Lesotho has made considerable progress towards a more equal society. However, although it is more equal than its neighbors, it remains among the top 20 percent of unequal countries. The main sources of inequality are inequality of opportunity and disparities in factor markets, with access to jobs and skills being severely constrained and uneven. Overall, relatively low human capital and uneven access to basic services and infrastructure, especially in rural and mountainous areas, perpetuate inequality of opportunity and hamper intergenerational mobility. Enhancing the quality of education, promoting skills development, creating jobs (especially for poor and young people), and paying special attention to lagging areas are key to accelerating the reduction in inequality.

A. Progress towards equality

Lesotho has made good progress towards a more equal society. In 2002, it was among the subset of countries with a Gini index above 50. But driven by inclusive consumption growth, by 2017 the per adult equivalent Gini index had fallen to 45.1. Lesotho is now more equal than its neighbors (Figure 1, panel a) although it remains among the top 20 percent of the world’s most unequal countries (panel b).

Figure 1. Inequality has fallen but remains relatively high

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Figure 1. Inequality has fallen but remains relatively high

a. Regional comparison of Gini coefficients

<table>
<thead>
<tr>
<th>Country</th>
<th>Gini Coefficient</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lesotho</td>
<td>45.10</td>
</tr>
<tr>
<td>Eswatini</td>
<td>53.20</td>
</tr>
<tr>
<td>Botswana</td>
<td>54.90</td>
</tr>
<tr>
<td>Namibia</td>
<td>59.30</td>
</tr>
<tr>
<td>South Africa</td>
<td>66.96</td>
</tr>
<tr>
<td>SACU Region*</td>
<td>68.77</td>
</tr>
</tbody>
</table>

Gini coefficient: 0-50 = low inequality, 50-65 = moderate inequality, 65-80 = high inequality


Note: Panel a presents the Gini coefficient of consumption for the whole SACU region, based on the earliest and latest rounds of household surveys from member countries.


2 The Gini index is a measure of inequality in a distribution. It varies between 0 (perfect equality), where every individual enjoys the same level of consumption per adult equivalent, and 1 (complete inequality), where a single individual accounts for all consumption.
B. Key drivers of inequality

Differences in tertiary or post-secondary education attainment are an increasingly important driver of inequality. Lesotho saw an increase in the contribution of post-secondary education to inequality (and with that, of education as a whole) between 2001 and 2018 (Figure 2). Very few adults have acquired tertiary education; this is also reflected in the country’s relatively low human capital levels.

The World Bank’s Human Capital Index (HCI) estimates that a child born in Lesotho in 2020 would reach only 40 percent of its potential productivity as an adult. Although this is an improvement from the 34 percent achieved in 2010, human capital in Lesotho remains relatively lower than in countries with similar levels of income.

Figure 2. Decomposition of inequality

a. Contribution of selected factors to inequality (%)

<table>
<thead>
<tr>
<th>Factor</th>
<th>2002</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Demographics</td>
<td>37.7</td>
<td>21.1</td>
</tr>
<tr>
<td>Education</td>
<td>43.8</td>
<td>19.9</td>
</tr>
<tr>
<td>Labor market</td>
<td>30.4</td>
<td>12.0</td>
</tr>
<tr>
<td>Location</td>
<td>19.9</td>
<td>3.6</td>
</tr>
</tbody>
</table>


Disparities in employment outcomes are an increasingly important contributor to inequality. Differences in labor market attributes (labor force status, industry of employment, and occupation type) account for 31.5 percent of overall inequality. Among these attributes, differences in occupation type (such as senior managers, professionals, and clerks), which reflect skills differences, contribute most to inequality. This is associated with wage disparities, which accounted for 77 percent of inequality in 2017 (as against the SACU average of 72 percent). Moreover, this is exacerbated by falling agricultural incomes, in part because of weather-related shocks, such as the 2015/16 El Niño event.

C. Inequality and the cycle of income generation

It is useful to analyze the process of household income generation to identify the sources of high and persistent inequality. The first step focuses on the pre-income distribution, which is the inequality of opportunity that arises from differences in circumstances at birth and during childhood, such as gender, race, location, parental education, and family wealth; these differences create expected inequalities in income distribution even before people interact with factor markets. The second component looks at the primary income distribution—how inequality is affected by access to factor endowments (or assets), such as education, skills, land, and capital, as well as their use and returns from interaction with markets. The third explores the secondary income distribution, assessing how inequality is influenced by taxes and government transfers. Finally, the fourth component relates to the tertiary income distribution—the disparities that remain after accounting for the role of social services (such as education, health, and infrastructure).
Box 1. Framework to assess sources of income and consumption inequality

The SACU regional inequality report uses an innovative framework built around the process that underlies household income generation to identify sources of high and persistent inequality. The framework is organized into four sequential components, presented in Figure 3.

**Figure 3. Framework to assess sources of income and consumption inequality**

- **Pre-income distribution: Inequality of opportunity**
  Arising from circumstances at birth or family background (including gender, race and parental education).

- **Primary income distribution: Inequality of pre-tax income**
  Influenced by differential access to, use of, and returns to assets (such as education, labor, land and capital).

- **Secondary income distribution: inequality after taxes and transfers**
  Affected by the structure, implementation capacity and incidence of fiscal policy.

- **Tertiary income distribution: Inequality after social services**
  Resulting from the provision of and access to public services (such as health, education and infrastructure).


**High inequality of opportunity**

Inherited circumstances strongly affect access to opportunities and are a major source of overall inequality. An analysis of the inherited circumstances for which data are available in all SACU countries—gender, age, region of residence (urban-rural, and regions)—suggests inequality of opportunity explained 14.7 percent of overall inequality in per capita consumption in 2017, up from 5.9 percent in 2002. The impact is even larger when human capital achievements during childhood, serious health problems, and environmental shocks are included in the analysis (World Bank 2019). Differences in educational achievement during childhood are found to be the most important contributor to unequal opportunities.

Inequality of opportunity is perpetuated by uneven and inequitable access to basic services, with rural and mountainous areas particularly affected. Although access to basic services has increased, this has largely been driven by significant gains in urban areas, and coverage in rural areas remains low. The poorest segments of the population tend to have the least access to services, which perpetuates the lack of both capacities and opportunities for these members of society.

Intergenerational mobility is relatively low, as is evident from the high correlation between a person’s life outcomes and those of their parents. The correlation between parents’ years of schooling and those of their children is particularly high relative to other countries. Schooling tends to be a strong predictor of lifetime earnings, and people born into poorer families are less likely to have access to this key pathway to economic mobility, making it difficult for them to advance.
**Inequities in labor market outcomes**

Limited job creation has led to poor labor market outcomes. Unemployment is particularly high among young people, women, and rural residents. According to the 2019 Labor Force Survey, the national unemployment rate ranged from 22.5 percent (standard definition) to 38.3 percent (expanded definition). The COVID-19 pandemic has exacerbated the unemployment challenge, both for the informal sector and for the many Basotho workers who cross the border to work in South Africa. Lesotho's textile sector, the biggest employer after government and a key employer of women, has been particularly affected by the pandemic. Slow job creation reduces the country’s potential to harness the demographic dividend associated with an increase in life expectancy and in the supply of working-age people alongside declining dependency ratios. Young people are more likely to be unemployed (29.1 percent), because of skills mismatches. The difference education makes to the probability of employment divides the labor market across skills and is a key factor underpinning income inequality.

Women have worse labor market outcomes than men. They are less likely to participate in the labor force, have a higher probability of being unemployed, and tend to earn relatively less. Although this gender effect varies considerably in SACU, it is highest in Lesotho: women are 19.7 percentage points less likely to be employed than men, after controlling for age, education, and geography. There is also a substantial gender wage gap that is not explained by differences in occupation or education. Women earn 32.1 percent less than men on average, even controlling for personal demographics, location, sector, occupation, education, and formality.

**Inequities and inefficiencies in social spending**

Social assistance reduces inequality, but the social protection system suffers from some administrative inefficiencies. Significant increases in social assistance between 2002 and 2017, particularly for the poorest people, helped reduce inequality. The main driver was old-age pensions, a noncontributory social assistance program introduced in 2004 to provide monthly cash transfers to citizens over 70—one of the poorest segments of the population. However, the targeting of some social protection programs could be improved, particularly post-secondary education bursaries, which are costly and tend to favor nonpoor households and thus widen disparities. To this end, Lesotho can leverage its social registry and targeting system, the National Information System for Social Assistance (NISSA), which already covers all 64 rural community councils and is being rolled out in the urban councils.4

**Spending on tertiary education is relatively high.** Around a third of the education budget is spent on tertiary education, despite participation rates in this level of education being much lower. Spending on tertiary education tends to benefit the wealthiest deciles and so increase inequality, because students who reach this level are disproportionately nonpoor. In contrast, spending on basic education benefits poorer people.

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**High vulnerability to climate change risks and economic shocks**

Because poor people have limited coping mechanisms, they suffer disproportionately from the adverse effects of climate change. The livelihoods of poor people are inextricably tied to the agriculture sector, which is often adversely affected by droughts and heavy seasonal floods. When shocks occur, households have few coping mechanisms, particularly for shocks that affect many households in the same community at the same time. They are often forced to reduce consumption, with long-run consequences for human capital attainment among their children. For instance, rural areas responded to the 2015/16 El Niño-induced drought by reducing consumption by an average of 23 percent. Without the drought, rural poverty would have been 6 percentage points lower, and the pace of national poverty reduction would nearly have doubled (World Bank 2020).

**The COVID-19 pandemic has increased economic vulnerability and likely widened disparities.** The pandemic has exacerbated the triple problem of high unemployment, poverty, and inequality. Poor and vulnerable people are again disproportionately affected because they lack the productive capacity to deal with and recover from the adverse socio-economic impacts of the crisis. Job losses and the subsequent decline in household...
incomes are, in turn, likely to reduce household investment in human capital.

**Social protection programs can potentially offset consumption losses from shocks; however, they currently cover only a small fraction of climate-vulnerable households.** Existing social protection programs tend to provide supplemental income rather than risk insurance. This limits the degree to which they can help households mitigate the impact of shocks.

### D. Policy considerations to accelerate the reduction in inequality

**Strengthen human capital.** In education, this requires enhancing the quality of education (ensuring that children are learning in school) by improving literacy and numeracy outcomes in the early grades. Given the high dropout rates in secondary school, developing and implementing a plan to retain secondary school students is important for strengthening human capital. Further, investing in nutrition through well-targeted investments, particularly for young children in their first 1,000 days, will help break the intergenerational cycle of malnutrition and poor health, and support human capital accumulation. These efforts must pay particular attention to lagging rural and mountainous regions.

**Promote private investment and exports to create jobs, ensuring equitable access.** Creating jobs requires strengthening the private sector through demand- and supply-side reforms. On the demand side, policies to make it easier to obtain a business license, enhance access to finance, and reduce regulatory compliance costs would improve the business environment. To this end, Lesotho could leverage the Prime Minister’s Delivery Unit to accelerate the adoption and implementation of outstanding legislation and business environment reforms. Closing gaps in key infrastructure such as electricity, sustainable and safe road connectivity, and information and communication technology is also important. In addition, pursuing deeper regional integration and trade dialogue with South Africa, the United States, and the European Union would help support Lesotho’s private sector. Given the dominance of micro-, small and medium enterprises, these reforms should focus on strengthening the ecosystem for such enterprises and improving their access to finance. On the supply side, targeted policies that boost entrepreneurship and promote skills development would increase the supply of skilled labor, enhance labor productivity, and reduce inequality. It is particularly important to strengthen the skills and employability of young people and ensure a gender-nuanced approach. As most poor people rely on subsistence agriculture, **raising productivity among smallholder farming households and microenterprises is important for addressing inequality in primary income.**

Promoting sustainable landscape management, including integrated catchment management and climate-smart agriculture, can increase agricultural productivity and incomes and contribute to a more vibrant rural economy, which in turn would reduce inequality.

**Improve the equity and efficiency of public spending.** In social protection, improving the administration of the social protection system by moving away from paper-based application processes to a unified web-based platform for applications and the delivery of benefits would strengthen the impact of social protection on inequality reduction. This could be complemented by better targeting of some social protection programs, particularly post-secondary education bursaries, which are costly and tend to favor nonpoor households. A good targeting mechanism, based on means tests and linked across programs, would be an important improvement. In education and health, it is vital to ensure that quality is commensurate with spending. This entails improving the targeting and efficiency of public spending, and enhancing complementarity between social protection programs and education, nutrition, and health investments, especially among young people.

**Strengthen climate risk management and resilience.** This entails improving the policy and institutional framework through strengthening the capacity of relevant ministries for risk and vulnerability assessment and supporting the Disaster Management Agency (and other relevant ministries) in disaster preparedness and response. Developing and adopting a national disaster risk management policy and strategy, along with a financing strategy, would improve the policy and institutional framework for climate risk management and resilience. The disaster risk management policy and strategy would require updated and harmonized institutional and regulatory frameworks, as well as sectoral policies and plans. The disaster risk financing strategy would formalize policy priorities based on a risk-layering approach and address both budget mobilization and budget execution. Overall, strengthening climate risk management and resilience requires a comprehensive approach that reduces risk and prevents disasters (physical resilience); minimizes the financial impact of shocks on the fiscal balance, subnational governments, households, and businesses (financial resilience); and helps households and society cope with shocks (social resilience).
Enhance the responsiveness of the social protection system to shocks. This would build on ongoing efforts by the Ministry of Social Development, in coordination with the Disaster Management Authority and with the support of development partners. An early warning system that informs, through clear and transparent rules, when and where to scale support would be required. Other requirements are prefinancing arrangements to finance the added benefits and a national database of all potential beneficiaries (e.g., real-time birth, death, income, location, and contact data) to help target social grants. This would build on progress made to update, extend, and strengthen the NISSA database, which stores some social payments data. It is also important to digitize government-to-person (G2P) payments faster but without excluding vulnerable populations. Strong institutional, legal, and technical safeguards must be implemented to ensure data protection and privacy.

Selected references
