

Unleashing Private Sector Job Creation: Challenges and Opportunities for Lesotho

Athene Laws and Ann-Alice Ticha

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Unleashing Private Sector Job Creation: Challenges and Opportunities for Lesotho

Prepared by Athene Laws and Ann-Alice Ticha *

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ABSTRACT: Lesotho's public sector led growth and employment model has struggled to develop a flourishing labor market, and recent external shocks have made developing job-rich growth an even more urgent priority. The primary challenge is a lack of labor demand due to a small, undiversified private sector and steep barriers to firm growth. Nonetheless, labor supply issues, including skills mismatches also compound the challenge. Addressing this issue will require a concerted effort on multiple policy fronts; combining public-sector reform, business-environment reform, expanding financial access for firms, better skills matching, and careful macroeconomic management.

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Author's E-Mail Address:	ALaws@imf.org , aticha@imf.org

SELECTED ISSUES PAPERS

Unleashing Private Sector Job Creation: Challenges and Opportunities for Lesotho

Kingdom of Lesotho

Prepared by Athene Laws and Ann-Alice Ticha ¹

¹ “The author(s) would like to thank Qianqian Zhang for her helpful comments, and the Lesotho authorities, civil society organizations, and market participants who engaged in discussions on the topic during the Article IV mission in June 2025.

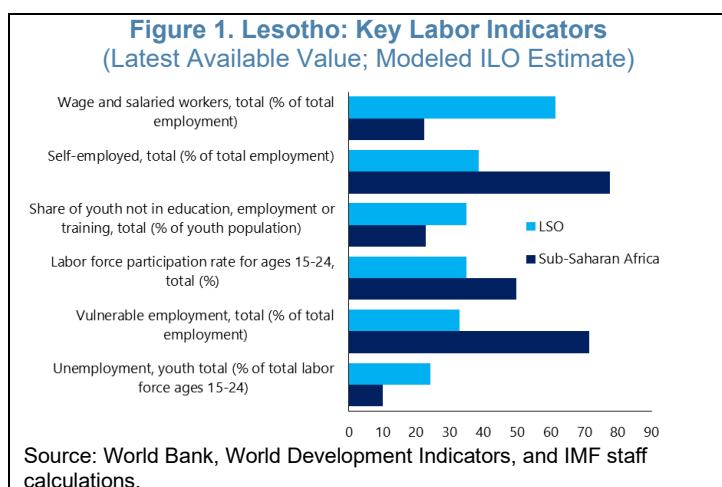
A. The Employment Landscape in Lesotho

1. For decades, Lesotho has operated a public sector led growth and employment model that has failed to deliver increased living standards. At 53 percent, Lesotho has one of the highest public expenditure to GDP ratios in the region, and 17 percent of GDP is spent on public sector wages alone (2024 estimates), accounting for 72 percent of tax revenue. Yet GDP per capita has fallen 14 percent between 2016 and 2023, with Lesotho possessing one of the lowest per-capita growth rates amongst its peers. Over half of the economy's formal workers are public sector employees and they earn, on average, over four times the median private sector wage (ILOSTAT, Lesotho 2023 SIP). The key engine for growth has been a series of mega projects, most recently the Lesotho Highland Water Project Phase II (LHWP-II). These projects tend to be capital intensive and source most of their workers and inputs from abroad, so spillovers to local employment and firms are small. Other key sectors, for example water exports and diamond mining, contribute significantly to GDP but generate little employment. The lack of job intensity from growth drivers matches regional trends: sub-Saharan African growth is not as job intensive as elsewhere in the world (IMF 2024).

2. Consequently, the labor market is marked by high unemployment, high informality, high poverty and a reliance on remittances

(Figures 1 and 2). The unemployment rate is high, estimated at 16 percent in 2024 versus 6 percent in Sub-Saharan Africa and 5 percent for emerging market and developing economies (EMDEs) around the world (ILOSTAT). Only 60 percent of people participate in the labor market (versus more than 70 percent for sub-Saharan Africa), and of those, nearly 80 percent are informally employed. Nearly four in ten people live in extreme poverty on less than \$2.15 per day (World Bank 2025). With

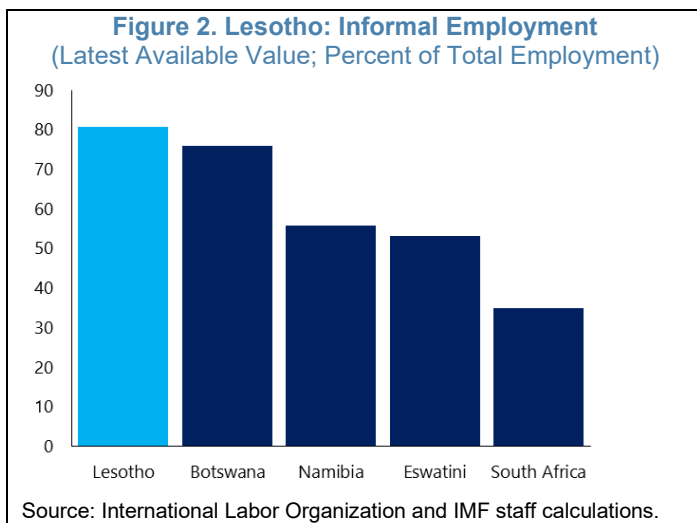
limited local jobs, many Basotho emigrate in search of better opportunities, sending over 20 percent of GDP home in remittances every year. While the humanitarian impact of remittances is essential, they are limited in their ability to drive jobs-rich, balanced growth (World Bank 2025).



3. On top of these structural challenges, Lesotho faces a deteriorating external environment around trade, aid, and geopolitics. Textiles has been a key sector for lower-skilled employment yet shrunk from a peak of 60,000 workers to around 30,000 currently due to declining global competitiveness, and an uncertain future outlook. In particular, textiles dominate exports to the United States (which account for near 10 percent of GDP) and could be severely impacted by possible trade policy changes—the African Growth and Opportunity Act (AGOA) may not be extended upon expiration in September, and potentially steep tariffs on exports to the United States are under discussion. Large cuts to official development assistance also include the possible cancellation of the Millennium Challenge Compact (MCC), which had been anticipated to kickstart significant private sector growth and increase employment opportunities in new sectors. Deepening

geoeconomic fragmentation could also reduce growth in key trading partners, most notably South Africa. In light of this daunting outlook, there is an urgent need for private sector led job creation.

4. The primary challenge in Lesotho is a lack of labor demand. Given that public sector dominance has not generated the desired employment and living standard outcomes, Lesotho must switch gears toward enabling more private sector job creation. However, the private sector is small, undiversified, and subject to considerable constraints. At a macro-structural level, the economy is concentrated in a small number of low value-added sectors (Section B). At the micro-level, private firms are constrained by barriers including limited financial access, corruption, policy instability, and informal sector practices (Section C). A secondary challenge is a labor supply mismatch, particularly for key skills, with individual workers facing challenges in accessing the labor market – most notably women and youths (Section D). A broad suite of policies targeting these barriers will be required, which in turn will require a sustained multi-year reform agenda (Section E).



5. A concerted, coordinated effort could change this bleak picture. A feasible reform scenario that incorporates macro-fiscal reform could increase growth by 1.5 percentage points (2025 Article IV upside scenario). Using estimates of the median elasticity between growth and job creation for sub-Saharan African (IMF 2024), this growth increase could be associated with the creation of 4,800 jobs per year. However, sub-Saharan Africa's growth is not job intensive as elsewhere in the world, generating only one-third the number of jobs seen in emerging markets and developing economies elsewhere. If comprehensive reforms boost the job-intensity of growth to levels seen outside the region, the same 1.5 percentage point increase in growth could create 14,000 jobs per year. Quantitatively, this would rapidly be enough to counteract the jobs lost through the recent shocks.

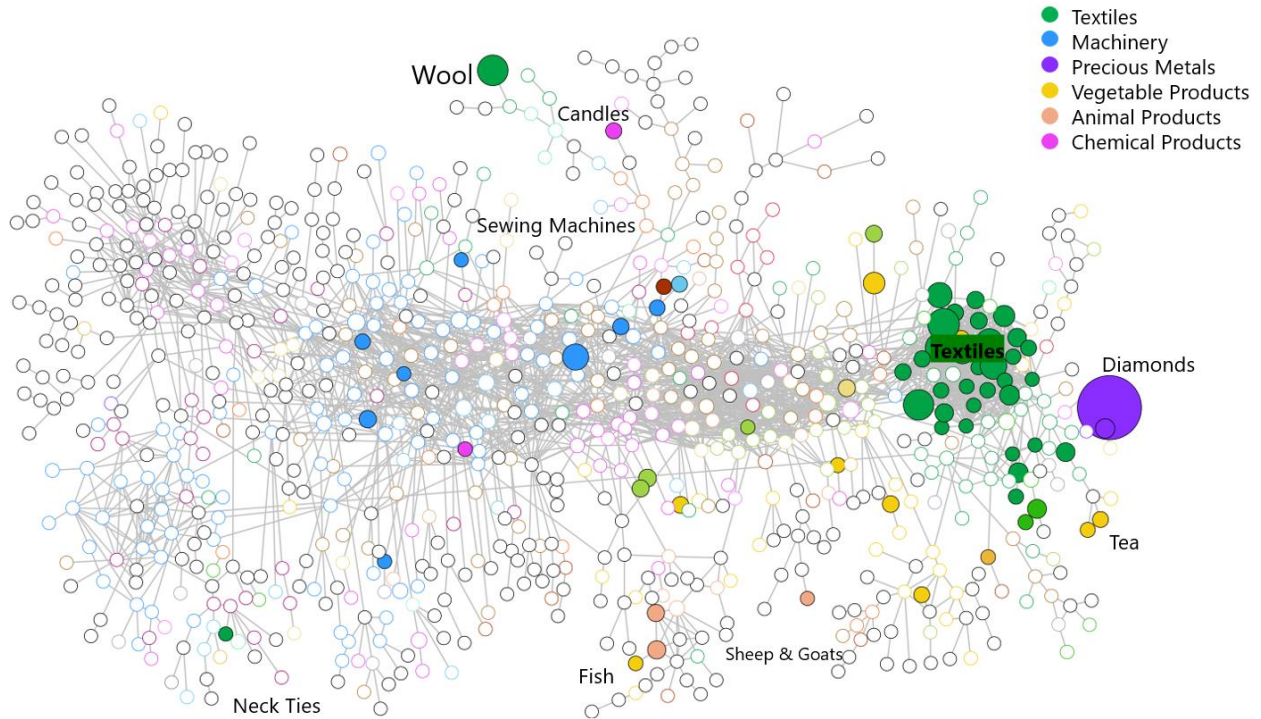
B. Macro-structural Barriers to Job Creation: Economic Activity is Concentrated, Limiting Structural Transformation

6. At the macroeconomic level, the economy is overly reliant on a few key sectors.

Figure 3 plots the product space of Lesotho and the linkages between different sectors in a network map. More central nodes are more connected—meaning there are more related industries to move towards. Lesotho's output is dominated by a small number of more peripheral (less connected) product clusters: most notably textiles, diamonds, wool, some machinery manufacturing and limited food and beverage manufacturing. A more diversified economy would have a greater number and spread of sectors, with more products located at the center of the chart.

Figure 3. Lesotho: Product Space Network
(Lesotho, 2023)

Lesotho's product space is defined by a cluster of products surrounding the textile industry and a few marginal products. To build a more resilient economy, the product space needs to diversify and move more towards the center where tight connections will help maintain agility even during sectoral shocks.



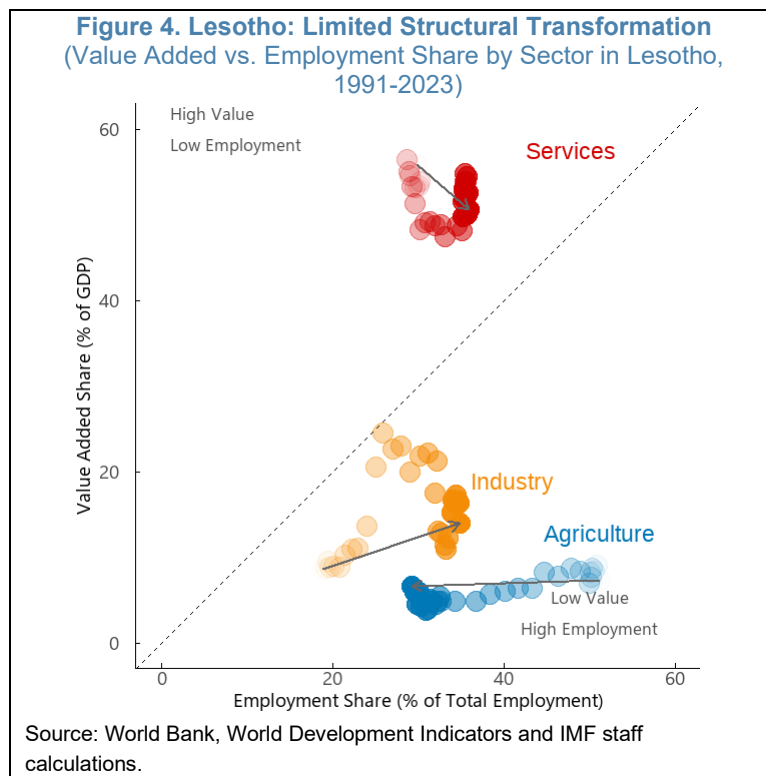
Source: Observatory of Economic Complexity, Lesotho Country Card and IMF staff.

7. Several key sectors are at the start of the value chain and not well connected to other potential products. Raw diamond mining and wool, for example, are large sectors that are located on the fringes of the network, limiting the opportunities to move into related industries. These sectors tend to also be at the bottom (upstream) of value chains, which typically offer less value added than higher (downstream) value chain stages. Bhorat and others (2019) outline how moving towards more complex, connected products tends to boost productivity, growth and resilience in an economy, allowing it to move up the value chain. However, it is much more difficult to enter industries that are less related to a country's existing product space. As such, it is more feasible to shift towards more central nodes of the existing product space and then move sideways to other related industries.

8. The textiles sector is the largest, more centrally located product cluster, but current trends suggest that even this advantage is at risk. If large trade shocks or declining competitiveness accelerate the downward trend in textile exports, the opportunities to move sideways into related manufacturing products will diminish. Food and beverage manufacturing and machinery manufacturing are other central sectors, but their scale in Lesotho is very small at present. So currently, Lesotho's economy risks not only losing its key existing employment industry, but also its ability to diversify easily into related industries.

9. Structural transformation has been limited, keeping the economy in a low productivity job trap.

Structural transformation refers to the movement of workers and economic activities from low value-added activities into high value-added activities, for example from basic agriculture into manufacturing or modern services. This pattern has been observed in EMDEs around the world, but only to a lesser extent in sub-Saharan Africa (IMF 2024). In Lesotho, there is very weak evidence of structural transformation. Figure 4 plots the relative shares of employment and value added, with points above the 45-degree line indicating relatively productive sectors (a higher share of value added than employment), and points below the 45-degree line indicating relatively less productive sectors. The least productive sector, agriculture, has shed some employment share as workers have moved into services and industry since the early 1990s. However, the evolution in productivity shares does not reflect effective structural transformation. Industry's share of value added has not increased proportionally with its employment growth, indicating a deterioration in its relative productivity. Productivity in services is even more sobering: despite its share of employment increasing, the share of value added has fallen. Overall, the economy has not transitioned towards more productive sectors as hoped.



10. Structural transformation requires moving up the value-added chain and diversifying, but not all high value sectors come with employment intensity. Many high value-added sectors (e.g. mining, clean energy) are by their nature capital intensive, not labor-intensive. To illustrate, Figure 5 shows the labor intensity of all 2-digit manufacturing sectors internationally – services are excluded due to a lack of reliable data. One of Lesotho's key industries, textiles, is one of the most labor-intensive industries internationally. Others, such as food and beverage and machinery manufacturing, are still above average. Manufacturing of raw materials, most relevant to Lesotho's diamond industry, is one of the least labor intensive. Nonetheless, even lower-employment intensity sectors can generate employment spillovers through ancillary industries and local demand.

11. Modern day structural transformation will look different to the past. In historical episodes of economic change (for example East Asia in the twentieth century), workers moved out of basic agriculture into manufacturing and, later, modern services. However, technological change has meant manufacturing is less labor intensive than in the past, thus past patterns for generating mass employment are less easy to replicate (Rodrik 2016, 2022). Fortunately, there are several other industries that provide potential, sometimes called 'Industries Without Smokestacks' (Page 2020). These feature a degree of labor intensity, scope for productivity growth and export capacity, and include: modern services such as tourism and financial services, high value agriculture and agro-processing.

12. Tourism, one of Lesotho's most promising potential industries, but is overly constrained. Tourism is a job intensive industry, and Lesotho's natural environment, cultural history and location in the Southern African tourist region present significant tourism growth potential, particularly in rural areas (UN 2023). Key barriers include inadequate infrastructure, with poor road and electricity access hampering

Figure 5. Lesotho: Job Intensity by Manufacturing Sector
(2019; 2-Digit Manufacturing Sectors Ranked by Employment to Value Added)

37	Recycling
19	Leather, leather products and footwear
18	Wearing apparel, fur
17	Textiles
36	Furniture; manufacturing n.e.c.
31	Electrical machinery and apparatus
20	Wood products (excl. furniture)
26	Non-metallic mineral products
25	Rubber and plastics products
30	Office, accounting and computing machinery
22	Printing and publishing
15	Food and beverages
28	Fabricated metal products
29	Machinery and equipment n.e.c.
<i>Average manufacturing</i>	
34	Motor vehicles, trailers, semi-trailers
35	Other transport equipment
21	Paper and paper products
27	Basic metals
24	Chemicals and chemical products
16	Tobacco products
23	Coke, refined petroleum products, nuclear fuel
33	Medical, precision and optical instruments
32	Radio, television and communication equipment

Source: UNIDO data and staff calculations. The survey covers manufacturing firms around the world. Results are similar focusing exclusively on SSA economies.

investment and development of potential tourist sites. Air connectivity is also limited and expensive while more cost-effective bus options take long, indirect routes, making travel to Lesotho more challenging. Trains could be another alternative, but currently only provide freight services. The visa process is also a significant hurdle, with high costs and an unreliable online system. Additionally, the reliance on South African statistics for traveler data and the lack of comprehensive internal data collection pose challenges for effective planning and development. Political influences on infrastructure development decisions further complicate efforts to improve access to tourist sites. Despite being situated in a heavily tourism-focused region, Lesotho has been unable to capitalize on regional tourism opportunities due to these challenges.

13. Agro-processing and agricultural-product related manufacturing are other examples of potential, but currently constrained, diversification. Lesotho holds significant potential in the horticulture, herbal (e.g. rosehip oil), natural cosmetics, honey and food processing industries, but these are struggling to scale upward appropriately. Rural infrastructure deficiencies are a key challenge here with insufficient irrigation, quality roads, rural logistics hubs, and cold chain storage. Meeting and certifying international standards are further challenges; the country has no current laboratory able to certify International Standards Organization (ISO) requirements. Various development partners, including the MCC and German Corporation for International Cooperation (GIZ), are supporting the development of industry specific national standards and the African Development Bank is funding a local standards lab to be built in the coming years. Businesses also struggle with the lack of a functioning e-commerce platform in Lesotho, because the current national payments system is not compatible with online payments. Reaching larger markets is therefore much more difficult.

C. Firm-level Barriers to Job Creation: Firms Face Many Barriers to Growth

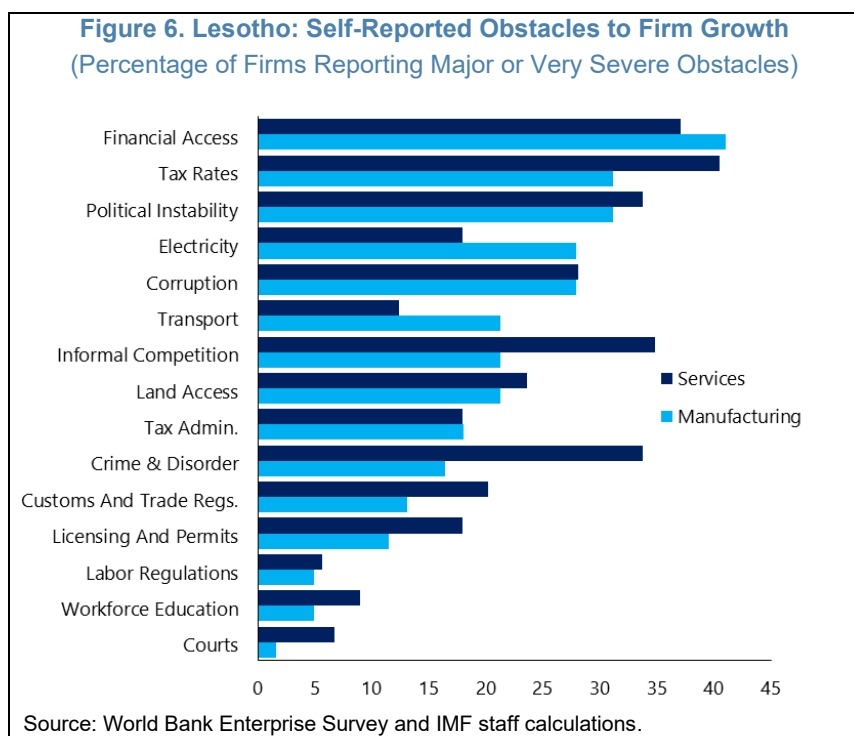
14. Micro, small and medium enterprises (MSME) are a key source of employment in Lesotho. The MSME sector employed an estimated 360,000 people in 2023, with 55 percent of MSMEs owned by women (FinScope, 2025). Almost half of MSMEs are in the wholesale or retail sector, with a further 20 percent in agriculture and 17 percent in manufacturing. Most are informal, but the formalization rate did increase from 18 percent in 2016 to 24 percent in 2023. These firms tend to be very small, with average monthly turnover ranging from USD \$390 in manufacturing firms to USD \$1,100 in household firms. Eighty-two percent are informal firms (unregistered), with half of those reporting the primary reason for informality is their small size. Many state they would formalize if registration were free, there were clear benefits explained to them, or if they had more information.

15. But MSMEs struggle to grow into larger enterprises that can employ more people.

Internationally, job creation is often most marked in medium to large firms, and these firms tend to pay higher wages and drive productivity growth. A large body of literature posits a 'missing middle' for firm size in Africa, with an overabundance of micro and small firms that struggle to scale up (see, for example, Abreha and others 2022). Comprehensive data is limited, but it similar issues are likely in Lesotho. Many of the large firms present in Lesotho are subsidiaries of South African parent companies and respond primarily to South African conditions. To understand the barriers preventing MSMEs growing, multiple firm level surveys have been undertaken, including the World Bank Enterprise Surveys (Figure 6) and the B-READY surveys.

16. Firms report access to finance as the primary barrier to growth, followed by a range of political and governance challenges.

Around 40 percent of firms report that accessing finance is a major or very severe obstacle (Box 1). Many firms also report political and governance challenges as key barriers, which mainly reflect concerns over regulation, tax rates, corruption, and political instability. In contrast, Lesotho performs relatively strongly for the effectiveness of the court system and its labor regulations, which is confirmed by the World Bank's B-READY analysis.² Adequacy of education is also not a key constraint, pointing again to the key role of labor demand, rather than labor supply, as Lesotho's main challenge.



17. Lesotho's overall business environment is unfavorable. It takes an average of 15 days to obtain an operating license, 73 days to obtain an import license and 78 days to obtain a construction related permit, all well above the SACU average (World Bank B-READY). Export-oriented firms have also identified the difficulties in obtaining employment visas and exchange restrictions. Many firms in the B-READY survey report having to pay unofficial 'compliance fees' to receive permits and services. Transparency International scores Lesotho at 37 out of 100 on the Corruptions Perception index in 2024, a score that has steadily declined since 2012.³ Moreover, given the dominance of the public sector, inefficiencies in government tendering, from a lack of competition and delayed payment, also shape the business environment. Firms in the B-READY survey perceive that government tender requirements are difficult to comply with. Even in cases where firms successfully win the tender, it takes 152 days for firms to receive payment under government contract

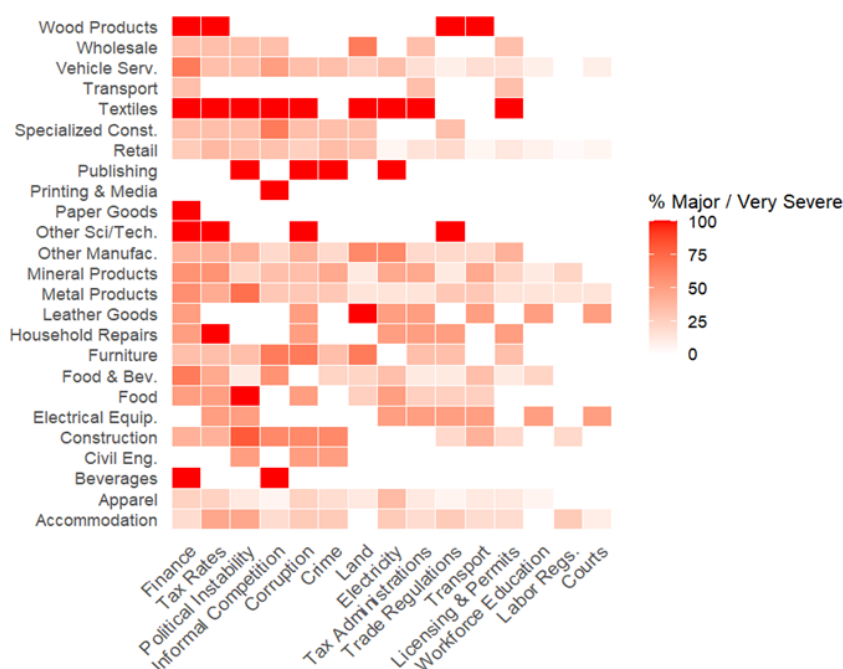
² Several disclaimers are noted for the B-READY scores. The scores could be biased, reducing compatibility across indicators and economies, since the computed scores under the Regulatory Framework and Public Services pillars are mainly collected through expert questionnaires using a small sample of responses (up to five per topic). There are inevitable inconsistencies in raw data, given the significant disparities in development levels and contextual differences among countries. Since the enterprise survey currently includes data only from registered firms, B-READY does not provide insights into the informal sector. The methodology is expected to be refined and evolve through additional iterations and feedback during the three-year rollout phase, from 2024 to 2026. Therefore, comparability across time may be reduced. Complexity in the methodology can reduce transparency. The questionnaires and surveys are not conducted within the same timeline. Survivorship bias is one of the caveats for the interpretation of results obtained from firm-level surveys (the report already acknowledges this caveat).

³ The CPI does not tell the full story of corruption in a country, only the level of corruption in the public sector in the past two years. CPI scores before and after 2012 are not strictly comparable, given the change in methodology in 2012.

(more than twice the sub-Saharan African average). B-READY also assesses market competition as weak, perhaps reflecting the small size of the economy. Streamlining the tax and licensing systems, and leveraging digital tools can be effective at unburdening administrative procedures and tracking compliance (World Bank 2024).

18. Competition from the informal sector compounds the weak business environment. Lesotho's high degree of informality is driven by weak institutional support, limited access to finance, and a lack of incentives to formalize. Insufficient levels of 'carrots' (incentives to formalize) and 'sticks' (enforcement) are present. Indeed, four in five informal sector firms state they would be willing to formalize if registration were free, they understood clear benefits, or it was less time consuming (Finscope 2025). The government recently announced free registration for youth led businesses, which is a step in this direction. Formalization also becomes more attractive if it enables greater access to finance, social protections and public procurement opportunities (ILO 2025).

Figure 7. Lesotho: Self-Reported Obstacles to Firm Growth by Industry
(Percentage of Firms Reporting Major or Very Severe Obstacles)



Source: World Bank Enterprise Survey and IMF staff calculations.

19. Despite its natural endowments, reliable and accessible electricity is another private-sector bottleneck. Despite having one of the lowest electricity prices for businesses in the region, operational inefficiencies and financial shortcomings of the Lesotho Electric Company (LEC) have undermined reliability and accessibility.⁴ About 65 percent of businesses experience electricity outages. The effects on operations are exacerbated because only about a quarter of Lesotho's businesses have access to a back-up electricity generator, compared to nearly half of sub-Saharan African firms (World Bank B-Ready). Furthermore, it takes a long time for business owners in Lesotho to obtain an electrical connection: 52 days versus the SACU average of 38 days. Consequently, about 30 percent of businesses identified electricity as a major to severe

⁴ Electricity prices for businesses in Lesotho are about 0.021USD/kWh, well below the African average of 0.123USD/kWh (Global Petrol Prices). While on paper an advantage for businesses, the prices are artificially low, with LEC importing around 50 percent of the nation's total electricity demand from South Africa and Mozambique and selling at a loss. LEC declared bankruptcy in 2025, underscoring the precarious nature of the electricity sector in Lesotho.

obstacle. In addition, the USA ITA estimates that only one-fifth of a potential 450 MW is currently utilized. Efficiently exploring the renewable electricity potential could ensure a stable, plentiful and cheap domestic supply and export capacity, generating a key business environment advantage for Lesotho in an electricity constrained region. Deep reforms to the electricity market and LEC governance are required to establish an efficient, accessible and reliable electricity sector that supports foreign direct investment.

20. These barriers are broadly shared across industries and geographic locations (Figure 7). There is some variation – manufacturing, for example, is more constrained by electricity than services, while crime, theft and disorder matter more for services. Many barriers are exacerbated in rural areas - for example access to finance, internet and electricity are even more binding for rural businesses (FinScope 2025). In general, the strong correlation of barriers implies that addressing the steepest barriers will benefit a wide swath of Lesotho's private sector.

21. Moving from survey impressions to actual outcomes, empirical analysis shows that firms employ fewer people and experience slower revenue growth when faced with these barriers. Firm level data on revenue, employment and reported barriers are used to measure the impact on business performance (see Amine and others, forthcoming). Firstly, principal component analysis consolidates all the barriers into seven key areas: financial constraints, informal competition, corruption, inadequate labor education, weak business environment, inadequate infrastructure and lack of security. Then, the three-year growth rate of employment, or revenue, is regressed on these indexes. Even accounting for the small sample size of Lesotho's data, the results in Table 1 show that a one standard deviation increase in financial constraints in Lesotho are associated with a drop in firm employment growth by 0.5 percent over three years. Negative employment effects are also found at the SACU level for informal competition, corruption, and inadequate education. Addressing these barriers is therefore critical to unlocking employment growth in Lesotho.

Table 1. Lesotho: Regression Results: Growth Constraints in Lesotho and SACU
(Dependent Variables: Employee and Sales Growth)

Variable	LSO: Employee Growth	SACU: Employee Growth	LSO: Sales Growth	SACU: Sales Growth
Financial Constraints	-0.512**	-0.0129	-0.656**	-0.156***
<i>Financial Constraints (Robust SE)</i>	(0.258)	(0.0324)	(0.302)	(0.0316)
Informal Competition	-0.146	-0.148***	-0.0189	-0.240***
<i>Informal Competition (Robust SE)</i>	(0.125)	(0.0407)	(0.149)	(0.0477)
Corruption	-0.269	-0.310***	-1.586	-0.592***
<i>Corruption (Robust SE)</i>	(1.719)	(0.0708)	(1.747)	(0.0737)
Inadequate Labor Education	-0.143	-0.0748*	-0.479**	-0.139***
<i>Inadequate Labor Education (Robust SE)</i>	(0.156)	(0.0391)	(0.195)	(0.0483)
Inadequate Infrastructure	-0.0731	0.0898**	0.0166	0.220***
<i>Inadequate Infrastructure (Robust SE)</i>	(0.102)	(0.0422)	(0.134)	(0.0528)
Weak Business Environment	-0.0495	0.0841**	-0.398**	0.00704
<i>Weak Business Environment (Robust SE)</i>	(0.148)	(0.0365)	(0.171)	(0.0449)
Lack of Security	0.152**	0.0553*	-0.0339	0.0143
<i>Lack of Security (Robust SE)</i>	(0.0775)	(0.0282)	(0.0929)	(0.0317)
Constant	1.993	0.391	5.340***	2.305***
<i>Constant (Robust SE)</i>	(1.218)	(0.255)	(1.299)	(0.296)
Observations	451	4,225	451	4,225
R-squared	0.073	0.110	0.121	0.199

Note: Robust standard errors in parentheses. *** p < 0.01, ** p < 0.05, * p < 0.1

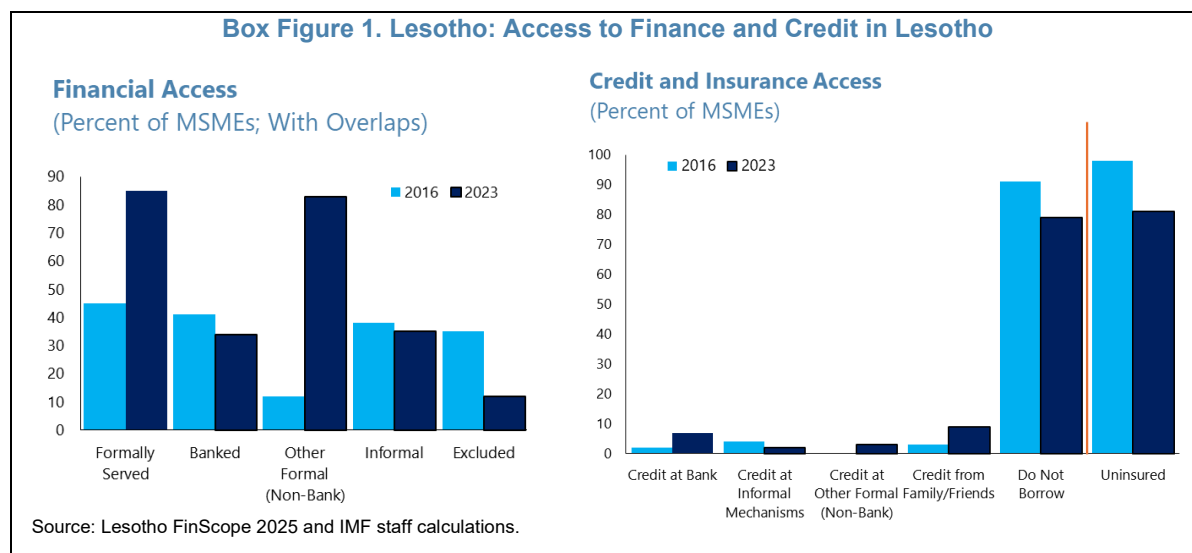
Source: World Bank Enterprise Survey and IMF staff calculations.

Box 1. Lesotho: Financial Access is a Key Job Creation Bottleneck

Lesotho's financial sector is shallow and highly concentrated, with few funds directed towards private sector firms. The financial sector is dominated by four commercial banks—three subsidiaries of South African banks and one state-owned bank—which primarily serve salaried individuals through payroll-based personal loans, and which therefore have limited engagement in corporate or MSME lending. The banking sector is characterized by excess liquidity, limited competition, and a narrow product offering. Non-bank financial institutions (NBFIs), including microfinance institutions (MFIs), insurance providers, and savings and credit cooperative societies (SACCOs), play a marginal role in business finance. Capital markets are nascent, with only one equity listing on the Maseru Securities Market.

While financial access for individuals has seen gains in Lesotho, firm access remains a key barrier to growth. The advent of mobile money has significantly enhanced individual financial inclusion. As a result, 7 percent of Basotho had financial access in 2021, up from 60 percent in 2011 (Finscope 2024). However, access for firms remains very limited, and two thirds of firms highlight insufficient operational cash flow as a key challenge (Finscope 2025). Only 17 percent of MSMEs have a formal bank account and only 10 percent receive credit from a formal financial institution in 2023 (Finscope 2025). Most MSMEs instead rely on mobile money (66 percent) for transactions, and informal mechanisms for saving and credit. Banks report SME lending as too high risk, with limited bankable projects, and instead focus on FDI and state-level projects. SACCOs provide localized business finance through their cooperative structure, but they are limited in scale. Banks, in turn, do not leverage SACCOs local networks and enforcement as intermediation to scale lending. There is an insurance gap too with 89 percent of firms not covered for any personal or business risk.

Box Figure 1. Lesotho: Access to Finance and Credit in Lesotho



A variety of factors ensure banks are hesitant to enter the credit business and assume direct lending to firms. The high degree of informality and lack of financial records by many firms inhibit lending—only 22 percent of MSMEs reliably keep financial records and only 18 percent are registered (Finscope 2025). In addition, Lesotho's credit infrastructure remains weak – only banks and the few largest NBFIs consistently share credit information to the bureau, and MSMEs are currently excluded from credit record coverage altogether - making it difficult for lenders to assess SME risk. Collateral is a further challenge: a lack of asset recognition and enforceability limits the opportunity for securing transactions. Steps have been taken here: the Lesotho Registry of Interest in Movable Assets (LERIMA) was launched in 2021, and the World Bank's CAFI project plans to launch a collateral registry, but lenders report usage challenges.

Box 1. Lesotho: Financial Access is a Key Job Creation Bottleneck (concluded)

Several government programs aim to support MSMEs and reduce risk – for example through direct grants, or through partial credit guarantee schemes (PCGs) – but grants are of low value, take up of PCGs is underwhelming, and fragmentation across the system hinders effectiveness.

On the other side of the market, firms are hesitant to use products from formal financial institutions. Financial literacy is a factor with many entrepreneurs unaware of the financial products available, unsure how to access them, or afraid to take on financial risks. Only 11 percent of businesses have a written business plan, and only 35 percent have a business budget (Finscope 2025). Only four in ten firms are aware of support organizations, such as the Basotho Enterprises Development Corporation (BEDCO), with even fewer utilizing services available. Lending terms are another barrier—33 percent of firms report “unfavorable rates, collateral, or procedures as main reason for not applying to loans” (B Ready Lesotho 2025). The lack of business insurance is similarly driven by perceived costs, and a lack of knowledge of how to obtain, or the types of insurance, available. These gaps in financial knowledge and capacity hinder MSMEs from engaging with formal financial institutions or scaling their operations.

The authorities have developed a comprehensive reform agenda to address the challenges, and recent developments are encouraging. Discussions with industry stakeholders in June 2025 highlighted some green shoots of financial deepening to MSMEs: the take up rate of the main partial credit guarantee scheme is increasing, and banks and NBFIs are experimenting with new MSME-focused lending products, such as operating loans based on signed government tenders. In addition, coordination across the key actors in the system (BEDCO, banks, MFIs, industry groups, development partners) appears to be improving. The authorities have put forward a comprehensive reform agenda in the National Financial Inclusion Strategy II (2024–28) and (forthcoming) Financial Sector Development Strategy II (2025–30). Key pillars include strengthening credit infrastructure (e.g., expanding credit bureau coverage to include MSMEs, integrating registries), enhancing public support instruments (e.g., reforming partial credit guarantee schemes, establishing a development finance institution), and promoting financial literacy through targeted education programs. The strategies also emphasize digitization, fintech regulation, and the development of inclusive financial products. Success will depend on sustained political commitment, effective institutional collaboration, and mobilization of resources from both public and private sectors.

D. Worker Level Barriers to Job Growth: Individuals Face Barriers Entering the Labor Market

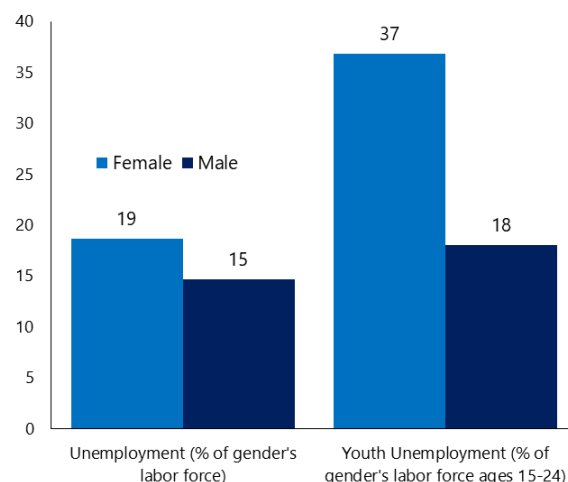
22. Without established employment experience, youths struggle to enter the labor market. The youth unemployment rate is 24.8 percent for 15–24 year olds versus 10.1 percent for sub-Saharan Africa (Figure 8). Furthermore, more than one in three youths are “neither in employment, education or training” (NEET) with the rate reaching over 40 percent for young women (ILOSTAT). Youths suffer from the experience paradox: the longer an individual is unemployed, the harder it can be to find employment as skills and networks atrophy (ILO 2024). And poor labor market outcomes early in a career are associated with poorer outcomes decades later. (ILO and ADB 2020, Kahn 2010). Youth in rural areas confront even steeper challenges: they have less access to job opportunities, and when employed they tend to have lower wages and are more likely to work in the informal sector. Generally, interventions linked to skills training and entrepreneurship are found to have a larger impact on youth labor market outcomes than employment services or subsidized employment (ILO 2025).

23. Women face additional barriers, experiencing disproportionately poor labor market outcomes. Across all age ranges, women face higher rates of unemployment than men. For example, 37 percent of young women are unemployed compared to 18 percent of their male counterparts (Figure 8). Labor force participation rates for women are lower (48.7 percent for women versus 67.7 percent for men in 2024), and the reliance on informal employment is higher (ILOSTAT). Lesotho has a high rate of female entrepreneurs relative to the sub-Saharan Africa average, but their businesses tend to be smaller, employ fewer people, operate in less-profitable sectors, and are subject to greater shocks (Cucagna and others 2025). The drivers of gender gaps align with many countries in sub-Saharan Africa, which include cultural, regulatory and legislative barriers (even with legislative progress, customary law differs), steeper domestic childcare responsibilities, early childbearing and maternal health challenges, and digital and financial access gaps (World Bank 2022; Kolovich and Newiak 2025). For example, maternal mortality was 478 deaths per 100,000 live births in 2020, significantly higher than the regional average, while 71 in every 1,000 girls aged 15–19 gave birth in 2023 (World Bank gender indicators). Women are far less likely to successfully access bank business loans; they are instead required to provide their husband’s name and income statements, and are less likely to be approved than men, particularly if unmarried (Robakowski-Van Stralen and Roberts 2024).

24. Skills mismatch is also a barrier to employment. Typically, unemployment rates around the world tend to fall for those with higher levels of education. However, in Lesotho, and sub-Saharan Africa more broadly, those with advanced levels of education have higher unemployment rates than those with intermediate levels of education (Figure 9). This paradox is evidence of potential skills mismatch—a disconnect between what is taught and what employers require (ILO 2019). For example, two-

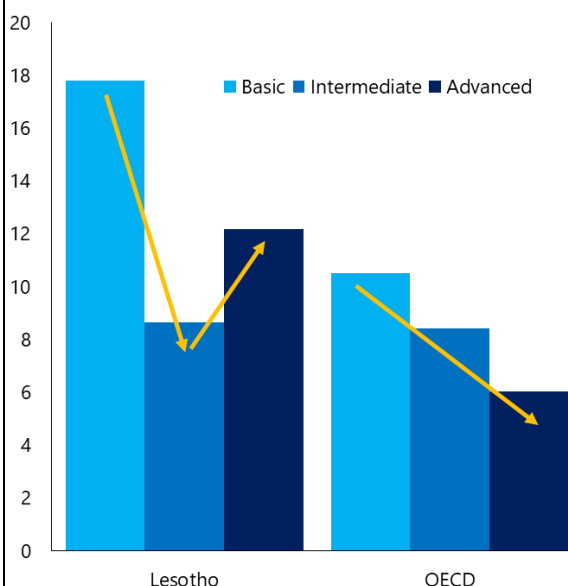
Figure 8. Lesotho: Unemployment by Age and Gender
(2023; Modeled ILO Estimate; Percent of Gender's Labor Force)

Women overall face higher unemployment than men, with female youth unemployment as high as 37 percent.



Source: World Bank World Development Indicators and IMF staff calculations

Figure 9. Lesotho: Skills Mismatch – Unemployment by Educational Attainment
(Latest Available Value; Percent of Total Labor by Educational Level)



Source: World Bank World Development Indicators and IMF staff calculations.

thirds of tertiary graduates studied social sciences and education, while most private and public investment is oriented towards agriculture, manufacturing, tourism, and technology (Rasagam and others 2023). The skills mismatch in Lesotho is exacerbated by a lack of robust labor market data; there is no detailed understanding of which sectors are growing or what skills are in demand. Governance around skills development is fragmented. The Ministry of Labor lacks influence over training programs, which are often run independently by the Prime Minister's office without coordination or clear feedback mechanisms. Career guidance is weak, and training centers are under-resourced. South Africa's model of inclusive governance in skills development offers a useful regional example (Franz and Dulvy 2020). However, the extremely high youth unemployment in South Africa demonstrates that addressing the labor supply issues alone is insufficient for jobs to flourish.

E. Policy Priorities to Spur Job Creation

25. A coordinated, concerted structural reform effort is needed to spur private sector led job creation. Broad-based structural reforms, sometimes called 'first generation reforms', are the priority. The most important set of these focus on unpicking the barriers to diversification and firm level growth. These should also be complemented by labor supply side policies that support job seekers and address skill mismatches. All of these will require a combination of learning from international best practice and tailoring to Lesotho specific circumstances. And it will require a long-term multi-year reform effort, placing an added premium on sustained political and social support. Measures to enhance effectiveness and build public trust include effective consultation and communication strategies to engage with stakeholders, explain trade-offs and discuss the importance of potential measures. Appropriate bundling, sequencing and pacing of reforms, with demonstrable upfront gains has been shown to improve chances of reform success (IMF 2024b, 2024c, 2025a).

26. The dominance of the public sector means that fiscal-structural reforms are essential for private sector success. The public sector will remain a key driver of economic activity but should switch roles: acting as an enabler of private sector development, rather than a substitute. Given the current role of large-scale construction and the growth benefits of effective infrastructure, improving public sector investment performance is a key issue. Capacity across the project management cycle must be built to improve capital budget execution, reduce delays, and generate stronger spillovers to the local construction economy. Public procurement should focus on efficiency and transparency, while the prevention of public sector arrears will improve direct links with private firms. Carefully addressing distortions from comparatively high public sector wages will address crowding out in the labor market.⁵ In addition, government efforts to spur private sector development could be better coordinated, and all programs should be subject to transparency and evaluation throughout their lifecycle.

27. Industrial policies should be approached with caution. Structural reforms, in particular policies that address growth barriers, are found to bring larger benefits to economic performance than industrial policies (IMF 2025b). Identified barriers, such as access to finance, electricity market failures, business environment weaknesses, and infrastructure deficits are the key bottlenecks to private sector development. Policymakers should be very cautious with 'picking winners' by directly supporting individual firms or sectors

⁵ Thevenot (2024) analyses the trade-offs and provides guidance on setting public sector wages.

without addressing these bottlenecks. Industrial policy methods can be fiscally costly or wasteful, prone to distortions, introduce governance challenges, and often do not solve the underlying market failures firms face. Industrial policies can also prove extremely difficult to unwind once they are no longer needed. In contrast, careful diagnosis of market failures with a targeted policy response is a more effective approach.

28. Public sector employment programs have a checkered history and must be approached with caution. The policies required to durably change the employment growth trajectory of Lesotho will take time to bear fruit. Given the acute needs now, the government is under pressure to provide a quicker solution. History shows that public employment programs often fail, primarily due to a lack of coordination, poor transparency and governance mechanisms, and insufficient exit pathways for employed individuals (ILO 2012, 2020). Therefore, if enacted as temporary social support, key principles for program design include having strong coordination mechanisms across agencies, ensuring employment is time limited with formal transition plans, embedding training and skills development throughout, and prioritizing transparency, and accountability. Additionally, designing evaluation from the start to build evidence and improve program performance is a key pillar. Most importantly, these programs are no substitute for the deep reforms required to spur durable, private sector led job creation.

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