SWAZILAND
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- **In spite of an expansionary fiscal stance, economic growth is expected to decelerate to just over 2% in 2014 as private sector investments remain low.**
- **Uncertainty in Southern Africa Customs Union (SACU) revenue receipts beyond 2015 calls for accelerated fiscal reforms that would lock-in the benefits from the current high inflows.**
- **An unfavourable business environment constrains the extent to which the economy could benefit from existing links into global value chains.**

Overview

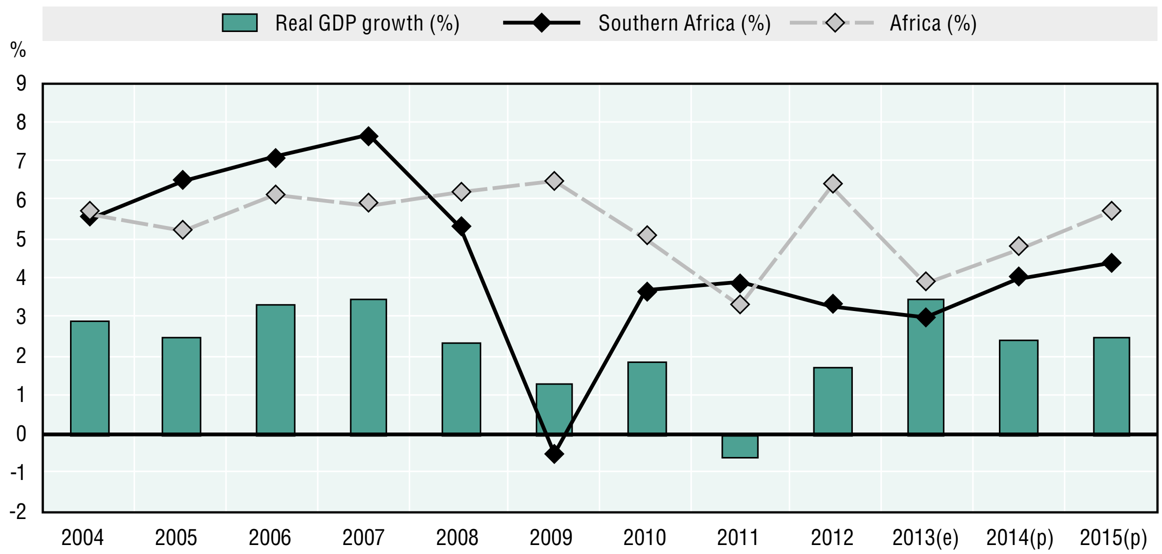
Economic growth in Swaziland is expected to weaken to just over 2% in 2014, down from the estimated 3.5% in 2013. This deceleration is largely the result of existing structural constraints, despite the large inflows from the Southern Africa Customs Union (SACU) revenue pool. The spending of SACU income means that no fiscal space has been created to enhance the government's ability to respond to potentially reduced SACU receipts in the future. The main growth drivers in 2013 were the recovery in domestic and external demand buoyed by public expenditure and stronger global demand for exports.

Price pressures have gradually been easing out, with headline inflation declining from a peak of 9.6% in May 2012 to 4.4% in December 2013. Reflecting the positive macroeconomic environment and growth of the economy, annualised private sector credit grew by 6.5% as of end-November 2013. The healthier fiscal position has also allowed gross foreign reserves to increase from an equivalent of 3.2 months of import cover at the beginning of the year to 4.8 months in November 2013.

The business environment is slowly improving but a significant number of reforms are still needed to make it conducive. Swaziland's ranking in the 2014 *Doing Business* Index by the World Bank was 123 out of 189 countries. Over the same period, the World Economic Forum's *Global Competitiveness Report 2013-14* ranked Swaziland at 124 out of 148 countries. Swaziland's governance indicators compare unfavourably with its neighbours. In 2013 the Ibrahim Index of African Governance ranked Swaziland 26th out of 52 countries with a score of 50.8, thus registering a slight rise over the 2012 ranking of 27th. The 2013 Index ranks Swaziland poorly in participation and human rights, as well as sustainable economic opportunity attributable to weak institutional capacity and a relatively rigid political system.

Swaziland's share in global trade has fallen over the years – its share in world merchandise exports peaked at around 0.02% of world trade in 2004, but fell sharply to 0.01% in 2010. The country's contribution in global value chains, although small in absolute terms, is quite significant for the domestic economy.

Figure 1. **Real GDP growth**



Source: AfDB, Statistics Department AEO. Estimates (e); projections (p).

Table 1. **Macroeconomic indicators**

	2012	2013(e)	2014(p)	2015(p)
Real GDP growth	1.7	3.5	2.4	2.5
Real GDP per capita growth	0.2	2.0	1.0	1.1
CPI inflation	8.9	5.7	5.9	5.6
Budget balance % GDP	-4.4	5.6	5.3	8.2
Current account balance % GDP	3.3	5.6	-0.9	-7.8

Source: Data from domestic authorities; estimates (e) and projections (p) based on authors' calculations.

Recent developments and prospects

Growth in 2013 was estimated at 3.5%, which represented acceleration in growth over the 1.7% recorded in 2012. The tertiary sector decline of 1.2% in 2011 was reversed to a positive growth of 2.5% in 2012. The transport, storage and communications sector experienced the largest growth at 19.3% in 2012 compared to 2.7% the previous year. Growth in the primary and secondary sectors was subdued due mainly to a combination of a poor agricultural season, especially the maize and citrus sub-sectors, and a slow recovery in South Africa and the European Union. These two markets account for about 70% of the country's exports.

Higher receipts from the SACU in 2012/13 helped reduce domestic payments arrears to the private sector, especially the construction sector where suspended activities were revived. Growth in 2013 therefore improved, largely driven by a recovery in manufacturing and service sectors. Construction benefited from public sector investments, especially given the 25% increase in the capital budget. By the third quarter of 2013, building plans approvals had jumped by more than 7% compared with that of 2012. As the construction sector recovered, the demand for quarried stone increased. This, together with the higher coal output, led to positive growth in the mining and quarrying sector. Weaknesses in the global economy, however, continue to pose some risks to Swaziland's growth prospects. Growth in the South African economy, in particular, has slowed down.

The demand side of the Swazi economy is likely to benefit from a number of factors, including among others: *i*) tax policy changes implemented in the 2013/14 budget have boosted disposable incomes, following upward adjustments in non-taxable income thresholds and increases in civil servants' salaries; *ii*) although not fully recovered yet, the external sector has been boosted by increasing export demand; and *iii*) the expansionary fiscal policy, as reflected in the increase in capital expenditures and the reduction in personal and corporate tax burdens. Strengthening domestic demand has also been observed in higher usage of utilities where both water and electricity demand have increased by about 1.5% and 4.8% in real terms in 2013.

Poor performance of the agriculture, manufacturing and utilities sectors in 2012, which resulted in lower than potential growth was reversed, with all sectors estimated to have registered growth in 2013. 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 sub-sectors registered positive growth above 2%. Similarly, electricity, gas and water supply recovered from a contraction of 20.9% in 2012 to positive growth in 2013 on account of favourable rains in the 2012/13 summer season. On the other hand, higher public capital expenditure supported continued recovery in the construction sector. The services sector, especially communications, could have seen higher growth had the expected reforms in the sector been implemented to boost demand and investment. The secondary sector, which comprises construction, manufacturing and power generation, gas and water supply sectors, is estimated to have reversed a 0.3% decline in 2012 to a more than 6% growth in 2013.

Improved growth in 2013 is unlikely to be sustained for the outlook period. Limited economic dynamism, due mainly to lack of new investments in the productive sectors, is likely to impact on growth in the near term. Private sector investment has been largely subdued despite recovering confidence in the economy. More importantly, existing downstream and upstream linkages in mature industries such as textiles, sugar and concentrates require further diversification of the product ranges to create new investment opportunities with significant growth spillovers to the rest of the economy. In addition, the share of government in gross domestic product (GDP) remains high, with the recovery in SACU revenue receipts having been critical in supporting recent growth. It is therefore expected that economic growth would slow down in 2014 and 2015 to levels of just over 2%, unless a significant increase in private sector investment is realised. The sugar sector's dominance will also continue, with more than 6 000 hectares of additional crop area planned until 2016.

Table 2. **GDP by sector (percentage)**

	2008	2012
Agriculture, hunting, forestry, fishing	7.9	7.2
of which fishing		
Mining	0.3	0.3
of which oil		
Manufacturing	42.2	42.2
Electricity, gas and water	0.9	1.2
Construction	3.0	2.2
Wholesale and retail trade, hotels and restaurants	10.9	9.6
of which hotels and restaurants	2.1	1.8
Transport, storage and communication	7.4	7.2
Finance, real estate and business services	7.6	7.6
Public administration, education, health and social work, community, social and personal services	15.6	17.9
Other services	4.2	4.6
Gross domestic product at basic prices / factor cost	**100.0**	**100.0**

Source: Data from domestic authorities.

Risks to growth remain. Of particular concern is the uncertainty of trends in SACU revenue receipts. There are ongoing negotiations on a revised revenue sharing formula, which might reduce Swaziland's share of SACU revenue receipts. In addition, the levels of tariff rates in the region and those for South Africa's main trading partners are declining in line with global trends. These two factors, coupled with weaker growth in South Africa and the slow progress in improving the business environment is hampering domestic and foreign investment inflows, posing significant downside risks to growth. Lastly, although the agriculture sector's contribution to Swaziland's GDP is less than 10%, it is vertically linked with the manufacturing sector that is dominated by sugar production. Given this linkage, adverse weather conditions have significant impact on growth. On a positive note, the recently appointed cabinet has openly declared that key reforms that would encourage investment will be pursued with vigour. This position is supportive of the development partners' ongoing work in strengthening the capacity of government to deliver on its development objectives.

Macroeconomic policy

Fiscal policy

There is a general recognition by the government on the need to enhance and sustain economic growth, as expressed in the 2013/14 national budget theme that centred on "jump-starting economic growth". The recently appointed cabinet has also adopted the concept of "development unusual", which reflects the government's commitment to addressing poverty and inequality. Given the improved fiscal situation, the government has signalled its intention to address some of the social challenges, including creating jobs, and spending more on human capital development. Accordingly, the government allocated almost 20% of its budget to education and training and about 12% to health. The challenge, however, is on sustaining such expenditures in future without negatively impacting fiscal sustainability, especially given the low allocations to the productive sectors. Agriculture, which is the mainstay of almost 70% of the population, was allocated only 4.2% of the total budget, well below the 10% agreed under the Comprehensive Africa Agriculture Development Program (CAAPD). Similarly, the capital budget allocation remains below 10% despite an increase of about 26% over that of 2012/13. In this context, it is critical that the government focuses more on translating policy intentions into concrete actions to achieve meaningful transformation on the ground.

The government continues to rely on SACU revenue receipts, which account for approximately 55.3% of total revenue and grants. Domestic revenues, including value-added tax (VAT, 14%), individual and corporate taxes (19%) and non-tax revenue (3.7%) amounted to about 43.2% of total revenues. Grants constituted about 1.5% of total revenue. On the expenditure-side, the estimated outturn of Swazi Lilangeni (SZL) 12.67 billion is slightly lower than the SZL 12.98 billion that had been budgeted, due mainly to lower than planned capital expenditures. The combination of lower than planned expenditures and better revenue performance is expected to result in a better fiscal outturn of about 0.7% surplus compared to the projected deficit of almost 1%. Overall, revenues in the current fiscal year increased by 9%, with domestic revenue having increased by 14% compared to the previous year.

Despite better than projected revenue performance, personal income taxes are expected to underperform. On the other hand, the reduction in corporate income taxes from 30% to 27.5% carved out about SZL 300 million of potential revenue. In addition, efficiencies in revenue collections are almost exhausted, which may result in lower revenue growth unless significant tax policy changes take place.

Recurrent spending for 2013/14 is estimated at 84% of total expenditure. General services and public order, safety and defence account for most of this line of spending. The size of the wage bill continues to be high and almost equivalent to the total amount of domestic revenue collections.

This structure of expenditure is unsustainable and poses a serious threat to fiscal viability. Also, implementation of capital projects remains below the 80% target, which has negative implications on the development objectives of the budget. Better budget planning, execution, reporting and control are therefore critical elements that need to be fully addressed under the ongoing public financial management (PFM) reforms.

Table 3. **Public finances (percentage of GDP)**

	2005	2010	2011	2012	2013(e)	2014(p)	2015(p)
Total revenue and grants	**30.6**	**31.8**	**23.1**	**24.1**	**35.4**	**35.9**	**40.9**
Tax revenue	29.2	29.7	21.4	22.7	34.5	34.2	39.3
Grants	0.7	0.6	0.0	0.1	0.0	0.7	0.7
Total expenditure and net lending (a)	**35.8**	**35.2**	**33.4**	**28.4**	**29.7**	**30.6**	**32.8**
Current expenditure	27.9	26.8	26.8	25.1	25.2	25.7	27.0
Excluding interest	26.8	26.1	26.1	24.2	24.1	24.4	25.5
Wages and salaries	12.3	13.1	14.9	14.2	13.4	13.1	13.1
Interest	1.1	0.7	0.7	0.9	1.1	1.3	1.5
Capital expenditure	7.9	8.3	6.6	3.4	4.5	5.0	5.8
Primary balance	**-4.2**	**-2.7**	**-9.6**	**-3.5**	**6.7**	**6.5**	**9.7**
Overall balance	**-5.3**	**-3.4**	**-10.3**	**-4.4**	**5.6**	**5.3**	**8.2**

Note: a. Only major items are reported.
Source: Data from domestic authorities; estimates (e) and projections (p) based on authors' calculations.
Fiscal year April n/March (n+1).

Monetary policy

Swaziland has no independent monetary and exchange rate policies as it is a member of the Common Monetary Area (CMA). Its currency is pegged at par to the South African Rand (ZAR). The Central Bank of Swaziland, however, has supervisory and regulatory authority over the financial sector. Monetary policy has largely been accommodative and tracks that of the South African Reserve Bank. The discount rate has been maintained at 5% since July 2012 and the prime lending rates are at 8.5%. The financial sector is well regulated and risks from the non-bank financial sector were addressed following the establishment of the Financial Services Regulatory Authority (FSRA). 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% during early 2012 to about 6% by end-2013.

The principal mandate of the Central Bank of Swaziland, within the Common Monetary Area (CMA), is to formulate and implement monetary policy to achieve price and financial stability and to promote economic growth. Inflation closely follows trends in South Africa although exogenous factors such as erratic weather conditions and the depreciation of the South African rand influence inflation dynamics. Price pressures are gradually easing out, with headline inflation declining from a peak of 9.6% in May 2012 to 4.4% in December 2013, driven mainly by decreases in the price of food and non-alcoholic beverages, which constitute about 29% of the Consumer Price Index (CPI) basket.

Reflecting the positive macroeconomic environment and growth of the economy, key monetary aggregates recorded positive growth in 2013. Annualised private sector credit grew by 6.5% as of end-November 2013, while public sector credit contracted. On a month-on-month basis, private sector credit increased by 21.6% in November, the largest recorded for the year. The healthier fiscal position allowed gross foreign reserves to increase from SZL 6.9 billion in January to SZL 8.2 billion in November 2013; equivalent to 4.8 months of import cover. The large inflow of SACU receipts account 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% in February 2013, broad money supply (M2) growth slowed to 11.5% in June, before picking up to about 18% in July. On average, broad money supply grew by 16.1% on a month-on-month basis. The depreciation of the SZL/ZAR exchange rate against major currencies also influenced the growth in money supply, given the rising foreign reserves.

Economic co-operation, regional integration and trade

Swaziland's membership of various regional and international trade arrangements is important to promoting trade, a critical element of its development and the health of the economy, given its small size. In the Common Market for Southern and Eastern Africa (COMESA), Swaziland has benefited from preferences accorded to it without having to reciprocate as it trades under derogation. South Africa, in particular, remains the largest single market for the country, and Swaziland benefits from the duty-free and quota-free trade arrangements under the SACU, as well as free movement of capital under the CMA. Deepening integration to include free movement of persons, however, is still to be agreed. Yet, Swaziland's multiple memberships to the different trading blocs, with no unified rules and regulations, strain the country's limited administrative capacity.

Swaziland has made some progress in implementing regional commitments. It has, together with other CMA countries, fulfilled the conditions for participation in the cross-border electronic payments system that began in July 2013. As part of the SACU, Swaziland meets most of the convergence criteria for the Southern African Development Community (SADC). Swaziland is also one of the most open countries in the world, with a trade to GDP ratio of about 120%. Despite the importance of trade to Swaziland's economy, the country is lowly ranked under the trade barriers (84), trade tariffs (78) and burden of customs procedures (137) categories in the *Global Competitiveness Report 2013*. The country's tariff structure has not changed in recent years despite efforts to improve trade facilitation. The external tariff for non-SACU imports is at an average rate of 11% across 157 tariff bands. About 21 tariff lines are at more than 15% duty, reflecting the existence of tariff peaks. The burden of customs procedures could be reduced if customs systems could be aligned to those of South Africa and thus facilitate quicker movement of goods between the two countries. Further efforts aimed at reducing the number of documents and declaration points for imports and exports will also help in reducing the costs and time that traders face.

Table 4. **Current account (percentage of GDP)**

	2005	2010	2011	2012	2013(e)	2014(p)	2015(p)
Trade balance	-10.0	-3.8	-0.8	2.0	2.8	-3.7	-10.7
Exports of goods (f.o.b.)	63.4	46.4	46.0	47.7	52.8	57.9	57.3
Imports of goods (f.o.b.)	73.4	50.2	46.8	45.7	50.0	61.6	68.0
Services	-4.7	-11.1	-14.4	-15.3	-9.5	-7.6	-6.5
Factor income	6.9	-5.8	-6.2	-7.5	-6.8	-6.9	-6.9
Current transfers	3.8	10.4	12.8	24.1	19.2	17.4	16.3
Current account balance	**-4.0**	**-10.3**	**-8.6**	**3.3**	**5.6**	**-0.9**	**-7.8**

Source: Data from the Central Bank and domestic authorities; estimates (e) and projections (p) based on authors' calculations.

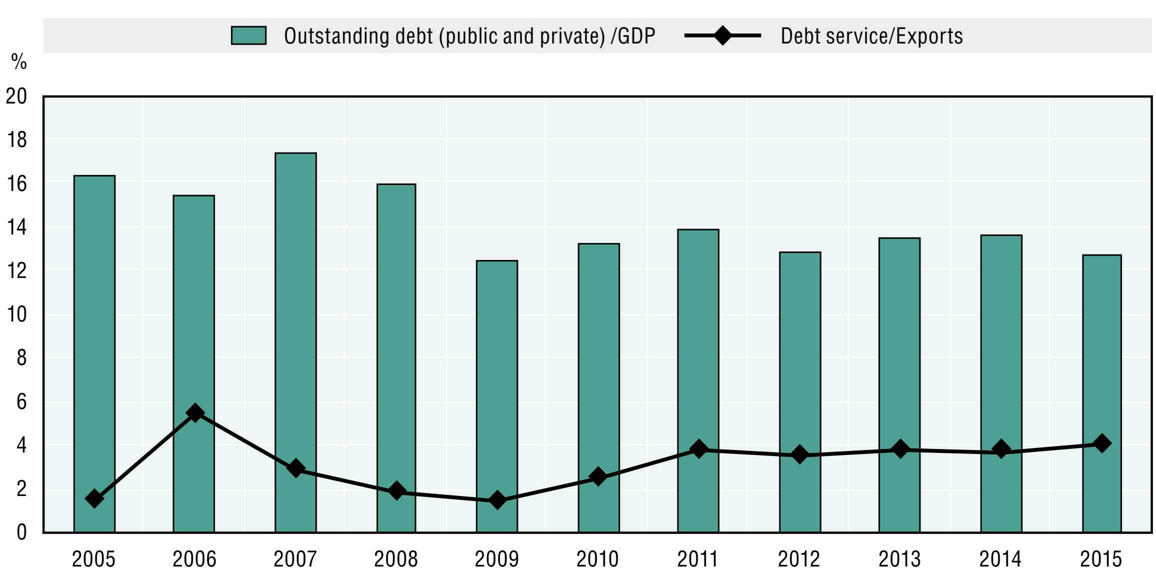
As of September 2013, Swaziland's balance of payments (BOP) recorded a surplus of SZL 82.3 million, although significantly lower than the SZL 629.4 million surplus at mid-year. The lower balance of payments (BOP) surplus was due mainly to capital account transfers. Projections point to a surplus by the end of the year, making it the third consecutive year of surpluses. The BOP outcome is largely a reflection of the fiscal position, which has improved due to higher inflows from the SACU revenue pool. There are concerns related to recent developments on the net income account where the historical surpluses turned into deficits in 2012. This could be a signal of declining job opportunities in South Africa coupled with low foreign investments. In the third quarter of 2013, exports rose by 37% while imports increased by 25%. Surplus on the trade balance shrunk due to declining competitiveness of Swaziland's exports. However, the current account complemented with increases in current transfers continues to be in surplus.

Debt policy

Public debt contracting is currently guided by the Finance Management and Audit Act (1967) and its 1992 amendments. This legal instrument is expected to be replaced by the Public Finance Management Bill of 2013 that was approved by the cabinet in 2013, but has not yet been implemented. The current debt policy sets no explicit limit on external debt. Government has however set the total debt threshold at 40% of GDP and domestic debt at 25%. Actual limits on debt, whether domestic or external, are determined within the budget and reflected in the Finance Act that authorises annual government financing and expenditures. Parliament also has to approve all proposals to contract debt on a case-by-case basis, while the Ministry of Finance initiates the borrowing process. All debt proposals have to demonstrate that the debt to be contracted is in line with the national development objectives and that such debt will not lead to debt unsustainability. In principle, Swaziland has a debt management unit, but it is not functional yet. The operationalisation of the debt unit is part of the plan under the PFM Action Plan being implemented by government.

The absence of an institutionalised framework to manage SACU receipts, upon which 55% of government revenue depends, increases the medium-term fiscal and debt risks for the country. Intermittent cash flow challenges in the first quarter of the 2013/14 fiscal year resulted in the accumulation of domestic arrears. While those challenges were finally addressed, it is clear that debt played an important role in the process. As a result, the projected decline in debt during 2013/14 has not been realised. Instead, debt rose from about 15% at the beginning of the year to 18% by end-2013. External debt has increased from 7.7% to 9.7% of GDP over the same period. Short-term debt as a proportion of total debt rose rapidly from 16% in 2009/10 to 30% in 2012/13. In view of the improved confidence in the economy, the government is gradually moving to restructure its debt tenor towards longer term debt. On 27 August 2013, a 5-year bond was issued at a fixed coupon rate of 8.5%. Swaziland's debt level, although increasing, remains among the lowest in sub-Saharan Africa and efforts should be directed at avoiding debt distress.

Figure 2. **Stock of total external debt (percentage of GDP) and debt service (percentage of exports of goods and services)**



Source: IMF (WEO & Article IV).

Economic and political governance

Private sector

The revision of the Swaziland Investor Roadmap and its re-launch in 2012 created a new impetus to implement reforms to improve competitiveness and improve the business environment. A lot more still needs to be done for Swaziland to improve its ranking in the World Bank report *Doing Business 2014*, which went from 120th in 2013 to 123rd in 2014. The *Global Competitiveness Report 2013/14* ranked Swaziland 124th out of 148 countries, three places down from the previous year. Some improvement was recorded in the macroeconomic environment and financial market development. Starting a business, however, still requires 12 procedures and takes 38 days while enforcing a contract takes 956 days, costs 56% of the value of the claim and requires 40 procedures. It is encouraging that the task force monitoring progress in implementing the Investor Road Map has remained active in ensuring that government commitments are implemented.

On the legislative side, government has continued to put in place supportive legal instruments. The competition commission regulations of 2010, which operationalised the Competition Act of 2007, complement the Fair Trade Act of 2001. The 2013 legislations such as the Communications Commission and Electronic Communications Acts removed existing constraints that provided for monopolies. Acrimonious legal battles over mobile telephone services between Swazi MTN and the Swaziland Posts and Telecommunications Corporation (SPTC) had tainted the government's ability to address competition-related issues. The creation of the communications sector regulator as provided for under the Communications Commission Act and the new framework provided under the Electronic Communications Act are expected to boost investment opportunities in the sector. The independence of the Commission, however, will be critical in ensuring that the implementation of the two legislations will bring the much needed liberalisation of the communications industry. Similarly, other sectors like energy are slowly opening up, with the establishment of independent power producers and a regulatory environment that seeks to enhance the operations of firms in the sector. This notwithstanding, sectors such as water and transport are still heavily regulated.

Acknowledging the constraints that government faces in financing development, further efforts have been made to attract private sector investment. In 2013, the government launched the public-private partnership (PPP) policy, which is the first step towards establishing a framework for partnership between the government and the private sector in developing infrastructure projects. Efforts to secure technical assistance in this regard are ongoing. More efforts, however, are required to improve dialogue between the private sector and government. Functional private sector institutions exist, although dialogue between the two partners needs to be more structured, including a framework of monitoring agreed actions to improve their relationship.

Financial sector

The banking sector remains stable and sound, with the non-bank financial sector now fully under control following the operationalisation of the Financial Services Regulatory Authority. Despite the improved macroeconomic environment and lower risk for bad loans, the financial sector has remained cautious in advancing credit to a broader clientele. The result has been increased concentration of credit, which continues to be dominated by the sugar industry. The World Bank projections show a declining trend in non-performing loans compared to levels in 2011 and 2012. As of November 2013, credit advanced to the household and private sector had increased by about 6.5%, which represents a significant recovery compared to the contraction experienced in 2012.

Of the four banks operating in Swaziland, three are subsidiaries of South African banks. Their credit policies are determined by senior management at head offices, which also approve loan applications. There is a perception that this process ignores or by-passes the knowledge of local loan officers, who may have useful information regarding their clients. As a result the sector has remained shallow and undiversified. Given the limited local market size, other financial institutions, such as pension and insurance firms, channel the locally mobilised resources to the South African market for investment purposes. The Swaziland government has had to implement minimum local investment requirements to encourage investments in the local economy. There are more than 200 savings and credit co-operatives, but the focus of these institutions is on small credit-amounts that are largely of a consumptive nature. Given the short tenure of government paper, mobilising resources for development purposes has therefore been challenging, even in cases when liquidity has been high. In this context, efforts to increase the issuance of long term government paper may assist in ensuring that locally generated resources could benefit the development of the country.

Going forward, financial sector development will remain a critical area in support of small-to-medium enterprises (SMEs). Particularly worrying is the fact that access to credit facilities is limited to only 53% of businesses. Although there was no new study on financial sector developments in 2013, there are no expectations of changes on access to formal banking services so that 37.5% of the population continues to be excluded from any form of financial services. The rural population and the youth are the most affected – with 44% of the rural population and about 78% of 18-19 year-olds having no access to any form of financial services. The existence of a Private Credit Registry, although having improved the availability of information regarding borrowers, appears to have had little impact on access to credit for the majority of the population.

Public sector management, institutions and reform

The application of public resources to realise the development objectives has been challenging. The budgeting system currently makes limited use of the medium-term expenditure framework. Due to poor IT systems, the accounting records are not reliable and in-year budget reports are not produced. Quarterly accounting reports comparing actuals against budget targets are maintained at the individual ministry's level, yet there is no evidence of their consolidation.

Financial management continues to face challenges, although there are efforts to address these through the PFM reforms that are being supported by development partners. It is, however, important that some basic requirements are put in place to ensure the effectiveness of the reforms. For example, ensuring that international accounting standards are used in preparing central government financial statements will assist in modernising government finances. This will also ensure that there is alignment between the various oversight bodies' activities. In particular, the Office of the Auditor General (AG) has made progress in aligning the country's National External Audit Service to best practice, including the decision to adopt the International Standards on Auditing with effect from the 2012/13 audit. On the other hand, public procurement is generally consistent with international standards and applicable to all levels of the public sector, except for State Owned Enterprises.

At the institutional level, the lack of an independent procurement institution compromises the outcome of such an important activity in government business. The NTB carries out both the oversight and implementation responsibilities, which raises questions on conflict of interest. There are, however, efforts to establish the Swaziland Public Procurement Regulatory Agency (SPPRA) to remedy this situation. A Government Tender Board (GTB) is also to be established in accordance with the Procurement Act. The lack of respective institutions has so far compromised the integrity and transparency of government procurement, which to some extent has made it difficult to deal with corrupt practices that continue to haemorrhage the economy.

Overall, Swaziland's governance indicators compare unfavourably with its neighbours. The Ibrahim Index of African Governance ranks Swaziland poorly in participation and human rights, as well as sustainable economic opportunity. In 2013, Swaziland was ranked 26 out of 52 countries, with a score of 50.8, below the regional average score of 59. The country's performance in public management dropped by 8.4 points over the last six years to a score of 53. In addition, The World Bank's Country Policy and Institutional Assessment (CPIA) shows a weakening governance environment, with the country's score declining from 3.5 in 2010 to 3 in 2011. In 2012, the governance score improved to 3.3 but the country's ranking slipped to 47 from 44 in 2011. There are major weaknesses on the expenditure side due to inefficient resource allocations. Strengthening the budgetary process to enhance resource allocation and capacitating oversight bodies to ensure effective delivery of their core mandate and to foster transparency in procurement and accountability will be important.

Natural resource management and environment

Swaziland is facing a number of environmental challenges which require attention. Cultivated plantations and natural woodlands are increasingly being degraded due to uncontrolled fires and extraction of forest products, agricultural development and large livestock populations. Swaziland is also prone to volatile weather conditions. The Climate Emergency Institute reports that, by 2050, Southern Africa's temperatures are expected to rise by 2-4°C and rainfall is expected to decrease by 10-20%compared to 1961-90 baselines. Land degradation and ecosystems are also projected to worsen, negatively impacting productivity and possibilities for gaining a livelihood, especially in Swaziland's low-lying regions.

Swaziland has institutions that focus on climate change and green growth, notably the National Climate Change Committee and Designated National Authority for the Clean Development Mechanism (CDM). The 2010 Technology Needs Assessment, whose aim was to identify and evaluate climate change mitigation and adaptation technologies and measures consistent with Swaziland's national development priorities, established gaps in education, training and public awareness. All greenhouse gas emissions are currently estimated at 25.4 million tons of CO_2 equivalent and are expected to increase to 33.4 million tons by 2030, as the country responds to poverty and food security challenges. Proposed mitigation measures include a fuel switch from coal to sugarcane trash in the sugar industry, strengthening and promoting renewable energy sources, efficient energy systems, and ethanol blending. Implementation of these proposals is supported by the Swaziland Environment Act of 1992 and the Environment Management Act of 2002, which provide the legal framework for managing the environment that requires that all government programmes be subjected to environmental assessment. The United Nations Development Programme (UNDP) is currently assisting in building national capacity on climate change issues.

Political context

The Swaziland Constitution is silent on political parties, and civil society agitation has mostly been manifested in peaceful labour-related protests. The restrictive political governance has limited the presence and participation of development partners, especially bilateral partners. In October 2013, Swaziland held parliamentary elections with a voter turnout of 65%. The election of women in Parliament was disappointing, with only one out of 55 seats being filled by a female candidate. His Majesty the King and the Parliament nominated nine women, thus bringing representation to 15.4%. Female representation at community levels represents a similar pattern, with some regions registering even lower numbers.

Swaziland remains at the low end of the global rankings on governance. Transparency International's Corruption Perception Index ranked the country 170th out of 174 countries in 2013. Access to justice is still limited, especially as a large part of the populace is not sensitised to their constitutional rights. The Attorney General's drafting department has completed the drafting of the National Legal Aid Policy and the Legal Aid Bill, which promotes access to justice especially by marginalised groups. Weak institutional capacity in the Commission on Human Rights and Public Administration/Integrity and the Anti-Corruption Commission still remains a concern. The government, as part of strengthening the Commission on Human Rights and Public Administration, is in the process of setting up the Commission's secretariat, which is envisaged to be operational by March 2014.

Social context and human development

Building human resources

In 2013, lingering effects of the fiscal crisis have had an impact on resource allocations to the social sector. This, together with the weak private sector, unable to maintain existing jobs, reduced households' capacity to provide for some of the basic requirements on health and education. At the same time, the government withdrew blanket university grants leaving prospective students without financial support to take courses of their choice. With Swaziland being one of the countries with the highest literacy rates in Africa, this decision may not have any immediate effect, as the affected courses were identified as not being in demand among employers. However, the affected students had not been warned in advance, and this has disrupted their educational plans. The government's Free Primary Education Program has continued to be supported; it is at this level where the greatest impact on education can be felt as it lays the foundation for higher levels. Timely release of primary education grants, however, has remained a challenge. Reflecting the erosion of government's capacity to fully fund education grants to orphans and vulnerable children, the release of funds for the Free Primary Education Program was delayed to allow for an audit of the fund. Prioritisation of social expenditures, especially those that are meant for the vulnerable is therefore essential.

Overall, Swaziland has made good progress with respect to achieving universal primary education, with net primary enrolment having risen from 72% in 2007 to 93% in 2013. Also, in 2009/10, 73.9% of children reached grade 7 without repeating a grade more than twice, compared to 59.8% in 2006/07. The 2013 *Global Human Development Report* classifies Swaziland as a medium human development country with ranking of 141 out of 187 countries. Swaziland's main health challenges are to reduce the incidence of HIV/AIDS and tuberculosis. Despite financial constraints, Swaziland is continuing to provide life-saving drugs to HIV/AIDS patients with the support of donors. Despite the financial challenges facing the health sector, marginal declines have been recorded on HIV/AIDS incidence amongst the 15-49 years category. Swaziland's greatest achievement in fighting disease is that it has seen the near-eradication of malaria. However, drug resistant tuberculosis is increasing.

Poverty reduction, social protection and labour

Despite its middle-income country status, poverty levels remain high. Even though poverty declined from 69% to 63% as reflected in the 2001 and 2010 Swaziland Household Income and Expenditure Survey (SHIES), huge regional differences in the prevalence of poverty remain. The driest regions of the country (Lubombo and Shiselweni) are the poorest. The Hhohho and Manzini regions, which include the major urban centres of Mbabane and Manzini, respectively, have the lowest poverty rates. Female-headed households are poorer than male-headed households, with 67% of the former group being considered poor compared to 59% for the latter. It has also been observed that rural households involved in non-commercial farming activities derive about 12% of their income from these activities and are the poorest. They are followed by self-employed headed households. Closely correlated to poverty is the extent of food security due mainly to unsustainable farming techniques, low rainfall and limited irrigable land. Extension services required to lift agricultural productivity, also, do not adequately cover smallholder farmers.

Efforts to reduce the poverty burden on the poor are being made. A social safety-net system, which includes cash and in-kind transfers, social care services, active labour market programmes, and community-based programmes, has been developed. Various ministries and departments are involved in the implementation of the programmes and these are the Department of Social Welfare (DSW) within the Deputy Prime Minister's Office (DPM), the National Emergency Response Council on HIV and AIDS (NERCHA), the Ministry of Education and Training (MOET), the Ministry of Health, and the National Disaster Management Agency (NDMA) in the DPM's Office. Some of the programmes that government is implementing include direct cash transfers in the form of old age grants, education grants to orphans and vulnerable children, and a public assistance grant system for disabled people. In-kind transfers are made up of school feeding programmes and Neighbourhood Care Points largely targeting children at risk of neglect, abuse and malnutrition.

Significant progress towards achieving the Millennium Development Goals (MDG) in the period before the fiscal crisis was not sustained. High levels of donor support have assisted Swaziland in registering successes, especially in the health and education sectors. Goal 2 (Achieving Universal Primary Education) and Goal 6 (Combating HIV/AIDS, malaria and other diseases) are likely to be achieved, while the rest still present significant challenges. The prevalence of HIV/AIDS is stabilised at 26%, yet it remains the highest in the world. This has reduced life expectancy to less than 50 years, adversely impacted labour productivity and has led to a smaller skills base. The fiscal situation has also suffered as the dependency ratio increased, leading to higher demands for public support; yet the fiscal crisis has constrained the government's ability to continue providing life-saving drugs to HIV/AIDS patients. Donors have moved in to fill the gap as far as prevention and treatment are concerned. However, the government has had to meet the costs of providing for orphans and the elderly who have lost their breadwinners. The introduction of the Free Primary Education Program, now in its fifth year, will ensure universal primary education by 2015. Net enrolments rose from 72% in 2007 to over 92% in 2010.

Gender equality

Despite progress on gender equality, including the ratification of international conventions such as the Protocol to the African Charter on Human Rights and People's Rights of Women in Africa in addition to the SADC Protocol on Gender and Development, strong paternalistic traditions are still to be overcome. According to the 2013 GHDR, Swaziland's human development index of 0.536 slipped down to 0.525 when gender inequality is considered and to 0.346 when adjusted for inequality. Women make up 53% of the labour force, although this is not been reflected in their labour force participation, where only 55% of them are employed compared to 76% of their male counterparts. Similarly, women are not adequately represented in politics and decision-making positions in the private sector. The recent elections resulted in less than 15% representation of women. The new government is expected to ratify the international conventions on gender. Government has formulated a number of policies and legislations that seek to protect the rights of marginalised people. A one-stop centre was established to cater for victims of gender based violence.

Thematic analysis: Global value chains and industrialisation in Africa

Swaziland's inflows of foreign direct investment (FDI) targeting the export market were larger than those for Botswana and Namibia in the early 1990s. Its attraction for such investments has declined since the demise of the apartheid regime in South Africa and the end of civil war in Mozambique. Despite the decline in FDI inflows, USD 136 million in 2010 to USD 90 million in 2012, the stock of foreign direct investment has remained significant at almost a billion dollars. In 2011 and 2012, the share of FDI in gross fixed capital formation was more than 24%. With foreign firms being key drivers of global value chains, Swaziland's participation in such activities, although small in terms of the global value, is quite significant at the domestic level. Swaziland's share in global trade, however, has fallen over the years – its share in world merchandise exports peaked at around 0.02% of world trade in 2004, but fell sharply to 0.01%in 2010. Exports have therefore declined as a source of economic growth, especially over the last decade, with the current ratio of exports of goods and services to GDP below the 30-year average of 0.67 and close to the value recorded in 1980.

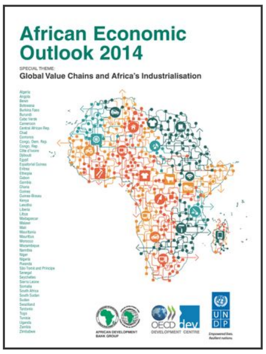
The *World Investment Report 2013* noted that value-added trade contributes nearly 30% to developing countries' GDP on average. Inflows of FDI constitute about 24% of GDP. Foreign direct investment is spread across many sectors of the economy, including natural resources, manufacturing and services. For a country whose trade openness ratio is about 1.94, global value chains are an important element of the country's economic activities. The exports from Swaziland include sugar and sugar products, forestry products, processed fruit products, textiles, soft drink concentrates, refrigerators and, more recently, pneumatic drills.

Based on the social accounting matrix for 2006, it is observed that the extent of value addition within specific sectors varies widely across products. In agriculture, for instance, winter grain, tobacco and canned fruit comprise of less than 20% in domestic value. Imports from South Africa and the rest of the world form most of the value in the final products. Such imports include packaging materials, marketing and transport services and the final products themselves. For canned fruit, the main producing firm is of South African origin and sells its product to the rest of the world and the home country. Opportunities for increasing local value are very limited in this operation due to the limited stages of production that are required to produce the final product unless Swaziland could attract a can producing firm. For the livestock and poultry sector, local value could be increased if Swaziland were to be able to increase the grain output that is required in feed production. Significant increases in productivity would be required to replace grain imports from South Africa.

In the extractive sector, the greatest domestic value is generated from forestry, coal, lignite and peat, while other mining activities generate less than 40% in domestic value. Once again, limited upscale activities in these products, given the size of the Swazi economy and the size of operations would suggest little scope to extract greater value out of such activities.

In manufacturing, sugar and textiles related activities are dominant in the Swaziland economy. As indicated in the Economic Diversification Study (EDS), the erosion of trade preferences for sugar and textiles pose a challenge for Swaziland. Although textiles are an important product by value, they constitute a large component of imports in the form of fabric. Given Swaziland's low labour costs and the rigid and hostile labour relations environment in South Africa, improving the productivity of labour could attract investments from its neighbour or further afield. With regards to sugar, critical issues relate to diversifying sugar products. Coca-Cola Swaziland (Conco Ltd) produces soft drink concentrates that are exported to 20 countries in Africa. Conco imports dairy products and sources most sugar materials locally. The EDS identified possible additional sugar and sugar-related products including chewing gum, solid sugar and alcoholic solutions as possible products where there is demonstrable competitive advantage. The existing relationship between Swazi and South African firms could also be exploited to diversify export markets.

Key challenges impacting negatively on Swaziland's ability to benefit from global value chains are the existing constraints to domestic production. Export-oriented firms have been hamstrung by an unfavourable investment environment, regulatory restrictions, government distortions and the high cost of trade. The service sector, which is one of the fastest growing sectors, especially telecommunications, is still to fully emerge out of a legislative bind that has impacted investments. Also, limited export market diversification has cast a shadow of uncertainty regarding trade preferences in key products. Limited access to finance by local small and medium-sized enterprises in the face of declining FDI affects the extent that the country can exploit existing links into global value chains.



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