation continued to decline, from 2.51 percent registered in January 2013 to 0.33 percent in December 2013 amidst fears of deflation as the rate approaches zero.

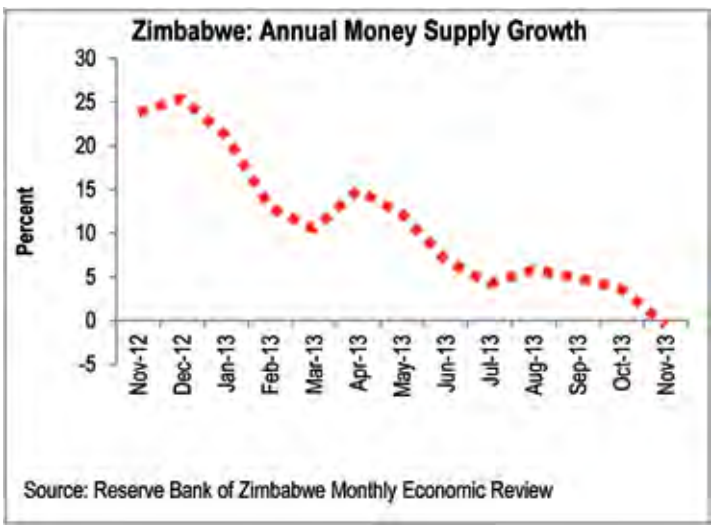
I. MACROECONOMIC MANAGEMENT OVERVIEW

Economic Growth: Real GDP growth for 2013 is projected at 3.4 percent, compared to 4.4 percent registered in 2012, largely due to underperformance in agriculture and mining sectors. Furthermore, the economy continues to suffer from a number of challenges including: low capital inflows, a liquidity crunch, external debt overhang, declining industrial capacity utilization and the high cost of utilities.

Monetary Policy and Banking System: Annual growth in broad money supply (M3), defined as total banking sector deposits (net of interbank deposits), declined from 23.8 percent in November 2012 to -0.5 percent in November 2013. On a month-on-month basis, M3 increased from -1.5 percent in August 2013 to 3.0 percent in September 2013 and retreated to 1 percent in October before further declining to -3.7 percent in November 2013. Annual total banking sector deposits slightly decreased to USD 3.81 billion in November 2013, from USD 3.82 billion registered in November 2012. On a month-on-month basis, total banking sector deposits decreased from USD 3.95 billion in October 2013 to USD 3.81 billion in November 2013. The decline could be attributed to panic depositor withdrawals over concerns regarding the soundness of the banking system, the biting liquidity crunch and general declining economic activity. The closure of Trust Bank by the Reserve Bank of Zimbabwe (RBZ) and the introduction of cash withdrawal limits by some small banks in December continue to blight confidence in the banking sector. Confidence in the financial system, as well as the attractiveness of financial instruments needs to be nurtured and given a boost in order to ensure and harness further growth in deposits, especially long-term deposits, which were at a low of 16.20 percent as at November 2013.

The loan-to-deposit ratio, calculated on the basis of total bank deposits as well as external and domestic sources of funding, increased from 91.2 percent in November 2012 to 97.2 percent in November 2013, increasing marginally, on a month-on-month basis, from the 94.1 percent registered in October 2013. However, banks need to continue exercising caution in lending, given the high level of non-performing loans, which stood at 15.64 percent as at 30 September 2013, well above the regional best practices levels, which are below 3 percent. The deteriorating asset quality is reflective of corporate viability challenges.





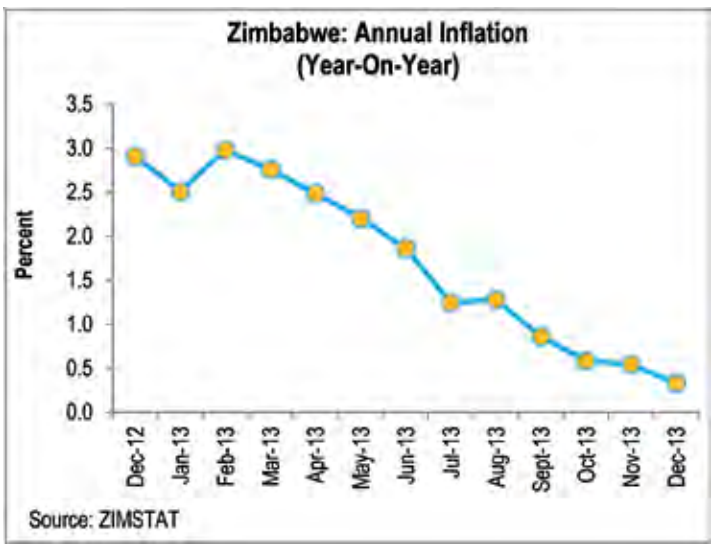
Zimbabwe's year-on-year consumer inflation continued to decline from 1.28 recorded in August 2013 to an all-time low in 45 months of 0.33 percent in December 2013. The top factors driving annual inflation downwards remained unchanged from November 2013 with the prices of communication (-13.99 percent); food and non-alcoholic beverages (-2.20 percent); furniture and equipment (-1.08 percent) and recreation and culture (-1.03 percent). The decline in annual inflation was mainly driven by a weak ZAR/USD exchange rate and depressed aggregate demands on the local economy.

On a month-on-month basis, inflation dropped -0.1 percent against 0.1 percent increase in November, shedding 0.2 percentage points. Food and non-alcoholic beverages inflation increased to -0.41 percent from -0.60 percent in November while non-food items inflation declined to 0.08 from 0.43 percent in November 2013. The decline in monthly inflation was attributed to the decline in the prices of furnishings, home equipment and routine maintenance (-0.93 percent); miscellaneous goods and services (-0.46 percent); food and non-alcoholic beverages (-0.41 percent) and furniture and equipment (-0.29 percent). Year-on-year inflation has remained well below 5 percent following the adoption of the multicurrency system. In the short to medium term, inflation will continue to be dependent on movements in international oil prices, the USD/rand exchange rate, world food prices, as well as the level of aggregate demand.

Commercial bank-weighted average lending rates for individual firmed from 13.95 percent in October 2013 to 14.18 percent in November 2013, while commercial bank-weighted lending rates for corporates also increased from 9.25 percent to 9.40 percent over the same period. Meanwhile, merchant bank-weighted average lending rates for both individuals and corporates firmed from 18.67 and 17.66 percent in October 2013, to 18.84 and 17.72 percent in November 2013, respectively. Lending rates have remained high due to the liquidity challenges compounded by limited access to offshore financing and the weak balance-of-payments position. Hence productive borrowing is being inhibited.

The range in commercial bank savings deposit rates for November 2013 has remained at the November 2012 range of 0.15-8 percent, and the three-month deposit rate range has remained at the July 2013 range of 3 to 20 percent. The wide range in the deposit and savings rates reflects the varying capacities among banks in rewarding depositors and savers.

Fiscal Policy: Fiscal space remains severely constrained due to the poor performance of domestic revenue inflows against the background of high recurrent expenditure, with employment costs accounting for about 75 percent of total expenditure. The Treasury only received USD 17 million of diamond dividends in 2013. Total revenue declined continuously from USD 353.43 million collected in September 2013 to USD 259.10 million in November 2013. This was 26.33 percent lower than the target of USD 351.7 million, making November the third consecutive month in which actual revenues missed the targets. Against the background of missed targets, the cumulative revenue outturn to November 2013 of USD 3.360 billion was 1.04 percent lower than the cumulative target of USD 3.395 billion. The lower revenue outturn was attributed to lower corporate tax performance, on the back of low industrial capacity utilization and delays by some companies in submitting corporate tax returns. The Zimbabwe Revenue Authority (ZIMRA) was quoted reporting that cumulative revenue collections for 2013 amounted to USD 3.43 billion, lower than the 2014 National Budget revised estimate of USD 3.72 billion. Cumulative expenditure to November amounted to USD 3.534 billion, of which 89.87 percent (USD 3.176 billion) were recurrent, while the remainder were capital projects, thus curtailing development and growth-enhancing investments. On the back of underperforming revenues, the Government's overall balance worsened from a deficit of USD 127.71 million as at end-October to USD 173.67 million by end-November 2013. This is a major concern if the country's fiscal commitments are to be met under the Staff Monitored Program (SMP), particularly, the need to align expenditures to available fiscal revenues, balancing support to social sectors and gradually rebuilding international reserves from the current low of 0.2 months of import cover.



External Sector: If one reflects on Zimbabwe's continued demand for imports and overreliance on export commodities, the country's balance of payments remains in a precarious position. A widening trade deficit does not augur well for an economy that is desperate for an improvement in the liquidity position and the building of reserves. During the period January to November 2013, total exports amounted to USD 3.3 billion. Total exports for the eleven months to November fell by 8.76 percent in 2013, compared to the same period in 2012. This shows that the estimated target of USD 4.43 billion for 2013 is not likely to be attained, as exports for December 2013 should be over a billion USD, at a time when exports for the eleven months averaged only USD 296 million. The 2014 National Budget Statement revealed that total imports for the year 2013 are expected to reach USD 7.682 billion. However, total imports for the eleven months to November 2013 amounted to USD 7.1 billion, increasing by about 4.9 percent compared to the same period in 2012. The trade deficit has continued to grow in 2013 to about USD 3.8 billion for the eleven months to November. This is an increase of about 19.9 percent compared to the same period in 2012. In 2014, exports are projected to reach USD 5 billion while imports are pegged at USD 8.3 billion, leaving a large trade deficit that will be difficult to fill and thus exacerbating the country's balance of payment position. The Government has anchored the envisaged growth in exports during 2014 on access to low costs for intermediate input while the reduction of input tariffs, an extension of the preferred economic operator

status and the implementation of the duty drawback system are expected to revitalize growth in exports.

II. INSTITUTIONAL AND STRUCTURAL REFORMS

The following are some of the key reforms announced in the 2014 Budget and developments during the period under review:

- Following the inauguration of the new ZANU (PF) Government, Zimbabwe made a new policy document available – the Zimbabwe Agenda for Sustainable Socio-Economic Transformation (Zim-ASSET) covering the period from October 2013 to December 2018. Zim-ASSET is premised on a cluster approach to economic development, focusing on the following four clusters: (i) Food Security and Nutrition; (ii) Social Services and Poverty Eradication; (iii) Infrastructure and Utilities; and (iv) Value Addition and Beneficiation.
- The Zimbabwean authorities requested a six-month extension of the IMF's Staff Monitored Program (SMP), originally scheduled for April to December 2013, to allow time for the national authorities to strengthen their policies and deliver on outstanding commitments under the program. The first review of the program is set for March 2014.
- During the 2014 National Budget presentation, the Minister of Finance and Economic Development reconfirmed the taking over of USD 1.35 billion RBZ debt by the Government through the issuance of five-year TBs at 5 percent.
- On the direction of the President, the Ministries of Mines and Finance will introduce measures to increase transparency, including directing the Mineral Marketing Corporation (MMCZ) to deduct revenues due to Treasury and pay them directly to Treasury, strengthening the capacity of diamonds valuators, establishing diamond inspectorate teams, and expanding the role of ZIMRA. The budget statement proposed a diamond- sharing formula where the Government receives 12.5 percent of gross proceeds of diamond sales.

III. DONOR COORDINATION

The Zimbabwe Field Office continued to participate in a number of donor coordination activities during the period under review, in particular, the Field Office participated in thematic sessions including: the monthly meeting between the World Bank and the AfDB to discuss current activities undertaken by the two institutions in policy advisory, knowledge work and technical assistance; the public financial management (PFM) meeting between the donors and the Accountant General's Department, Fishmongers Group (Representatives of some bilateral donors), etc. The Management Unit of the Zimbabwe Multi Donor Trust Fund (ZimFund) held Program Oversight Committee meetings between the Government, the bank and ZimFund donors, as well as a number of technical meetings with stakeholders on the ZimFund projects. During the quarter, ZWFO also consulted relevant development partners on the design of Governance and Institutional Strengthening Project, the Youth and Tourism Enhancement Project and the Transport Sector Master Plan Study, which were initiated in early September/October 2013 and approved in December 2013.

The Bank hosted a number of partner consultation meetings during the quarter including with: a delegation from the Global Fund to Fight HIV/AIDS, TB and Malaria whose objective was to explore the possibility for ZWFO managing the Global Funds resource for Zimbabwe from 2014 to 2016 and the African Water Facility Conference held in Harare in November 2013. In addition, from 2 to 6 December 2013, the African Community of Practice on Managing for Development Results (AfCoP-MfDR) organized two back-to-back workshops in Harare and the Africa for Results Forum and the Sixth AfCoP Annual Meeting. These two events are organized with the support of the African Development Bank and the African Capacity-Building Foundation (ACBF).

IV. ISSUES NEEDING PARTICULAR ATTENTION

Going forward, in the short term, the following issues need particular attention: the situation in the banking sector, the food security situation, the first crop assessment, weather conditions, the implementation of the agreed civil service wage pact; the IMF SMP Review, Article IV Consultation and Debt Sustainability Analysis in March 2014; and a review of restrictive measures by the EU around February 2014. In the medium term, the implementation of indigenization and economic empowerment regulations need to be monitored.

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