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MALAWI

December 2019

SECOND AND THIRD REVIEWS UNDER THE THREE-YEAR EXTENDED CREDIT FACILITY ARRANGEMENT AND REQUESTS FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA AND AUGMENTATION OF ACCESS—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MALAWI

In the context of the Second and Third Reviews Under the Three-Year Extended Credit Facility Arrangement and Requests for Waivers of Nonobservance of Performance Criteria and Augmentation of Access, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on November 22, 2019, following discussions that ended on October 15, 2019, with the officials of Malawi on economic developments and policies underpinning the IMF arrangement under the Extended Credit Facility. Based on information available at the time of these discussions, the staff report was completed on November 7, 2019.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the International Development Association (IDA).
- A **Statement by the Executive Director** for Malawi.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Malawi*
Memorandum of Economic and Financial Policies by the authorities of Malawi*
Technical Memorandum of Understanding*
*Also included in Staff Report

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November 25, 2019

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IMF Executive Board Completes Second and Third Reviews and an Augmentation of Access under Malawi's ECF Arrangement and Approves US$43.3 Million Disbursement

On November 22, 2019, the Executive Board of the International Monetary Fund (IMF) completed the second and third reviews of Malawi's performance under its program supported by a three-year arrangement under the Extended Credit Facility (ECF). Completion of the reviews enables Malawi to draw the equivalent of SDR 31.55 million (about US$43.3 million), bringing total disbursements under the arrangement to SDR 53.85 million (about US $73.9 million).

In completing the reviews, the Executive Board also approved an augmentation of access under the ECF arrangement of SDR 27.76 million (about US$38.1 million or 20 percent of quota). The additional financing will help the authorities meet new balance of payments needs associated with reconstruction following Cyclone Idai. It will bring Malawi's total access under the current arrangement to SDR 105.835 million (about US$145.3 million) equivalent to 76.25 percent of Malawi's quota). The Executive Board also approved the authorities' request for waivers of nonobservance of the performance criteria on the primary fiscal balance at end-December 2018 and end-June 2019.

The three-year ECF arrangement was approved on April 30, 2018 for SDR 78.075 million (about US$107.7 million, equivalent of 56.25 percent of Malawi's quota in the IMF), to support the country's economic and financial reforms. The authorities remain committed to the policy priorities of the ECF arrangement which aim to entrench macroeconomic stability, preserve debt sustainability, and advance governance reforms while fostering higher, more inclusive, and resilient growth.

Following the Executive Board discussion on Malawi, the First Deputy Managing Director Mr. David Lipton, and Acting Chair, stated:

"Despite large reconstruction and balance of payments needs following Cyclone Idai Malawi's program performance has been satisfactory. Program-supported structural reforms advanced, addressing several important gaps that had previously been identified in public financial management. All quantitative performance criteria were met except those on the primary balance, which were missed largely due to faster than envisaged implementation of rural electrification and development projects, unexpected spending for disaster relief and to ensure safety during elections and post-election protests.

“The authorities aim to further entrench macroeconomic stability and preserve debt sustainability to support higher, more inclusive, and resilient growth. Fiscal policy will focus on improving revenue outcomes and spending management to strengthen the fiscal path while allowing for spending for post-cyclone reconstruction needs and to strengthen Malawi’s resilience to climate change. Monetary policy will continue to target inflation. Maintaining exchange rate flexibility and efforts to further strengthen financial sector resilience will be important for buffering shocks and supporting broad-based private sector development.

“Further implementation of structural reforms and measures to improve governance and transparency are needed to strengthen economic outcomes. To this end, enhancing public financial management—through strong cash management, commitment controls, routine bank reconciliations, and transparency in the budget process—investment spending efficiency, monitoring of state-owned enterprises, and debt management will be critical. In the financial sector, sustainably increasing access to finance will require addressing structural barriers, such as challenges with the collateral registry, mobile banking, and property rights.

“The medium-term economic outlook is favorable. Low per capita economic growth and its resilience to weather shocks is expected to gradually improve with enhanced electricity generation and irrigation, as well as crop diversification.”

INTERNATIONAL MONETARY FUND

MALAWI

November 7, 2019

SECOND AND THIRD REVIEWS UNDER THE THREE-YEAR EXTENDED CREDIT FACILITY ARRANGEMENT AND REQUESTS FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA AND AUGMENTATION OF ACCESS

KEY ISSUES

Context. Economic growth is recovering after last year's drought and insect infestations—despite the impact of Tropical Cyclone Idai in the south and political protests following the May 2019 presidential election. The authorities are requesting an augmentation of access under the Extended Credit Facility (ECF) of 20 percent of quota (SDR 27.76 million) to finance significant reconstruction imports.

Program performance. All quantitative performance criteria (QPC) for end-December 2018 and end-June 2019, were met except on the primary fiscal balance which was missed by 1.5 and 2.5 percent of GDP due to revenue shortfalls and expenditure overruns—despite a consolidation of 2 percent of GDP during FY 2018/19. Indicative targets (ITs) on domestic arrears and social spending were met. Based on corrective measures, the authorities request waivers of non-observance. Most structural benchmarks were completed (some with delay).

Program strategy. The authorities aim to entrench macroeconomic stability, preserve debt sustainability, and advance governance reforms while attaining higher, more inclusive, and resilient growth. Essential reconstruction and security spending will be accommodated by reprioritizing spending and a modest relaxation in the FY 2019/20 domestic primary balance target (relative to the first review under the ECF arrangement). Governance reforms focus on enhancing public financial management, investment spending efficiency, and monitoring of state-owned enterprises. Monetary policy remains targeted on containing inflation and exchange rate flexibility will buffer shocks and preserve competitiveness. Financial sector resilience continues to be strengthened.

Staff views. Staff supports the authorities' request for completion of the second and third reviews under the ECF arrangement, waivers of non-observance for the missed QPCs—given the authorities' commitment to corrective measures—and the request for augmentation of access. This would result in a disbursement of SDR 31.55 million and help catalyze donor support.

Approved By
David Robinson (AFR) and S. Ali Abbas (SPR)

Discussions on the second and third reviews under the ECF arrangement and request for augmentation of access were held on September 10-18, 2019 in Lilongwe and Blantyre. The staff team comprised Ms. Mitra (head), Ms. Farahbaksh, Ms. Gwenhamo, Ms. Yoon (all AFR), Mr. Lee (SPR), Mr. Swistak (FAD), Mr. Banda (local economist), and Mr. Anderson (FAD long-term expert). Mr. Robinson (AFR) and Mr. Sitima-wina (OED) joined in key discussions. Mr. Hettinger (World Bank) joined the technical meetings. Ms. Ourigou assisted in the preparation of the staff report. The mission held discussions with Hon. Joseph Mwanamvekha, Minister of Finance; Dr. Dalitso Kabambe, Governor of the Reserve Bank of Malawi; and other senior officials. The mission also met representatives of the private sector, civil society, and development partners and held a press conference.

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CONTEXT

1. **In May 2019, the incumbent President Peter Mutharika and his party were re-elected for a second term, forming a minority government.** The main opposition parties are contesting the presidential election results in court and demanding the Electoral Commission Chair resign. Protests have resulted in considerable property damage and economic disruption. Development challenges have been compounded by chronic electricity shortages, high youth unemployment, and alleged corruption.

2. **Tropical Cyclone Idai had significant humanitarian tolls and infrastructure costs requiring reconstruction**. The cyclone struck southern Malawi in March and resulted in severe flooding affecting over a million people—taking over 60 lives, ruining crops, and destroying homes, hospitals, schools, and other critical infrastructure. Recovery and reconstruction (projected to cost $370 million or 5 percent of GDP) would build resilience for Malawi, which is globally amongst the countries most vulnerable to climate change (Box 1).[1]

3. **The new government expressed its commitment to the policy priorities in the ECF and have requested an augmentation in access under the ECF to finance imports for post-cyclone reconstruction**. The second review was not completed in Spring 2019 as, prior to the elections, agreement could not be reached on measures to bring the FY 2018/19 position back on track by end-June, the end of the fiscal year. The agreed FY 2019/20 program corrects for the slippage in FY 2018/19 while prioritizing security spending and post-cyclone rehabilitation and reconstruction. During 2019H2 and 2020, the reconstruction will involve about $204 million (3 percent of GDP) in imports of goods and services, resulting in a balance of payments financing gap of $125 million (1.6 percent of GDP)—net of policy adjustments of about $80 million (1 percent of GDP) reflecting reprioritization of fiscal spending and use of foreign currency reserves buffers. The proposed $40 million augmentation would help fill this financing gap and would complement $15 million of donor support and $120 million of World Bank support ($50 million of which will replace previously planned near-term projects) over 2019-20. Securing further donor financing to enable more rapid progress towards the SDGs will require accelerating reforms in agriculture, public financial management, and procurement.

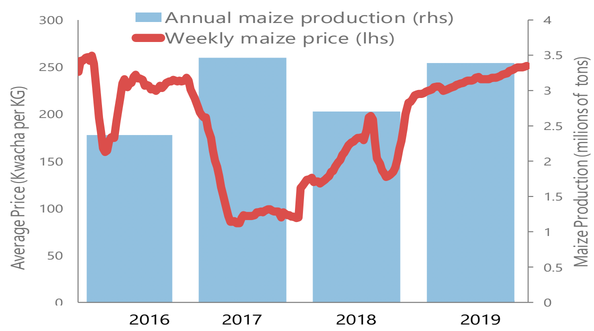
RECENT DEVELOPMENTS

4. **Economic growth is strengthening despite the impact of Cyclone Idai**—rising from 3.2 percent in 2018 to 4.5 percent in 2019—driven by reconstruction, increased electricity generation and an agricultural rebound. Cyclone-related agricultural losses were more than compensated by bumper harvests in the rest of the country, resulting in significantly larger agricultural production following last year's widespread drought and insect infestations (Text Figure 1). However, delays in imports transiting through cyclone-damaged parts of Mozambique

[1] Post-Disaster Needs Assessment published by the Government of Malawi with financial and technical support from the World Bank, Global Facility for Disaster Reduction and Recovery, and the United Nations.

and Malawi, pre-election uncertainties, and disruptions from post-election protests weigh on manufacturing and wholesale and retail trade. Inflation is anticipated to average 9.1 percent this year, reflecting elevated food prices due to cyclone-related supply chain disruptions and hoarding by suppliers, while non-food inflation remains on a downward trend (Text Figure 2).

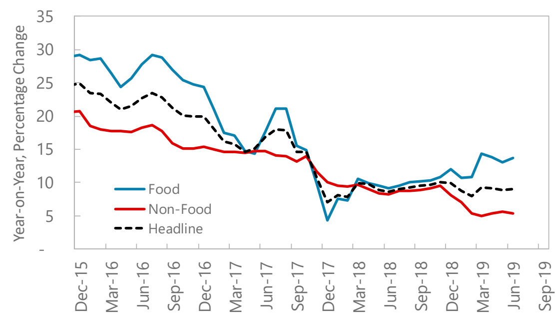
Text Figure 1. Malawi: Maize Production and Prices



Sources: Malawian authorities; IMF staff estimates.

Text Figure 2. Malawi: Inflation

(Year-on-year percentage changes)



Sources: Malawian authorities; IMF staff estimates.

5. **The fiscal position improved in FY 2018/19 (relative to FY 2017/18) but not as much as programmed under the ECF arrangement** (Text Table 1). The primary deficit was reined in by 2 percent of GDP relative to last year but exceeded the program target (adjusted for deviations in grants and debt service payments relative to the first review under the ECF arrangement) by 2.5 percent of GDP. The authorities indicated that income tax revenues were hurt in the last quarter of the fiscal year due to reduced activity in manufacturing and services following the post-cyclone disruption in imports and business closures during protests (income tax revenues did not benefit from the agricultural rebound). Non-tax revenues underperformed due to lower than anticipated dividends from the Reserve Bank of Malawi (RBM) and state-owned enterprises (SOEs). Rural

Text Table 1. Malawi: Central Government Operations

(FY 2017/18-2018/19, percent of GDP)[1]

	FY 2017/18	FY 2018/19		
	Est.	1st Rev.	Proj.	Change
Revenue	**21.1**	**22.6**	**21.2**	**-1.4**
Tax	17.4	18.1	17.4	-0.7
Non-tax revenue	2.2	2.2	1.7	-0.4
Grants	1.5	2.3	2.0	-0.3
o/w Project	1.5	2.3	1.5	-0.9
Spending	**28.9**	**26.5**	**27.8**	**1.3**
Wages	6.6	7.4	7.2	-0.1
Goods & Services	6.8	5.8	6.6	0.8
Generic	2.7	2.3	2.5	0.2
o/w Disaster relief	0.0	0.0	0.1	0.1
Elections	0.6	1.0	1.2	0.2
o/w Unanticipated security	0.0	0.0	0.5	0.5
Social spending and road maintenance	2.1	1.8	1.9	0.0
Rural electrification	0.5	0.3	0.7	0.5
Other	0.9	0.4	0.4	0.0
Transfers	5.1	4.1	4.2	0.1
Pensions	1.6	1.5	1.6	0.0
Universities, SOEs	2.2	1.2	1.4	0.1
FSIP	0.7	0.8	0.7	-0.1
Other	0.5	0.5	0.5	0.0
Interest	4.0	3.9	4.2	0.3
Other	1.6	0.1	0.1	0.0
Development spending	4.8	5.1	5.3	0.2
Foreign financed	3.1	3.7	3.1	-0.6
Domestically financed	1.6	1.4	2.2	0.8
Net Lending	0.1	0.2	0.1	0.0
Discrepancy	-0.4	0.0	0.1	0.1
Overall Balance	-8.3	-3.9	-6.5	-2.6
Primary Balance	**-4.3**	**0.0**	**-2.3**	**-2.3**
Adjusted Primary Balance	-4.3	0.1	-2.3	-2.5
Domestic Primary Balance	-2.6	1.4	-1.2	-2.6

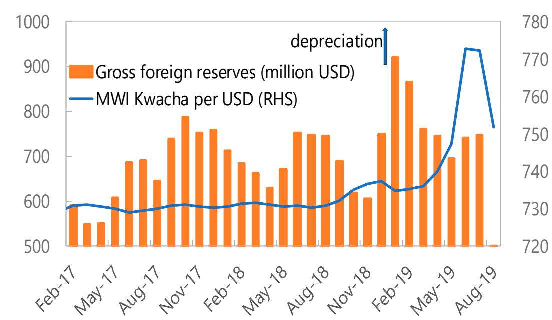
[1]The program target for FY 2018/19 was the overall primary balance.

Sources: Malawian authorities; IMF staff estimates.

electrification and domestically-financed development projects planned for FY 2019/20 were implemented faster than envisaged. The remaining spending overruns mainly reflect cyclone disaster relief, spending to ensure safety during elections and post-election protests, and transfers to universities to raise salaries following staff strikes. Foreign-financed development spending was lower than programmed due to shortfalls in grants that were only partially offset by increased project-based concessional foreign borrowing. The deficit was largely financed domestically, without any net financing from the RBM.

6. **The cyclone increased current account pressures in 2019H2 due to a sharp rise in imports for reconstruction.** Offsetting factors in the first half of the year including disruptions from the cyclone and policy uncertainty ahead of elections slowed import growth for the full year. Exports remained broadly stable with strengthening exports of cotton, edible nuts, and sugar compensating for reduced tobacco exports (reflecting lower global demand). Consequently, the current account deficit is expected to improve from 20.6 percent of GDP in 2018 to 18.4 percent of GDP in 2019.[2] Given continued large reconstruction imports in 2020, international reserves coverage in months of prospective imports is expected to remain around 2.9 by end-2019.

Text Figure 3. Malawi: Gross Reserves and Nominal Exchange Rate



Sources: Malawian authorities; IMF staff estimates.

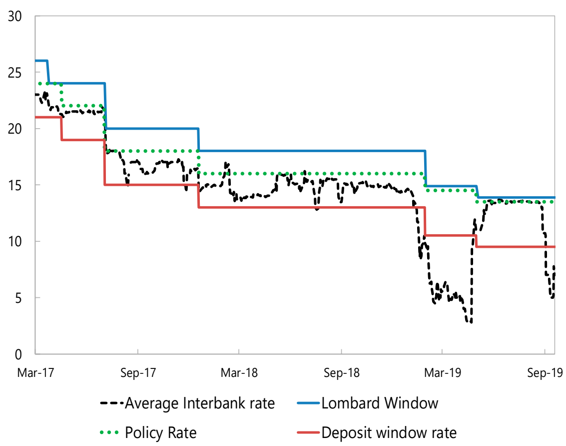
7. **For the first time in two years, the Kwacha fluctuated substantially against the US dollar** (Text Figure 3). A 6 percent depreciation in 2019H1—the largest since mid-2016—was followed by a 5 percent appreciation in 2019Q3. Nevertheless, the real effective exchange rate appreciated about 13 percent over the past twelve months (August 2018-August 2019) due to large headline inflation differentials with trading partners (non-food inflation differentials are smaller).

8. **In 2019H1, the RBM loosened monetary policy in line with reduced inflationary pressures**. Following a trend decline in non-food inflation, reduced international fuel prices, and declines in average Treasury bill yields (for all tenors), the policy rate was reduced by 150 basis points (bps) in January and another 100 bps in May to 13.5 percent. The rate has remained unchanged in 2019H2. Reserve requirements were also reduced by 250 and

[2] Fund staff has adopted the Malawi National Statistics Office's (NSO) trade data based on its improved reliability. Previously, the IMF's reported series was based on staff estimates. Consequently, the IMF's reported current account deficit widened for 2017 from 11.1 to 25.6 percent of GDP (reflecting export shares revised downward by 10.6 percent of GDP and import shares revised upward by 3.8 percent of GDP); and for 2018 from 9.3 to 20.6 percent of GDP (reflecting export shares revised downward by 11.5 percent of GDP and services and shares of imports and unrequited transfers revised upward by 4.0 and 4.2 percent of GDP). Errors and omissions were adjusted by offsetting amounts, leaving the overall balance unchanged. Future TA missions on capital and financial accounts' statistics will seek to better identify the offsetting flows to the current account adjustment.

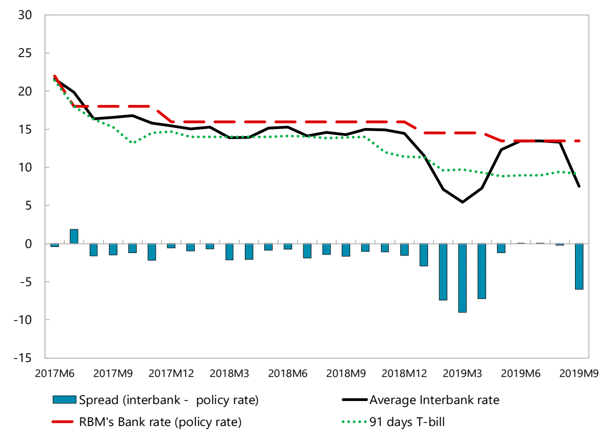
375 bps to 5 and 3.75 percent on local and foreign currency deposits, respectively, and the Lombard rate by 310 bps to 14.9 percent (all in January). The additional liquidity from these policy changes as well as weak demand for repurchase agreements (reflecting their low rates) used by the RBM to mop up liquidity have resulted in greater interbank rate volatility—the rate was below the interest rate corridor for extended periods twice this year (Figures 4 and 5, MEFP ¶4). Credit growth rose from 11.5 percent at end-2018 to 18.8 percent in August 2019.

Text Figure 4. Malawi: Interest Rate Corridor
(Percent, Jan.2017–Jul.2019)



Sources: Malawian authorities; IMF staff estimates.

Text Figure 5. Malawi: Policy, Interbank and Treasury Bill Interest Rates
(Percent, Mar.2017–Jun.2019)



9. The banking system remains well capitalized, liquid, and profitable. Non-performing loans declined by 1.3 percentage points since end-2018 to 4.8 percent at end-June 2019, while provisioning increased to 55 percent of total loans. The RBM's June 2019 stress test showed that overall the banking system is resilient to interest rate and income risk shocks but vulnerable to some credit and liquidity risk shocks. One small loss-making bank was recapitalized and another is looking for a partner to inject capital and may otherwise exit the market. The cyclone had little impact on banks.

MACROECONOMIC OUTLOOK AND RISKS

10. Growth is expected to accelerate. Manufacturing and wholesale trade are anticipated to be boosted by new electricity sources coming on line from 2020 (more than offsetting any adverse effects from fiscal consolidation), while post-cyclone reconstruction will also provide an impetus to growth. Growth is projected to reach 5 percent in 2020, rising to 6.5 percent over the medium-term, with greater access to finance and more resilient infrastructure—including enhanced electricity generation and irrigation (e.g., the Shire Valley project), crop diversification, and better road networks.

11. Inflation is anticipated to continue moderating while the current account gradually improves. Inflation is projected to decline to 8.7 percent in 2020 and converge towards 5 percent over the medium-term, benefitting from improved agricultural resilience gradually lowering food prices, lower international fuel prices, and strengthened fiscal and monetary policy implementation. The current account deficit will narrow to about 15 percent of GDP but only gradually as sizeable infrastructure-related imports will partly offset the impact of lower fuel import prices and steady growth of non-traditional exports. International reserves are expected to rise just above 4 months of prospective imports supported by strengthened competitiveness, export diversification, and fiscal restraint.

12. Risks are tilted to the downside. Legislation introducing interest rate caps was rejected in March 2019 by the previous Parliament but remains a much-discussed populist measure. The new minority government will need to build consensus to advance reforms. If protests continue into next year, urban economic activity could substantially decline. If growth fails to accelerate, then with Malawi's growing population, job creation would be insufficient to absorb new entrants into the labor market resulting in higher rates of unemployment. Adverse weather conditions—intensified by climate change—and infestations could hurt growth, raise inflation, and increase balance of payments pressures. Escalated global trade tensions could depress export demand and raise import costs (Annex I: Risk Assessment Matrix). On the upside, accelerated reform implementation could boost investor and donor confidence, potentially unlocking external financing, including additional concessional funding.

PERFORMANCE UNDER THE PROGRAM

13. All but one quantitative performance criteria (QPC) were met at end-December 2018 and end-June 2019 (Table 10). The primary balance target (adjusted for deviations in grants, and debt service payments relative to the first review under the ECF arrangement) was missed by
1.5 percent of GDP in December due to front-loading of planned spending for the year and 2.5 percent of GDP in June due to revenue shortfalls and expenditure overruns. The indicative targets (ITs) on new domestic arrears and on social spending were met for both end-December and end-June.

14. Program-supported reforms advanced, addressing several important gaps that had been previously identified in public financial management (Table 11a).

- The end-December 2018 structural benchmarks (SBs) on commitment control and cash management were met and those covering the publication of five reports by Ministries, Departments, and Agencies (MDAs), debt, and bank account reconciliation were completed by end-March 2019. Regulations, policies, and guidelines for SOE oversight are complete except cabinet approval of the dividend policy (new SB for end-December 2020).

- The end-June 2019 SBs on publication of five reports by MDAs, commitment control, and expansion of accounts covered by IFMIS were met. The SBs covering quarterly consolidated financial reports, debt, bank account reconciliation, and the pilot audit of SOEs were completed by mid-September. The ex-post performance audits of two (out of three) capital projects was completed on time; completion of the remaining audit—delayed by accounting system issues—is expected by June 2020. The SBs on budget release and expanding budget coverage of IFMIS will be completed by end-2020 as they required approval of the FY 2019/20 budget, which took place in October. The end-September 2019 SB on the RBM's strategy for unwinding its holding of government securities was met.

- The end-December 2019 SB on the audit of the public sector investment program (PSIP) database was completed in June 2019. This will be an important step towards improving project management and more accurate projections of project-based donor support.

15. Corrective measures have been agreed for the missed QPCs and the authorities request waivers of nonobservance on this basis. Spending has been reduced relative to the FY 2018/19 outcome, returning to levels envisaged during the first review under the ECF arrangement and consistent with maintaining critical growth-enhancing spending. Despite corrective measures, the domestic primary balance falls short by 0.4 percent of GDP of what was targeted during the first review under the ECF arrangement in order to accommodate spending on post-cyclone reconstruction and security to ensure public safety (¶18).

POLICY DISCUSSIONS

Policies are anchored on preserving debt sustainability, entrenching macroeconomic stability, and advancing governance reforms in support of attaining higher, more inclusive, and resilient growth. Improving revenue outcomes and spending management—especially investment spending efficiency and monitoring of SOEs to contain fiscal risks—will be critical for strengthening the fiscal path, against the backdrop of large post-cyclone reconstruction needs and the urgency to raise resilience to climate change. Tight monetary policy will contain inflation. Greater exchange rate flexibility and strengthening financial sector resilience will help buffer shocks and support broad-based private sector development. Governance reforms continue to gain momentum—including in public financial management and debt management—and are expected to gradually catalyze donor support.

A. Preserving Debt Sustainability

16. Malawi is at moderate risk of external debt distress and high overall risk of debt distress. The Low-Income Country Debt Sustainability Framework (LIC DSF), carried out jointly by the staffs of the IMF and the World Bank (Annex II: Debt Sustainability Analysis) indicate that:

- All baseline external debt indicators are below their policy-dependent debt burden thresholds. Stress tests highlight vulnerabilities to export shocks given the country's narrow export base and heavy reliance on rain-fed agriculture.

- The baseline present value (PV) of the public debt-to-GDP ratio remains above the benchmark until 2027—a consequence of high interest rates on domestic debt accumulated during 2014–17 (when inflation ranged between 20-30 percent) and of primary deficits averaging 2.5 percent of GDP over the past four years (partly due to natural disasters). Stress tests underline continued vulnerability to climate change shocks.

17. Staff and the authorities agreed on the need for firm actions to prevent future fiscal slippages and reduce debt vulnerabilities. Public debt will be reduced from 62 to 44 percent of GDP by 2027—corresponding to the PV of public debt falling below the LIC DSF threshold for a country with weak debt carrying capacity. To this end, a domestic primary surplus of 2 percent of GDP will be targeted during FY 2020/21-24/25, reinforced by a revenue mobilization strategy, continued improvements in budget planning and management, procurement, public investment management, oversight of SOEs, and debt management (¶20, 25). The program limit of no non-concessional external borrowing will continue.

B. Sustaining Macroeconomic Stability

Fiscal Policy

18. To preserve debt sustainability, the authorities are committed to fiscal adjustment in FY 2019/20 while prioritizing post-cyclone reconstruction and public safety (MEFP ¶17). A tightening of the domestic primary balance (by 2.1 percentage points relative to FY 2018/19) to target a surplus of 0.9 percent of GDP balances these competing objectives (Text Table 2). This represents a 0.4 percentage point of GDP loosening relative to the first review under the ECF arrangement. Domestic revenue is lower by 0.2 percent of GDP and spending is higher by 0.2 percent of GDP; the latter reflects post cyclone rehabilitation and reconstruction and additional security spending of 2.3 percent of GDP offset by 2.1 percent of GDP in spending cuts (0.5 percent of GDP from goods and services and 1.6 percent of GDP from domestically-financed capital spending). The resulting expenditure envelope will be in line with the spending levels of recent years (except FY 2018/19) and consistent with maintaining critical growth-enhancing spending. Spending commitments will be carefully monitored (MEFP ¶23) and undertaken as revenues materialize in order to avoid fiscal slippages. Key measures include:

- Revenues are anticipated to be 1.6 percent of GDP lower than at the time of the first review under the ECF due to lower grant projections (1.4 percent of GDP) and slightly lower tax and non-tax revenue projections (0.2 percent of GDP).
    - Post-election political uncertainty is expected to continue weighing on revenues. Nevertheless, tax measures in the approved FY 2019/20 budget, which have already come into effect, will help contain revenue shortfalls. These include new environmental taxes (a vehicle tax and excises on plastic products), an import surcharge on select goods (e.g., alcohol, cigarettes), and increased withholding taxes—most of which are progressive and, as

experienced with past revenue measures, are expected to have limited impact on economic growth.[3] Increased imports will widen the tax base.

- User fees and charges are being adjusted upwards and their enforcement stepped up; and road tolling fees are being introduced. Implementation of the revised dividend policy will enforce SOE dividend payments.

- World Bank budget support for post-cyclone reconstruction of 0.6 percent of GDP ($40 million) was disbursed at end-FY 2018/19 and will be spent in FY 2019/20.

- Expenditures are anticipated to be 0.5 percent of GDP higher than at the time of the first review under the ECF due to higher projections of interest spending (0.2 percent of GDP) and slightly higher projections of spending on goods and services and subsidies and transfers (0.3 percent of GDP).

  - Wage and pension increases will be contained to inflation; and new hiring will be limited to essential staff.

  - Goods and services spending is 0.2 percent of GDP higher than in the first review under the ECF arrangement, reflecting increased spending for post-cyclone rehabilitation support (0.2 percent of GDP) and ensuring public safety (0.5 percent of GDP) partially offset by reductions in generic goods and services (0.4 percent of GDP) and maize purchases (given overstocking; 0.1 percent of GDP). The reduction in goods and services spending relative to FY 2018/19 is expected to have limited impact on the economy since the savings is primarily from a reduction in imports of equipment to safely hold elections.

  - To support post-cyclone reconstruction domestically-financed capital spending will be reoriented towards resilient reconstruction (1.5 percent of GDP) with an equivalent cut in previously planned projects—of which 0.8 percent of GDP in projects were already executed in FY 2018/19 and 0.7 percent of GDP in projects will either be delayed or cut. Further increases in capital spending are constrained by implementation capacity. Better targeting of the iron sheet subsidy will cut costs by 0.1 percent of GDP.

  - The risk of food insecurity is being addressed through reforms in the Farm Input Subsidy Program (FISP) spending and ADMARC's strategic grain reserves (which has no impact on the budget). Better targeting of FISP is expected to reduce costs by 0.1 percent of GDP this year.

[3] Revenue reducing measures in the budget (e.g., increased income tax exemptions) will be offset by broadening the non-import tax base.

Text Table 2. Malawi: Central Government Operations
(FY 2018/19-2019/20, Percent of GDP)[1]

	FY2018/19			FY 2019/20		
	1st Rev.	Proj.	Change	1st Rev.	Proj.	Change
Revenue	22.6	21.2	-1.4	23.5	22.0	-1.6
Tax	18.1	17.4	-0.7	18.1	18.0	-0.1
Non-tax revenue	2.2	1.7	-0.4	2.0	1.8	-0.1
Budget support	0.0	0.6	0.6	1.0	0.0	-1.0
Project grants	2.3	1.5	-0.9	2.5	2.2	-0.4
Spending	26.5	27.8	1.3	26.3	26.8	0.5
Wages	7.4	7.2	-0.1	7.4	7.3	0.0
Goods & services	5.8	6.6	0.8	5.1	5.2	0.2
Generic	2.3	2.5	0.2	2.4	2.7	0.3
Social and road maintenance spending	1.8	1.9	0.0	2.1	2.0	-0.1
Other[2]	1.7	2.3	0.6	0.6	0.6	0.0
Subsidies and transfers	4.1	4.2	0.1	4.0	4.1	0.1
Interest	3.9	4.2	0.3	3.8	4.1	0.2
Development spending						
Foreign financed	3.7	3.1	-0.6	3.7	3.9	0.1
Domestically financed	1.4	2.2	0.8	2.0	1.9	-0.1
Other	0.2	0.2	0.0	0.2	0.2	0.0
Overall balance	-3.9	-6.5	-2.6	-2.7	-4.9	-2.1
Domestic Primary Balance	1.4	-1.2	-2.6	1.3	0.9	-0.4

[1] The program target in FY 2019/20 is the domestic primary balance. In previous years, the program target was the overall primary balance.

[2] In FY 2018/19, other goods and services spending includes 1.2 percent of GDP in spending to hold elections and rural electrification spending that is 0.4 percent of GDP higher than past outcomes.

Sources: Malawian authorities; IMF staff estimates.

19. **Over the near and medium-terms, raising revenues, reorienting spending and increasing its efficiency, as well as containing fiscal risks will be critical to reducing debt vulnerabilities and supporting disinflation and higher, more inclusive, and resilient growth.**

- To expand space for growth-enhancing spending and building resilience to climate change, a comprehensive review of the tax system will be undertaken and a domestic revenue mobilization strategy put in place and incorporated into the FY 2020/21 budget (MEFP ¶20). The resulting measures (including reduction of VAT exemptions and increased use of excise taxation) are projected to yield at least 0.3 percent of GDP in FY 2020/21 and 0.2 percent of GDP in following years. Tax revenues will be further enhanced with risk-based audits, improved tax compliance, and rollout of the Integrated Tax Administration System (ITAS); and non-tax revenues improved by moving fees and charges towards marginal cost pricing, enlarging the coverage of road tolls, and increasing digitalization. Tax revenue collections will be closely monitored and any gaps in administration will be immediately addressed. All of these measures will also promote a better business environment through strengthened transparency and reduced corruption.

- The composition of spending will be shifted toward growth-enhancing areas and ensuring adequate social safety nets (MEFP ¶21). The authorities plan to review FISP eligibility and voucher value aiming to halve the cost over the medium-term. Public sector employment reforms are also planned. Transfers to public entities will be reduced by bolstering their revenue generating capacity and management. Enhancement of public investment management will support spending efficiency (MEFP ¶19). To this end, the authorities agreed to begin implementing the findings of the recent PSIP audit (especially project rationalization), strengthen PSIP linkages to the budgeting and budget execution processes, and continue building capacity.

- Fiscal risks will be contained through improved SOE oversight (MEFP ¶18)—including submission to Parliament and publication of a consolidated annual report on SOEs and developing a prototype SOE database—and continuing rigorous implementation of the automatic fuel pricing mechanism.

Monetary, Exchange Rate, and Financial Sector Policies

20. Monetary policy will continue to focus on containing inflation. With non-food inflation on a downward path and running just above 5 percent, at the lower end of the RBM's target, policy rate reductions during 2019H1 appear appropriate. Amid rising food prices, staff and the authorities agreed that the monetary policy stance should be calibrated to keep inflation in single digits. The authorities continue to expand capacity in developing high frequency data, liquidity forecasting, and the forecasting and policy analysis system (FPAS) modeling to support eventual transition toward inflation targeting.

21. Recent changes to the monetary policy framework should be reviewed. In September, the RBM shifted the reference rate (the basis for banks' lending rates) from the Lombard rate to a weighted average of the Lombard rate, the interbank rate, Treasury bill rates, and the savings
rate—with a view to improving financial intermediation and, ultimately, access to finance. Staff stressed this new reference rate formula is less transparent than using the policy rate and could raise banks' intermediation costs as it is less predictable. Instead, the RBM should continue addressing structural barriers to reducing the cost of borrowing, including with a road map to improve access to finance. The RBM agreed to consult with the Fund, by end-2020, and review this policy as well as examine whether the foreign currency reserve requirement rate should be raised and unified with the local currency rate (MEFP ¶10). Staff urged the RBM to raise repurchase agreement rates in order to more effectively mop up liquidity and keep the interbank rate aligned with the policy rate.

22. Exchange rate flexibility will help cushion shocks and preserve competitiveness. The authorities reiterated their commitment to a flexible exchange rate regime—noting the recent fluctuations in the Kwacha against the U.S. dollar—and stressed that their intervention in the FX market is solely for accumulating reserves and smoothing excess volatility. Staff noted the importance of deepening the interbank FX market as pricing is currently determined in a segmented and underdeveloped interbank FX market while most transactions occur in the retail market and directly with the RBM—neither of which contribute to interbank market price formation.[4] As a first step, the RBM will prepare a report on obstacles to FX market development (MEFP ¶15).

23. The authorities are committed to strengthening banking resilience and financial sector oversight (MEFP ¶10,12-14). All banks are fully compliant with the IFRS9 standards. Regulations to enhance the Domestic Systemically Important Banks supervision took effect in June 2019 and amendments to the Banking Act of 2010 and Financial Services Act of 2010—aligning the legal framework for bank resolution closer to international best practices—as well as a consumer protection bill will be submitted to Parliament by end-2020. Staff recommended continued vigilance given recent credit growth. The RBM is encouraging banks to improve their loan recovery and analysis of collateral quality, including enhancing the collateral registry. A new reporting template for credit bureaus has improved the quality of reporting to banks. Increased foreign currency lending (which tripled to 23 percent over the past decade) is being closely monitored.

C. Advancing Governance Reforms

24. Strengthening governance and reducing corruption vulnerabilities remain critical to improving economic outcomes and bolstering confidence. Progress in key areas include:

- **Important steps have been taken to enhance the RBM's independence and deepen the domestic debt market (MEFP ¶10, 11)**. In December 2018, Parliament approved a new RBM Act, which prohibits monetary financing of the government (except for short-term advances that have to be repaid in cash). To safeguard the RBM's independence, it was agreed that no more conversions of ways and means cash advances into government securities will take place. Between end-2017 and end-June 2019, the RBM's holdings of government securities declined by 12 percent. In particular, its share of the total stock of Treasury bills declined from 2.6 to 0.1 percent and of Treasury notes from 76 to 39 percent. These efforts are supported by increased engagement of the Ministry of Finance (MoF) debt management unit in domestic debt management policies and operations in collaboration with the RBM; and routine publication of an issuance calendar indicating the volume of securities to be offered in each auction. Staff and the authorities agreed on the importance of developing a strategy for building reliable benchmarks in the Treasury bill market. A comprehensive Medium-Term Debt Management Strategy for 2018-22 has been developed.

[4] Box 1, IMF Country Report 18/336.

- **Public Financial Management (PFM) reforms are beginning to improve fiscal discipline, transparency, and integrity but risks remain (MEFP ¶23-27).** These reforms focus on cash management, routine fiscal reporting and bank reconciliation, reconciliation of debt data between the MoF and the RBM, strengthening the quality control of fiscal reporting, improving the medium-term budgetary framework, and further broadening current IFMIS coverage. The authorities have ambitious plans for implementing a new IFMIS from July 2020. Staff cautioned against proceeding too quickly, which could create governance challenges stemming from implementation slippage and simultaneous introduction of new practices and technologies. Mitigating measures could include change management, training, phased implementation, credible quality assurance, and a transparent governance framework.

PROGRAM MODALITIES AND SAFEGUARDS

25. The authorities are requesting an augmentation of access under the ECF to meet new balance of payments needs associated with post-cyclone reconstruction. The augmentation of SDR 27.76 million (20 percent of quota, provided in three equal tranches) would bring total access under the program to SDR 105.835 million (76.25 percent of quota, Table 7).

26. Malawi's capacity to repay the Fund remains strong (Table 8). Financing assurances are in place for the remainder of the program with external financing requirements mainly met through project loans from multilateral and bilateral donors. Malawi has a strong track record in meeting its obligations to the Fund in a timely manner.

27. Modifications to the program and monitoring. The domestic primary balance replaces the existing primary balance QPC to reduce the effect of uncertainties in predicting external grants and loans on the measurement of fiscal performance. The domestic primary balance will be calculated by subtracting current expenditures (except interest), domestically-financed development expenditures, and net lending from domestic revenues. A new IT on net foreign borrowing (based on net disbursements of concessional external debt) by the central government has been introduced. New SBs for the fourth and fifth reviews are proposed on cabinet approval of an SOE dividend policy, developing a domestic revenue mobilization strategy, adoption of electronic funds transfers and implementation of treasury management systems, and a report on obstacles to foreign exchange market development. The program will continue to be reviewed semi-annually based on performance criteria, indicative targets (Table 10), and structural benchmarks (Table 11b). Targeted technical assistance remains critical to achieving program objectives.

28. Implementation of recommendations from the July 2018 updated safeguards assessment has been slower than the timeline envisaged in the assessment. The assessment recommended legal amendments to strengthen the RBM's governance and autonomy which were enacted in 2019 and will be further enhanced with the elimination of the conversion of cash advances into securities, as well as, following legal review, legislation needed to eliminate any ambiguity in this regard (¶24). Limited progress has been made in addressing concerns over the RBM's reserve management practices though the authorities have informed staff that steps are being initiated with support from the World Bank. A recent lapse in the RBM's banking for the government suggests a deterioration in controls which the RBM is taking steps to address. An emergency liquidity assistance (ELA) framework is being developed. Staff is continuing to engage with the authorities on these issues.

STAFF APPRAISAL

29. Malawi's macroeconomic outlook is positive but vulnerable to climate change shocks. This year, solid growth prevailed because Cyclone Idai only affected southern Malawi and harvests were bountiful in the rest of the country. In recent years, this was not always the case, where extreme droughts, floods, or both have taken a much larger toll on economic activity. Over the medium-term, with more resilient infrastructure (enhanced electricity generation and irrigation) and crop diversification, growth will strengthen and its susceptibility to weather shocks will decline. Improved competitiveness will support a narrowing of the current account deficit. Prudent policy implementation will contain inflation to single digits.

30. Debt vulnerabilities have risen and firm actions are needed to reduce them. Malawi is at moderate risk of external debt distress and high overall risk of debt distress. While some fiscal consolidation was achieved in FY 2018/19 and additional consolidation is envisaged in FY 2019/20, the pace of consolidation is slower than previously envisaged due to the need to accommodate post-cyclone reconstruction needs and increased security spending. This places increased emphasis on the authorities' delivering their planned medium-term fiscal adjustment to lower debt vulnerabilities. The authorities' medium-term plan appropriately focuses on strong revenue mobilization, further reorientation of spending towards growth-enhancing items, and advancing public investment management reforms. In particular, new borrowing should focus on projects with high rates of return that are closely aligned to development priorities and rely on concessional loans to contain borrowing costs. The upcoming submission to Parliament of an annual report on all SOEs will be an important step towards containing contingent liabilities.

31. Governance and transparency reforms—critical to reducing vulnerabilities to corruption, containing fiscal spending, and catalyzing donor support—are advancing. Good progress is being made in reforms to cash management, fiscal reporting, bank reconciliation, debt, improving the medium-term budgetary framework, and further broadening IFMIS coverage. The authorities are committed to implementing a new IFMIS but this needs to be carefully managed to minimize governance challenges stemming from implementation slippage and simultaneous introduction of new practices and technologies. Staff welcomes on-going efforts to deepen the domestic debt market and the increased engagement of the MoF in this area. The RBM has reduced its holdings of government securities and the new RBM Act enhances the RBM's independence. Staff urged the authorities to press forward with implementation of the remaining safeguards recommendations.

32. Monetary policy should continue to anchor inflation and the recent increase in exchange rate flexibility is welcome. While policy rate reductions earlier this year appear appropriate, persistently high food prices call for calibrating the monetary policy stance to preserve single-digit inflation. To avoid extreme bouts of excess liquidity in the market and maintain the interbank rate within the corridor, staff recommended raising repurchase agreement rates. Continued exchange rate flexibility will be critical for cushioning shocks and enhancing competitiveness and will be facilitated by a deepening of the interbank FX market.

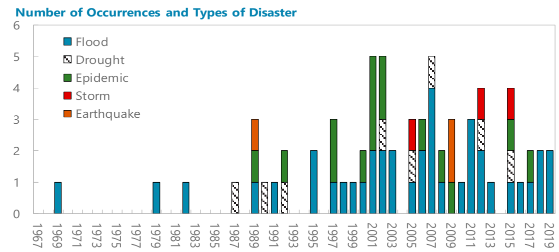
33. The banking system remains resilient. All banks are fully compliant with the IFRS9 standards. Non-performing loans have been reduced and provisioning increased. Plans for enhancing the collateral registry and steps to improve the quality of credit bureaus' reporting should support deeper financial intermediation. While credit to the private sector has picked up in recent months, sustainably increasing access to finance will require addressing structural barriers to reduce the cost of borrowing.

34. Staff supports the completion of the second and third reviews under the ECF, the request for waivers of non-observance for the end-December 2018 and end-June 2019 QPCs on the primary balance, and the request for augmentation of access. These recommendations are based on the authorities' commitment to corrective fiscal measures and on the strength of the reform agenda articulated by the authorities in their MEFP.

Box 1. Malawi and Climate Change

Malawi is extremely vulnerable to climate change: the frequency and intensity of droughts, intense rainfall, and flash floods have increased over the last 50 years (Figure 1). Globally, Malawi is ranked as the 23rd most vulnerable to climate change (MapleCroft, 2018) and 21st least prepared to adapt (Notre Dame Global Adaptation Initiative (ND-GAIN) Index, 2015). Against the backdrop of a rapidly growing population[1], reliance on rain-fed agriculture and poor infrastructure drive these vulnerabilities—each natural disaster poses a risk to food security and worsening income inequality.

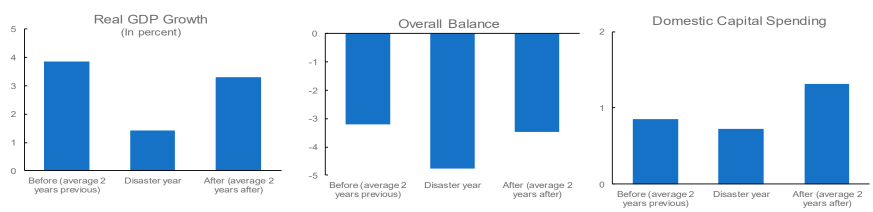
Weather-related Catastrophes in Malawi, 1967–2019



Source: EM-DAT: The Emergency Events Database.

Natural disasters have substantial macroeconomic costs for Malawi. An event study finds that even two years after the natural disaster, real GDP growth falls short of its pre-disaster rate (Figure 2).[2] Recouping lost physical and human capital can take years and reduced agriculture production spills over to livestock, food processing, and other sectors. Adverse revenue effects and large social assistance and reconstruction needs results in a lasting deterioration of the fiscal position, even two years after the disaster, weighing on debt. In the aftermath of a disaster, reduced agricultural exports, increased trade transit costs, and imports for reconstruction can raise current account pressures.

Real GDP Growth, Fiscal Balance, and Public Capital Spending Before and After Natural Disaster
(in percent of GDP unless otherwise indicated)



Source: EM-DAT: The Emergency Events Database.

A range of disaster relief policies are in place—including an emergency response plan with defined decision-making processes and readiness to contain disruptions to public services. Steps are being taken to improve mitigation, for example, with new environmental taxes.

However, a strategic approach to building resilience is still being developed. The National Disaster Recovery Framework and the 2017 Strategic Program for Climate Resilience are a good start. However, a realistic and costed roadmap is needed and it should include (i) structural resilience (roadways, energy, crops, livestock, fisheries, irrigation water supply systems); (ii) financial resilience (self-insurance, risk-transfer instruments); (iii) contingency planning to support post-disaster social; and policy buffers.

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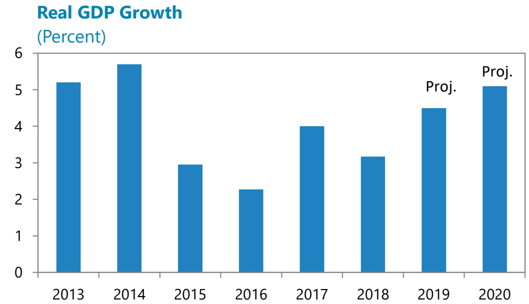
[1] With a 3 percent per annum growth rate, Malawi's population is expected to triple by 2050.

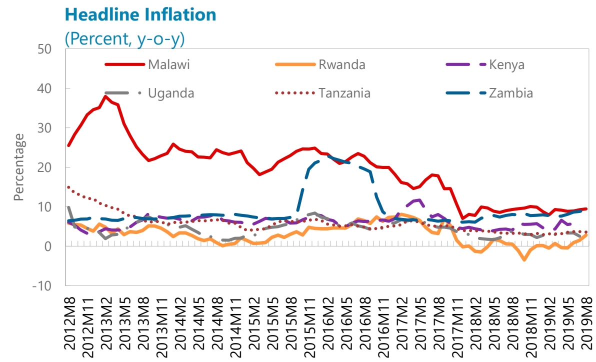
[2] The study covers episodes of natural disaster over the last two decades. While it does not determine causality, the study provides a useful benchmark in the absence of sufficient data for econometric analysis. A natural disaster is defined as one that results in damage and losses of at least 0.5 percent of GDP.

Figure 1. Malawi: Recent Economic Developments, 2013–20

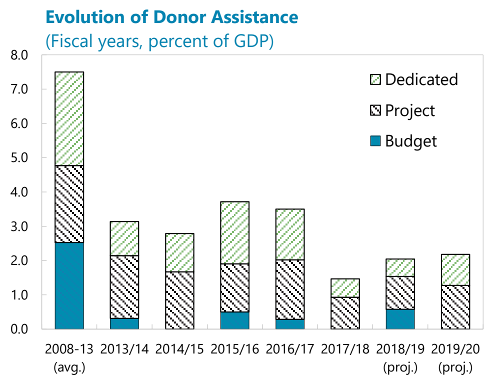
Real GDP growth is expected to rebound to 4.5 percent in 2019 from 3.2 percent in 2018.



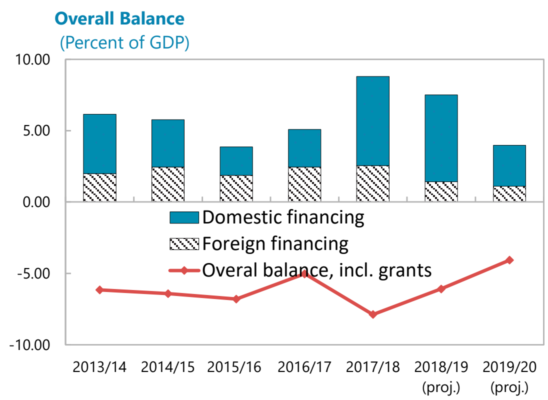
Despite being contained to single digits, headline inflation remains high compared to neighboring countries.



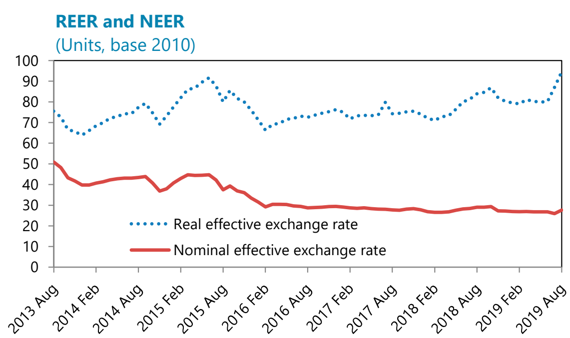
Donor assistance was adversely impacted by the cashgate scandal since 2013, and has yet to recover.



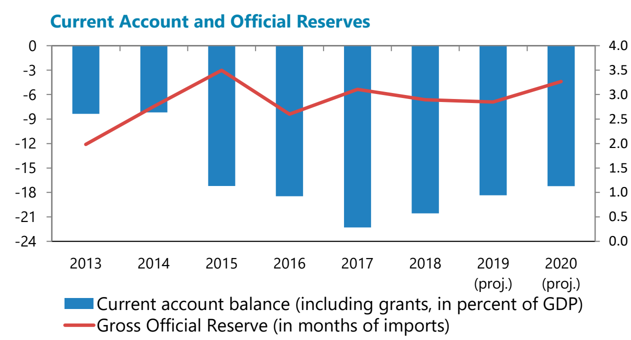
The fiscal stance tightened in FY2018/19 and was mainly domestically financed.



The REER has depreciated over the past year, following nominal exchange rate depreciation.



The current account deficit is narrowing with lower fuel prices and improved exports.



Sources: Malawian authorities; IMF staff estimates.

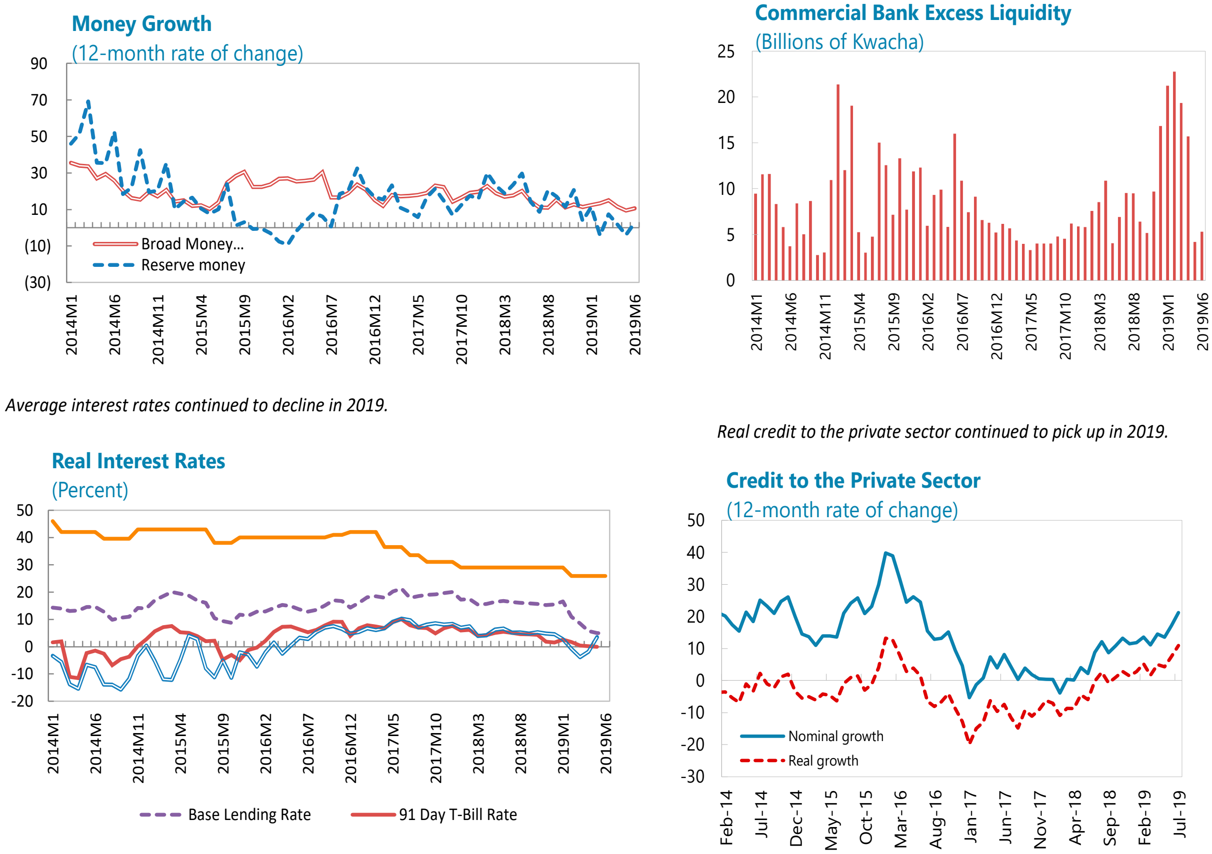
Figure 2. Malawi: Recent Monetary Developments, 2014-20

Money growth has declined over the past six years.

Excess liquidity in the banking system spiked in 2019H1 and then declined back to average levels (as of July).

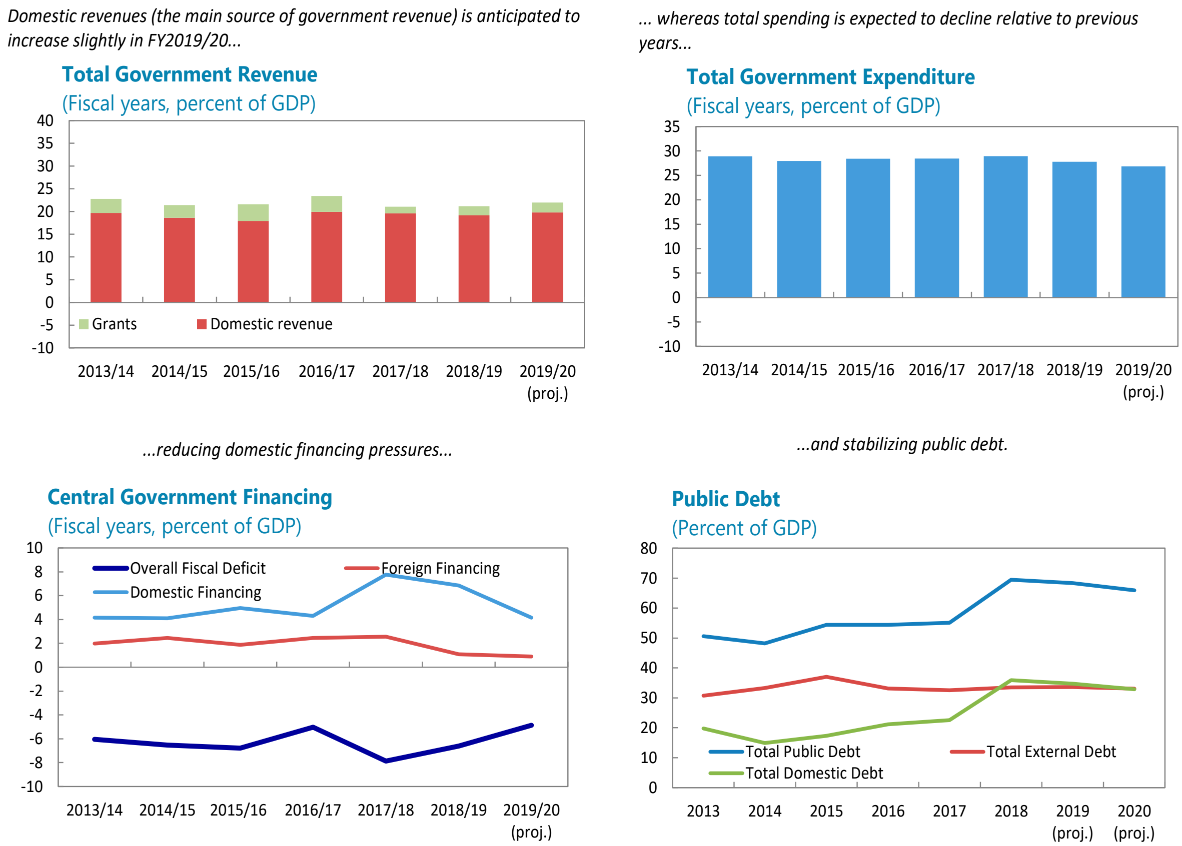
Average interest rates continued to decline in 2019.

Real credit to the private sector continued to pick up in 2019.



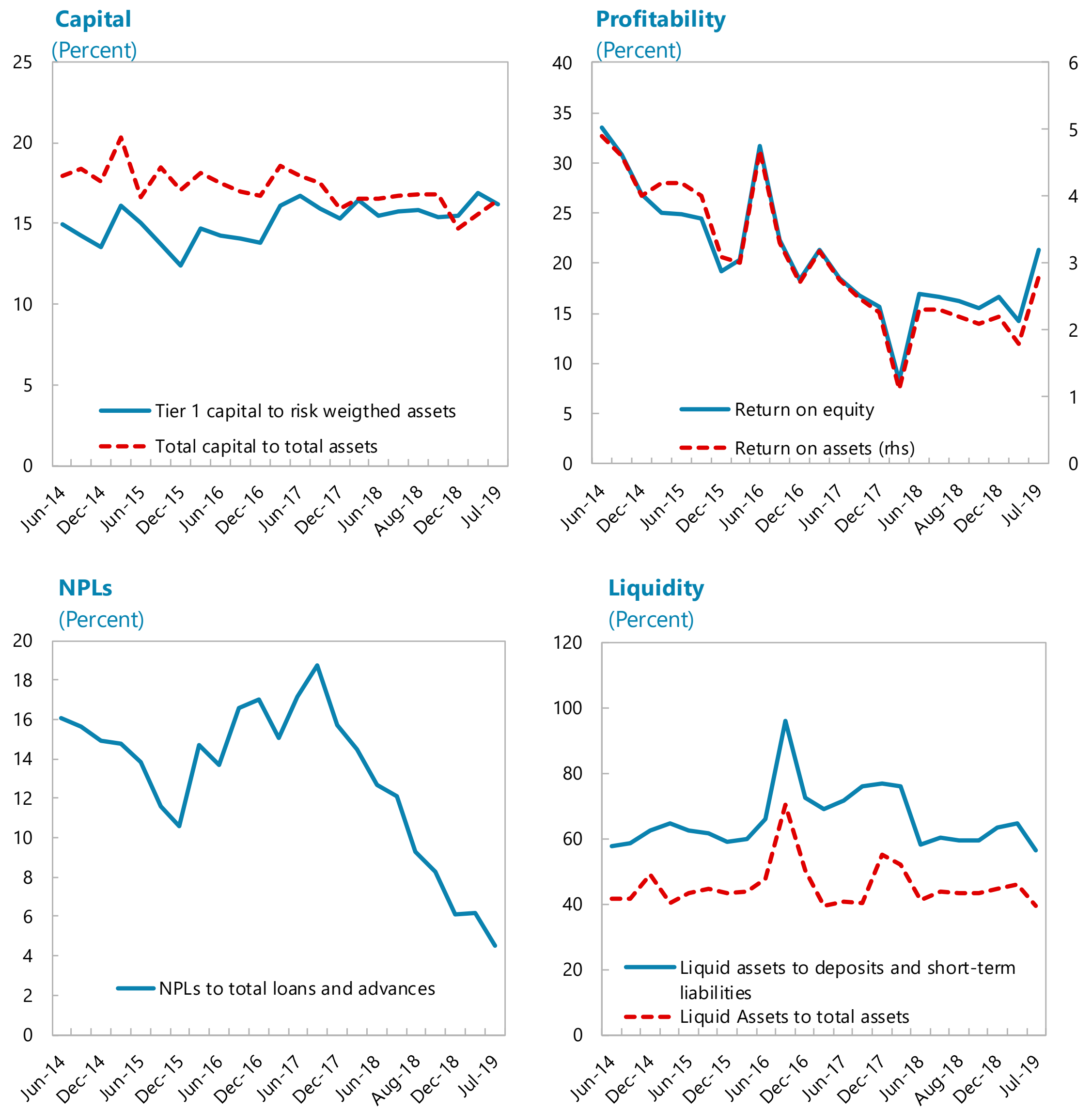
Sources: Malawian authorities; IMF staff estimates.

Figure 3. Malawi: Fiscal Developments and Outlook, 2013–20



Sources: Malawian authorities; IMF staff estimates.

Figure 4. Malawi: Selected Financial Stability Indicators, 2014–19



Sources: Malawian authorities; IMF staff estimates.

Table 1. Malawi: Selected Economic Indicators, 2017–24

	2017	2018		2019		2020	2021	2022	2023	2024
	Est.	1st.	Est.	1st.	Proj.			Proj.		
National accounts and prices (percent change, unless otherwise indicated)										
GDP at constant market prices	4.0	3.2	3.2	4.0	4.5	5.1	5.5	6.0	6.5	6.5
Nominal GDP (billions of Kwacha)	4,550	5,007	5,054	5,625	5,702	6,466	7,279	8,163	9,141	10,166
GDP deflator	10.9	7.8	7.7	8.0	8.0	7.9	6.7	5.8	5.1	4.4
Consumer prices (end of period)	7.1	9.5	9.9	8.9	9.8	7.9	7.0	5.9	5.3	5.0
Consumer prices (annual average)	11.5	9.1	9.2	9.0	9.1	8.7	7.4	6.4	5.8	5.0
Investment and savings (percent of GDP)										
National savings	-8.9	1.9	-9.1	4.7	-6.0	-4.6	-3.6	-2.2	-1.1	-0.1
Gross investment	13.4	11.3	11.5	12.3	12.4	12.6	13.3	13.5	13.7	13.9
Government	6.6	4.8	5.0	5.4	5.6	5.8	6.3	6.5	6.7	6.7
Private	6.7	6.5	6.5	6.9	6.8	6.8	6.9	6.9	7.0	7.2
Saving-investment balance	-22.3	-9.3	-20.6	-7.6	-18.4	-17.2	-16.8	-15.7	-14.8	-14.0
Central government (percent of GDP on a fiscal year basis)[1]										
Revenue	23.4	21.3	21.1	22.6	21.2	22.0	22.5	23.1	23.3	23.3
Tax and nontax revenue	19.9	19.8	19.6	20.2	19.1	19.8	20.3	20.7	20.8	20.8
Grants	3.5	1.5	1.5	2.3	2.0	2.2	2.2	2.4	2.5	2.5
Expenditure and net lending	28.4	29.2	28.9	26.5	27.8	26.8	25.7	25.0	24.6	24.7
Overall balance (excluding grants)	-8.5	-9.4	-9.3	-6.3	-8.7	-7.0	-5.4	-4.3	-3.8	-3.9
Overall balance (including grants)	-5.0	-7.9	-7.9	-3.9	-6.6	-4.9	-3.2	-2.0	-1.3	-1.4
Foreign financing	2.5	2.6	2.6	0.6	1.1	0.9	1.1	1.1	1.0	1.1
Total domestic financing	4.3	7.8	7.8	4.8	6.9	4.3	2.1	0.9	0.3	0.3
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Discrepancy	0.0	-0.4	-0.4	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Primary balance	-0.6	-4.3	-4.3	0.0	-2.3	-0.8	0.2	0.2	0.3	0.2
Primary balance (excluding budget support and dedicated grants)	-2.4	-4.9	-4.8	-1.1	-3.4	-1.7	-0.7	-0.7	-0.6	-0.6
Domestic primary balance[2]	-1.7	-1.1	-2.6	1.4	-1.2	0.9	2.0	2.0	2.0	2.0
Money and credit (change in percent of broad money at the beginning of the period, unless otherwise indicated)										
Money and quasi money	19.7	11.9	11.4	12.3	12.8	13.4	12.8	12.6	12.5	12.3
Net foreign assets	11.1	-11.5	-7.8	7.4	-0.3	10.1	10.8	9.4	10.0	9.5
Net domestic assets	8.5	23.5	23.0	4.9	9.8	3.3	2.0	3.2	2.5	2.8
Credit to the government	21.3	9.8	7.3	2.9	1.6	2.3	1.8	0.1	0.2	0.4
Credit to the private sector (percent change)	0.4	8.0	11.5	10.1	13.7	14.8	15.2	16.1	16.2	16.1
External sector (US$ millions, unless otherwise indicated)										
Exports (goods and services)	1,053	1,844	1,112	1,982	1,239	1,365	1,482	1,611	1,749	1,902
Imports (goods and services)	2,756	2,695	2,927	2,846	3,109	3,270	3,486	3,629	3,819	4,015
of which: recovery and reconstruction related	…	…	…	…	85	109	40	…	…	…
Gross official reserves	758	695	750	791	777	950	1,097	1,204	1,342	1,489
(months of imports)	3.1	2.9	2.9	3.2	2.9	3.3	3.6	3.8	4.0	4.1
Current account (percent of GDP, assuming financing gap is closed)[3]	-22.3	-9.3	-20.6	-7.6	-18.4	-17.2	-16.8	-15.7	-14.8	-14.0
Current account, excl. official transfers (percent of GDP)	-22.5	-9.3	-20.5	-8.7	-18.9	-17.2	-16.8	-15.7	-14.8	-14.0
Current account, excl. project related imports (percent of GDP)	-19.0	-7.1	-18.6	-4.8	-15.9	-14.9	-14.3	-13.0	-12.1	-11.3
Current account, excl. official transfers and project related imports (percent of G	-19.2	-7.1	-18.6	-5.9	-16.5	-14.9	-14.3	-13.0	-12.1	-11.2
Current account (percent of GDP, assuming financing gap is not closed)[4]	-22.3	-9.3	-20.6	-7.6	-18.9	-17.2	-16.8	-15.7	-14.8	-14.0
Real effective exchange rate (percent change)	4.5	…	7.6	…	…	…	…	…	…	…
Overall balance (percent of GDP)	2.1	-1.0	-0.2	1.1	-1.1	1.6	1.8	1.6	1.7	1.7
Financing gap	0.0	0.0	0.0	0.0	93.7	31.0	0.0	0.0	0.0	0.0
Of which: IMF ECF Augmentation	…	…	…	…	12.9	26.0	…	…	…	…
World Bank	…	…	…	…	70.0	0.0	…	…	…	…
Others	…	…	…	…	10.0	5.0	…	…	…	…
Terms of trade (percent change)	-2.0	-4.1	-6.2	-0.9	2.4	0.5	0.6	0.0	-0.7	-1.2
Debt stock and service (percent of GDP, unless otherwise indicated)										
External debt (public sector)	32.8	31.2	31.2	31.4	29.8	29.5	29.1	28.0	26.8	25.8
NPV of public external debt (percent of exports)	82.7	75.7	123.3	74.3	116.3	110.8	107.7	102.5	97.2	107.0
Domestic public debt	23.9	26.1	28.0	24.8	32.0	30.6	29.0	25.9	23.4	21.4
Total public debt	56.7	57.3	59.2	56.1	61.8	60.0	58.1	54.0	50.2	47.3
External debt service (percent of exports)	9.3	7.2	6.4	4.5	7.1	6.9	7.2	7.8	7.3	7.1
External debt service (percent of revenue excl. grants)	8.0	9.5	5.1	6.1	6.1	5.5	5.9	6.5	6.1	6.0
91-day treasury bill rate (end of period)	14.7	…	11.4	…	…	…	…	…	…	…

Sources: Malawian authorities and IMF staff estimates and projections.

[1] The fiscal year starts in July and ends in June. The current financial year, 2020, runs from July 1, 2019 to June 30, 2020.

[2] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and nontax revenues.

[3] Based on the findings of recent technical support missions, confirming the reliability of the trade data produced by the Malawi National Statistics Office (NSO), the IMF has now adpoted the NSO's current account data. Previously, the series reported by the IMF was based on staff estimates. Errors and omissions were adjusted by offsetting amounts, leaving the overall balance unchanged for historical data. Errors and omissions are projected at zero and short-term capital and other inflows projections are adjusted in the financial account. Future TA missions on capital and financial accounts' statistics will seek to better identify the offsetting flows to the current account adjustment.

[4] The current account assuming the financing gap is not closed, excludes $40 million of budget support from the World Bank in 2019.

Table 2a. Malawi: Central Government Operations, 2017/18–23/24

(Billions of Kwacha)

	2017/18		2018/19			2019/20			2020/21	2021/22	2022/23	2023/24
	Program	Est.	Approved Budget	1st Review	Est.	1st Review	Approved Budget	Proj.	Proj.			
Revenue	1,065	1,007	1,264	1,194	1,133	1,402	1,595	1,330	1,540	1,773	2,011	2,239
Tax and nontax revenue	931	937	1,067	1,070	1,023	1,194	1,445	1,198	1,392	1,590	1,793	2,001
Tax Revenue	839	830	940	956	931	1,076	1,324	1,087	1,260	1,440	1,625	1,813
Taxes on income and profits	422	419	477	481	456	541	632	531	608	692	780	870
Taxes on goods and services	354	353	402	407	408	458	580	470	553	634	714	797
Taxes on international trade	75	76	78	89	88	101	123	115	131	149	167	187
Other taxes	-13	-18	-17	-21	-22	-24	-11	-28	-32	-35	-37	-41
Nontax revenue	92	107	127	114	92	118	121	111	132	150	168	187
Grants	134	70	197	123	109	208	150	132	148	182	219	238
Budget support grants	0	0	60	0	31	60	0	0	0	0	0	0
Project grants	87	44	74	67	52	83	85	77	88	114	144	163
Dedicated grants	48	26	63	56	27	65	65	55	60	69	75	75
Expenditure and net lending	1,414	1,384	1,488	1,402	1,488	1,566	1,751	1,624	1,760	1,924	2,122	2,372
Current expenditure	1,093	1,152	1,132	1,125	1,196	1,215	1,304	1,266	1,344	1,420	1,544	1,726
Wages and salaries	315	316	394	390	387	439	443	443	501	563	631	704
Interest payments	190	190	183	208	224	228	244	246	233	168	134	155
Domestic	176	177	169	189	209	211	229	230	215	149	112	132
Foreign	14	14	14	19	16	17	15	15	17	19	22	24
Goods and services	289	327	336	306	354	305	345	318	335	389	448	500
Generic goods and services	130	130	130	120	131	145	177	164	163	191	214	239
Census	3	3	6	6	6	0	1	1	0	0	0	0
Road maintenance and storage levey expenses	20	28	32	22	23	24	38	27	31	34	38	43
Agricultural sector	7	7	7	7	6	9	9	9	11	13	14	16
Health sector	36	40	45	43	43	57	54	54	61	76	93	104
Education sector	25	25	28	29	27	39	30	30	33	41	51	57
National / local elections	10	30	51	51	63	2	1	1	1	0	0	0
Statutory expenditures	2	4	2	2	6	2	5	8	9	5	3	3
Maize purchases and winter cropping program	25	35	20	10	9	10	10	8	8	9	10	11
Rural electrification	18	22	15	15	39	16	20	16	18	20	23	26
Subsidies and other current transfers	237	242	215	217	225	239	265	252	271	294	325	359
Pension and gratuities	69	76	81	81	84	91	101	95	107	120	135	150
Transfers to road and revenue authorities	25	25	28	29	29	32	40	34	38	43	49	54
Transfers to public entities and households	110	106	66	66	74	76	88	88	95	101	113	127
Fertilizer and seed subsidy	33	35	41	41	39	40	36	36	31	30	28	28
Of which : seed subsidy	5	7	11	11	10	13	5	5	5	5	5	5
Arrears payments[1]	62	77	4	4	5	4	7	7	5	6	6	7
of which : Issuance of zero interest promissory notes for securitizing domestic arrears	58	73	0	0	0	0	0	0	0	0	0	0
Development expenditure	317	227	349	270	284	343	438	349	407	499	574	642
Foreign financed	228	149	219	197	168	223	306	233	271	319	369	412
Domestically financed	89	78	130	73	116	120	131	115	136	180	205	230
Net lending	4	4	8	8	8	7	9	9	9	4	4	4
Discrepancy	14	-19	0	0	5	0	0	0	0	0	0	0
Overall balance (incl. grants and discrepancy)	-335	-395	-225	-208	-350	-164	-156	-294	-220	-151	-111	-133
Overall balance[2]	-277	-323	-225	-208	-350	-164	-156	-294	-220	-151	-111	-133
Total financing (net)	335	395	225	208	350	165	156	294	220	151	111	133
Foreign financing (net)	155	122	41	32	58	112	110	55	78	83	89	106
Borrowing	183	150	82	79	89	154	156	102	123	137	150	174
Budget support loans	63	65	0	0	0	0	0	0	0	0	0	0
Project loans	100	82	79	79	78	140	150	96	116	128	141	163
Other external loans[3]	20	2	3	0	11	14	7	6	7	8	10	11
Amortization	-28	-27	-40	-47	-31	-43	-47	-47	-46	-54	-61	-68
Sale of non-financial assets (privatization proceeds)	0	0	0	0	0	0	0	0	0	0	0	0
Net issuance of promissory notes for securitizing domestic arrears	-45	-25	0	-78	-75	0	0	-9	0	0	0	0
Net domestic financing (NDF)	225	298	183	254	367	54	46	249	143	68	22	27
of which: RBM financing of central government	69	-43	0	0	-79	0	0	0	0	0	0	0
Financing gap	0	0	0	0	0	-1	0	0	0	0	0	0
Memorandum items:												
Issuance of promissory notes for securitizing domestic arrears	58	73	0	0	0	0	0	0	0	0	0	0
Primary balance (including grants and discrepancy)	-145	-205	-42	0	-126	65	88	-49	12	17	22	22
Primary balance (excluding budget support and dedicated grants)	-193	-231	-164	-56	-183	-61	23	-103	-48	-52	-52	-53
Adjusted primary balance (including grants and discrepancy)[4]	-163			8								
Domestic primary balance[5]	-51	-126	-20	73	-67	79	245	53	136	154	173	197
Maturing promissory notes for domestic arrears	103	98	0	78	75	0	0	9	0	0	0	0
NDF adjusted for payment of arrears	123	200	183	176	292	54	46	239	143	68	22	27
Nominal GDP (fiscal year)	4,764	4,783	5,353	5,292	5,353	5,956	6,055	6,055	6,841	7,687	8,614	9,614

Sources: Malawi Ministry of Finance and IMF staff projections.

[1] This includes promissory notes issued for the repayment of domestic arrears accumulated before FY2014/15.

[2] Excludes issuance of promissory notes for securitization of arrears.

[3] Other external loans include program loans other than budgetary support.

[4] Adjusted primary balance is calculated by subtracting shortfalls in budget support grants, dedicated grants, and budget support loans, as well as increase in debt service payments to WB and AfDB.

[5] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and nontax revenues.

Table 2b. Malawi: Central Government Operations, 2017/18–23/24

(Percent of GDP)

	2017/18		2018/19			2019/20			2020/21	2021/22	2022/23	2023/24
	Program	Est.	Approved Budget	1st Review	Est.	1st Review	Approved Budget	Proj.	Proj.			
Revenue	22.4	21.1	23.6	22.6	21.2	23.5	26.3	22.0	22.5	23.1	23.3	23.3
Tax and nontax revenue	19.5	19.6	19.9	20.2	19.1	20.0	23.9	19.8	20.3	20.7	20.8	20.8
Tax Revenue	17.6	17.4	17.6	18.1	17.4	18.1	21.9	18.0	18.4	18.7	18.9	18.9
Taxes on income and profits	8.9	8.8	8.9	9.1	8.5	9.1	10.4	8.8	8.9	9.0	9.1	9.1
Taxes on goods and services	7.4	7.4	7.5	7.7	7.6	7.7	9.6	7.8	8.1	8.3	8.3	8.3
Taxes on international trade	1.6	1.6	1.5	1.7	1.6	1.7	2.0	1.9	1.9	1.9	1.9	1.9
Other taxes	-0.3	-0.4	-0.3	-0.4	-0.4	-0.4	-0.2	-0.5	-0.5	-0.5	-0.4	-0.4
Nontax revenue[1]	1.9	2.2	2.4	2.2	1.7	2.0	2.0	1.8	1.9	1.9	1.9	1.9
Grants	2.8	1.5	3.7	2.3	2.0	3.5	2.5	2.2	2.2	2.4	2.5	2.5
Budget support grants	0.0	0.0	1.1	0.0	0.6	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Project grants	1.8	0.9	1.4	1.3	1.0	1.4	1.4	1.3	1.3	1.5	1.7	1.7
Dedicated grants	1.0	0.5	1.2	1.1	0.5	1.1	1.1	0.9	0.9	0.9	0.9	0.8
Expenditure and net lending	29.7	28.9	27.8	26.5	27.8	26.3	28.9	26.8	25.7	25.0	24.6	24.7
Current expenditure	23.0	24.1	21.1	21.3	22.3	20.4	21.5	20.9	19.6	18.5	17.9	17.9
Wages and salaries	6.6	6.6	7.4	7.4	7.2	7.4	7.3	7.3	7.3	7.3	7.3	7.3
Interest payments	4.0	4.0	3.4	3.9	4.2	3.8	4.0	4.1	3.4	2.2	1.6	1.6
Domestic	3.7	3.7	3.1	3.6	3.9	3.5	3.8	3.8	3.1	1.9	1.3	1.4
Foreign	0.3	0.3	0.3	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.2
Goods and services	6.1	6.8	6.3	5.8	6.6	5.1	5.7	5.2	4.9	5.1	5.2	5.2
Generic goods and services	2.7	2.7	2.4	2.3	2.5	2.4	2.9	2.7	2.4	2.5	2.5	2.5
Road maintenance and storage levy expenses	0.4	0.6	0.6	0.4	0.4	0.4	0.6	0.5	0.4	0.4	0.4	0.4
Agricultural sector	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Health sector	0.8	0.8	0.8	0.8	0.8	1.0	0.9	0.9	0.9	1.0	1.1	1.1
Education sector	0.5	0.5	0.5	0.6	0.5	0.7	0.5	0.5	0.5	0.5	0.6	0.6
National / local elections	0.2	0.6	1.0	1.0	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Statutory expenditures	0.0	0.1	0.0	0.0	0.1	0.0	0.1	0.1	0.1	0.1	0.0	0.0
Maize purchases and winter cropping programs	0.5	0.7	0.4	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1
Rural electrification	0.4	0.5	0.3	0.3	0.7	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Subsidies and other current transfers	5.0	5.1	4.0	4.1	4.2	4.0	4.4	4.2	4.0	3.8	3.8	3.7
Pension and gratuities	1.4	1.6	1.5	1.5	1.6	1.5	1.7	1.6	1.6	1.6	1.6	1.6
Transfers to road and revenue authorities	0.5	0.5	0.5	0.5	0.5	0.5	0.7	0.6	0.6	0.6	0.6	0.6
Transfers to public entities	2.3	2.2	1.2	1.2	1.4	1.3	1.5	1.5	1.4	1.3	1.3	1.3
Fertilizer and seed subsidy	0.7	0.7	0.8	0.8	0.7	0.7	0.6	0.6	0.5	0.4	0.3	0.3
Of which : seed subsidy	0.1	0.1	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Arrears payments[1]	1.3	1.6	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
of which : Issuance of zero interest promissory notes for securitizing domestic arrears	1.2	1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Development expenditure	6.6	4.8	6.5	5.1	5.3	5.8	7.2	5.8	5.9	6.5	6.7	6.7
Foreign financed	4.8	3.1	4.1	3.7	3.1	3.7	5.1	3.9	4.0	4.2	4.3	4.3
Domestically financed	1.9	1.6	2.4	1.4	2.2	2.0	2.2	1.9	2.0	2.3	2.4	2.4
Net lending	0.1	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.0	0.0
Discrepancy	0.3	-0.4	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (including grants and discrepancy)	-7.0	-8.3	-4.2	-3.9	-6.5	-2.7	-2.6	-4.9	-3.2	-2.0	-1.3	-1.4
Overall balance[2]	-5.8	-6.7	-4.2	-3.9	-6.5	-2.7	-2.6	-4.9	-3.2	-2.0	-1.3	-1.4
Total financing (net)	7.0	8.3	4.2	3.9	6.5	2.8	2.6	4.9	3.2	2.0	1.3	1.4
Foreign financing (net)	3.2	2.6	0.8	0.6	1.1	1.9	1.8	0.9	1.1	1.1	1.0	1.1
Borrowing	3.8	3.1	1.5	1.5	1.7	2.6	2.6	1.7	1.8	1.8	1.7	1.8
Budget support loans	1.3	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	2.1	1.7	1.5	1.5	1.5	2.4	2.5	1.6	1.7	1.7	1.6	1.7
Other external loans[3]	0.4	0.1	0.1	0.0	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Amortization	-0.6	-0.6	-0.8	-0.9	-0.6	-0.7	-0.8	-0.8	-0.7	-0.7	-0.7	-0.7
Sale of non-financial assets (privatization proceeds)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net issuance of promissory notes for securitizing domestic arrears	-0.9	-0.5	0.0	-1.5	-1.4	0.0	0.0	-0.2	0.0	0.0	0.0	0.0
Net domestic financing (NDF)	4.7	6.2	3.4	4.8	6.9	0.9	0.8	4.1	2.1	0.9	0.3	0.3
of which: RBM financing of central government	1.4	-1.0	0.0	0.0	-1.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:												
Primary balance (including grants and discrepancy)	-3.0	-4.3	-0.8	0.0	-2.3	1.1	1.5	-0.8	0.2	0.2	0.3	0.2
Primary balance (excluding budget support and dedicated grants)	-4.0	-4.8	-3.1	-1.1	-3.4	-1.0	0.4	-1.7	-0.7	-0.7	-0.6	-0.6
Adjusted primary balance (including grants and discrepancy)[4]	-3.4			0.1								
Domestic primary balance[5]	-1.1	-2.6	-0.4	1.4	-1.2	1.3	4.0	0.9	2.0	2.0	2.0	2.0
Maturing promissory notes for domestic arrears	2.2	2.0	0.0	1.5	1.4	0.0	0.0	0.2	0.0	0.0	0.0	0.0
NDF adjusted for payment of arrears	2.6	4.2	3.4	3.3	5.4	0.9	0.8	4.0	2.1	0.9	0.3	0.3
Nominal GDP (fiscal year)	4,764	4,783	5,353	5,292	5,353	5,956	6,055	6,055	6,841	7,687	8,614	9,614

Sources: Malawi Ministry of Finance and IMF staff projections.

[1] This includes promissory notes issued for the repayment of domestic arrears accumulated before FY2014/15.

[2] Excludes issuance of promissory notes for securitization of arrears.

[3] Other external loans include program loans other than budgetary support.

[4] Adjusted primary balance is calculated by subtracting shortfalls in budget support grants, dedicated grants, and budget support loans, as well as increase in debt service payments to WB and AfDB.

[5] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and nontax revenues.

Table 2c. Malawi: Central Government Quarterly Operations in FY 18/19 and FY 19/20

(Billions of Kwacha)

	2018/19					2019/20				
	Q1	Q2	Q3	Q4	Annual	Q1	Q2	Q3	Q4	Annual
			Est.			Est.		Proj.		
Revenue	289.1	274.5	257.6	311.4	1,132.6	316.9	328.4	333.6	350.8	1,329.7
Tax and nontax revenue	266.8	257.0	245.0	254.5	1,023.4	279.4	290.5	308.5	319.5	1,197.9
Tax revenue	244.9	234.1	220.6	231.5	931.1	260.6	264.7	276.4	285.6	1,087.2
Taxes on income and profits	116.6	112.6	113.7	113.5	456.4	130.3	119.5	140.3	140.9	531.0
Taxes on goods and services	108.1	103.8	95.0	101.2	408.1	110.6	120.8	115.2	122.9	469.5
Taxes on international trade	24.8	23.9	18.4	21.2	88.3	24.1	31.5	27.7	31.8	115.0
Other taxes	-4.5	-6.2	-6.5	-4.4	-21.6	-4.4	-7.1	-6.8	-10.0	-28.3
Nontax revenue	21.9	22.9	24.5	23.0	92.2	18.9	25.8	32.1	33.9	110.7
Grants	22.3	17.5	12.6	56.9	109.3	37.5	37.9	25.1	31.4	131.8
Budget support grants	0.0	0.0	0.0	30.7	30.7	0.0	0.0	0.0	0.0	0.0
Project grants	16.0	4.1	12.4	19.0	51.5	19.2	19.2	19.2	19.2	77.0
Dedicated grants	6.4	13.4	0.1	7.1	27.0	18.2	18.6	5.8	12.1	54.8
Expenditure and net lending	383.4	370.9	377.8	355.7	1,487.9	426.9	442.9	377.4	376.8	1,624.1
Current expenditure	298.8	299.5	300.2	297.6	1,196.2	323.4	352.3	299.1	291.3	1,266.1
Wages and salaries	93.8	97.3	98.4	97.9	387.4	108.5	110.2	112.2	112.5	443.4
Interest payments	53.6	38.5	56.0	76.2	224.3	56.0	67.0	51.9	70.9	245.8
Domestic	49.4	35.0	51.8	72.4	208.7	52.3	63.2	47.9	67.0	230.4
Foreign	4.3	3.4	4.2	3.8	15.6	3.8	3.8	4.0	3.9	15.5
Goods and services	99.3	97.8	80.4	76.6	354.1	94.6	99.8	65.2	58.1	317.6
Generic goods and services	42.1	42.5	29.4	17.4	131.5	53.3	54.7	32.3	23.5	163.9
Census	6.4	0.0	0.0	0.0	6.4	0.5	0.0	0.0	0.0	0.5
Road Maintenance	6.6	5.2	5.9	5.5	23.2	7.4	6.6	7.0	6.4	27.4
Agricultural sector	1.7	1.6	1.9	1.1	6.3	2.3	2.4	3.1	1.5	9.3
Health sector	12.2	10.1	10.5	10.0	42.8	11.8	17.5	11.4	13.5	54.3
Education sector	10.0	7.8	5.4	3.6	26.8	9.9	8.0	5.4	6.4	29.6
National / local elections	14.3	15.1	13.6	19.9	62.9	0.7	0.3	0.0	0.0	1.0
PFEM	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Statutory expenditures	1.8	3.5	0.9	0.2	6.4	2.1	2.5	1.4	1.7	7.6
National AIDS Commission	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Maize purchases and winter cropping program	0.4	7.0	1.4	0.0	8.7	3.5	3.0	1.5	0.0	8.0
Rural Electrification	3.8	5.1	11.3	18.9	39.1	3.1	4.8	3.0	5.1	16.0
Subsidies and other current transfers	50.5	65.8	64.9	44.0	225.3	61.4	74.2	68.8	47.9	252.2
Pension and gratuities	20.4	20.2	23.4	19.7	83.6	24.5	21.9	25.8	22.5	94.7
Transfers to road and revenue authorities	7.2	7.4	7.3	6.9	28.8	8.1	8.2	8.5	8.9	33.7
Transfers to public entities and households	20.5	20.9	16.6	16.4	74.3	26.3	28.4	17.2	16.4	88.3
Fertilizer and seed subsidy	2.5	17.4	17.7	1.1	38.6	2.6	15.6	17.3	0.0	35.5
Of which: seed subsidy	2.1	3.0	4.0	1.1	10.2	1.3	1.2	1.2	1.2	5.0
Arrears payments[1]	1.6	0.1	0.5	3.0	5.2	2.9	1.1	1.0	2.0	7.0
Of which, issuance of zero-coupon promissory notes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Development expenditure	78.6	69.4	77.6	58.1	283.7	97.5	89.0	76.9	85.6	348.9
Foreign financed	49.5	36.1	42.4	40.0	168.0	75.4	59.1	46.3	52.6	233.5
Domestically financed	29.1	33.3	35.2	18.1	115.7	22.0	29.9	30.6	33.0	115.5
Net lending	6.0	2.0	0.0	0.0	8.0	6.0	1.6	1.4	0.0	9.0
Overall balance (including grants)	-94.3	-96.4	-120.2	-44.3	-355.2	-110.1	-114.5	-43.8	-26.0	-294.4
Discrepancy	38.0	-23.0	-20.3	10.7	5.3	0.0	0.0	0.0	0.0	0.0
Overall balance (including grants and discrepancy)	-56.3	-119.4	-140.5	-33.7	-349.9	-110.1	-114.5	-43.8	-26.0	-294.4
Overall balance[2]	**-56.3**	**-119.4**	**-140.5**	**-33.7**	**-349.9**	**-110.1**	**-114.5**	**-43.8**	**-26.0**	**-294.4**
Foreign financing (net)	18.3	12.4	21.0	6.5	58.3	26.7	10.0	9.3	9.1	55.0
Borrowing	27.1	18.6	29.8	13.8	89.4	38.0	21.2	21.2	21.2	101.7
Budget support loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	21.1	15.5	28.1	13.4	78.1	36.5	19.7	19.7	19.7	95.7
Other external loans[3]	6.1	3.1	1.7	0.5	11.3	1.5	1.5	1.5	1.5	6.0
Amortization	-8.8	-6.2	-8.8	-7.3	-31.2	-11.3	-11.3	-12.0	-12.1	-46.7
Net Issuance of promissory notes for securitizing domestic arrears	-25.5	-17.4	-3.7	-28.5	-75.1	-7.6	-1.8	0.0	0.0	-9.4
Net domestic financing (NDF)	63.5	124.4	123.2	55.7	366.8	91.0	106.3	34.5	16.9	248.9
of which: RBM financing of central government	-15.0	40.5	-175.6	70.9	-79.3	0.0	0.0	0.0	0.0	0.0
Financing gap	38.0	-23.0	-20.3	10.7	5.3	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Primary balance (including grants and discrepancy)	-2.7	-81.0	-84.5	42.5	-125.6	-54.0	-47.5	8.1	44.8	-48.6
Primary balance (excluding budget support and dedicated grants)	-9.0	-94.4	-84.6	4.7	-183.4	-72.3	-66.1	2.3	32.7	-103.4
Domestic primary balance[4]	24.5	-62.3	-54.7	25.7	-66.9	-16.1	-26.3	29.4	66.1	53.1
Maturing promissory notes for domestic arrears	25.5	17.4	3.7	28.5	75.1	7.6	1.8	0.0	0.0	9.4
NDF adjusted for payment of arrears	38.0	107.0	119.5	27.2	291.7	83.4	104.5	34.5	16.9	239.4
Nominal GDP					5,353.2					6,052.7

Sources: Malawi Ministry of Finance and IMF staff estimates.

[1] This includes promissory notes issued for the repayment of domestic arrears accumulated before FY2014/15.

[2] Excludes issuance of promissory notes for securitization of arrears.

[3] Other external loans include program loans other than budgetary support.

[4] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and nontax revenues.

Table 3a. Malawi: Monetary Authorities' Balance Sheet, 2018–20

(Billions of Kwacha, unless otherwise indicated)

	2018				2019				2020			
	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Dec.
					Est.		Proj.				Proj.	
Reserve Money	255	301	299	289	274	309	311	315	309	333	352	357
Currency outside banks	147	207	192	189	165	217	...	...	...	...	...	...
Cash in vault	27	24	25	40	26	28	...	...	...	...	...	...
Commercial bank deposits with RBM	81	70	81	60	83	64	...	...	...	...	...	...
Net foreign assets (NFA)	248	315	274	313	329	338	275	282	315	346	384	413
Foreign assets	481	546	501	547	562	582	543	586	620	674	713	766
Foreign liabilities	-234	-231	-228	-234	-233	-244	-269	-304	-305	-328	-329	-353
Net domestic assets	7	-15	65	17	-15	14	36	33	-6	-13	-32	-56
Credit to government (net)	419	295	280	320	145	215	215	215	215	215	215	215
Credit to domestic banks	0	0	0	0	0	0	0	0	0	0	0	0
Other items (net)	-411	-309	-215	-303	-160	-202	-179	-183	-221	-229	-247	-271
Open market operations	-395	-283	-201	-214	-91	-120	...	...	...	...	...	...
Others	-16	-26	-14	-89	-69	-81	...	...	...	...	...	...
Memorandum items:												
Money multiplier	4.0	3.8	3.8	4.1	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.3
Annual growth of reserve money (percent)	18.7	14.2	17.1	3.8	7.4	2.8	4.1	8.8	13.0	7.8	13.3	13.4
91-day treasury bill rate	14.0	14.1	14.0	11.4	9.7	9.0	...	...	...	...	...	...
NFA of the central bank (US$ millions)	434	434	376	428	444	423	371	374	411	444	484	512
Foreign assets (US$ millions)	753	753	689	750	761	741	733	777	808	865	899	950
Foreign liabilities (US$ millions)	-318	-318	-313	-322	-316	-318	-363	-403	-398	-421	-415	-438

Sources: Reserve Bank of Malawi; and IMF staff projections.

Table 3b. Malawi: Monetary Survey, 2018–20

(Billions of Kwacha, unless otherwise indicated)

	2018				2019				2020			
	Mar.	Jun.	Sept.	Dec.	Mar.	June.	Sept.	Dec.	Mar.	June.	Sept.	Dec.
					Est.	Proj.			Proj.			
Money and quasi-money	1,021	1,142	1,141	1,196	1,174	1,263	1,333	1,350	1,326	1,429	1,510	1,531
Money	477	551	502	555	532	217	...	...	...	...	...	...
Quasi-money	544	591	638	642	642	667	...	...	...	...	...	...
Of which: foreign currency deposits	184	211	228	200	196	218	...	...	...	...	...	...
Net foreign assets (NFA)	344	408	330	371	413	421	359	368	402	435	474	504
Monetary authorities	248	315	274	313	329	338	275	282	315	346	384	413
Gross foreign assets	481	546	501	547	562	582	543	586	620	674	713	766
Foreign liabilities	-234	-231	-228	-234	-233	-244	-269	-304	-305	-328	-329	-353
Commercial banks (net)	96	92	56	59	84	82	84	86	87	89	90	92
Net domestic assets	676	734	850	865	802	886	974	982	924	994	1,036	1,027
Credit to government (net)	583	510	546	607	547	616	605	627	633	637	647	658
Credit to statutory bodies (net)	4	12	34	34	45	49	50	50	52	55	58	61
Credit to private sector	398	428	447	457	442	502	512	519	490	560	578	596
Other items (net)	-308	-216	-217	-273	-273	-323	-193	-214	-252	-257	-248	-288
Memorandum items:												
Velocity of money (annualized GDP divided by broad money)	4.6	4.2	4.3	4.2	4.4	4.2	4.1	4.2	4.4	4.2	4.1	4.2
Annual growth of broad money (percent)	17.0	14.6	6.2	11.4	15.0	10.7	16.9	12.8	13.0	13.1	13.3	13.4
Annual growth of credit to the private sector (percent)	0.4	2.1	9.1	11.5	11.1	17.1	14.5	13.7	10.8	11.6	12.9	14.8
NFA of the commercial banks (US$ millions)	132.9	127.1	77.6	80.3	105.0	113.6	113.6	113.6	113.6	113.6	113.6	113.6
Gross foreign assets (US$ millions)	163.8	187.2	145.0	153.4	156.7	155.9	155.9	155.9	155.9	155.9	155.9	155.9
Foreign liabilities (US$ millions)	-30.9	-60.2	-67.5	-73.1	-51.7	-42.3	-42.3	-42.3	-42.3	-42.3	-42.3	-42.3
Foreign currency deposits(US$ millions)	251.6	289.3	311.7	272.3	266.2	279.2	...	...	...	...	...	...
Nominal GDP (billions of Kwacha)	4,654	4,783	4,915	5,054	5,187	5,353	5,523	5,702	5,830	6,022	6,216	6,466

Sources: Reserve Bank of Malawi; and IMF staff projections.

Table 4a. Malawi: Balance of Payments, 2017–24

(Millions of USD, unless otherwise indicated)

	2017	2018		2019		2020	2021	2022	2023	2024
	Est.	1st.	Est.	1st.	Proj.	Proj.				
Current account balance[1]	-1,388.8	-637.0	-1,418.6	-553.3	-1,442.8	-1,426.6	-1,480.6	-1,471.2	-1,494.4	-1,509.3
Merchandise trade balance	-1,556.5	-590.9	-1,663.5	-605.3	-1,732.5	-1,802.5	-1,890.8	-1,910.9	-1,966.2	-2,036.5
Exports	896.5	1,701.9	929.8	1,813.8	1,038.3	1,144.6	1,239.3	1,343.1	1,454.2	1,577.9
Of which: Tobacco	486.1	586.3	426.4	621.3	422.0	444.2	467.5	492.1	519.0	548.5
Imports	-2,452.9	-2,292.8	-2,593.3	-2,419.1	-2,770.8	-2,947.1	-3,130.1	-3,254.1	-3,420.4	-3,614.5
Of which: Petroleum products	-306.1	-446.5	-342.6	-477.9	-342.1	-341.4	-355.7	-378.5	-408.7	-445.1
Project related	-207.1	-152.8	-131.5	-201.6	-184.2	-189.3	-225.2	-249.9	-277.1	-294.0
Services balance	-299.0	-408.0	-315.4	-410.7	-317.8	-291.7	-312.6	-319.6	-329.7	-316.5
Interest public sector	-13.7	-21.6	-10.1	-19.8	-18.9	-20.0	-20.9	-22.2	-23.8	-25.2
Other factor payments (net)	-139.5	-126.4	-153.9	-131.5	-161.0	-169.3	-178.8	-189.6	-202.0	-215.3
Nonfactor (net)	-145.8	-260.1	-151.4	-259.5	-137.9	-102.4	-112.8	-107.7	-103.9	-76.0
Receipts	156.9	142.0	182.4	167.7	200.6	220.8	242.9	267.5	294.9	324.1
Payments	-302.6	-402.1	-333.8	-427.2	-338.5	-323.2	-355.8	-375.2	-398.8	-400.1
Unrequited transfers (net)	466.6	362.0	560.3	462.7	607.5	667.6	722.8	759.3	801.6	843.7
Private (net)	451.4	362.8	561.4	388.1	608.6	668.7	723.9	760.4	802.7	844.9
Official (net)	15.2	-0.8	-1.1	74.6	-1.1	-1.1	-1.1	-1.1	-1.2	-1.2
Receipts	16.1	0.0	0.0	75.5	0.0	0.0	0.0	0.0	0.0	0.0
Budget support	16.1	0.0	0.0	75.5	0.0	0.0	0.0	0.0	0.0	0.0
Payments	-1.0	-0.8	-1.1	-0.8	-1.1	-1.1	-1.1	-1.1	-1.2	-1.2
Capital account balance	317.5	282.8	263.5	346.9	326.0	399.5	457.8	504.7	549.9	578.8
Project and dedicated grants	188.9	121.8	92.4	169.7	112.4	161.5	199.0	230.0	259.2	262.1
Off-budget project support[2]	128.5	161.0	171.1	177.2	213.7	238.0	258.9	274.7	290.7	316.7
Financial account balance	380.1	285.6	789.5	288.6	1,035.8	1,160.2	1,183.5	1,114.3	1,117.9	1,111.0
Medium- and long-term flows (net)	207.5	43.9	76.7	98.8	86.5	79.4	98.7	99.3	108.7	128.7
Disbursements	239.9	117.9	127.0	149.6	137.8	133.1	157.0	164.9	178.8	203.4
Budget support and other program loans	86.1	3.0	3.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project support loans	129.7	113.3	109.8	140.5	131.0	124.6	147.5	154.4	167.1	190.2
Other medium-term loans	24.1	1.7	14.2	9.1	6.9	8.5	9.6	10.5	11.7	13.1
Amortization	-32.5	-74.0	-50.3	-50.9	-51.4	-53.7	-58.4	-65.6	-70.1	-74.7
SDR allocation	5.3	-1.0	-2.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Foreign direct investment and other inflows	131.5	134.6	134.6	153.3	178.9	224.3	267.7	315.8	369.0	415.1
Short-term capital and other inflows	48.3	n.a.	469.8	36.6	804.2	856.5	817.1	699.3	640.2	567.2
Commercial banks net foreign assets	-7.2	45.9	108.3	0.0	-33.8	0.0	0.0	0.0	0.0	0.0
Errors and omissions	815.8	0.0	354.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	129.9	-69.7	-12.7	82.2	-80.9	133.0	160.8	147.8	173.5	180.5
Financing	-129.9	69.7	12.7	-82.2	-12.8	-164.0	-160.8	-147.8	-173.5	-180.5
Gross reserves (- increase)	-152.9	62.6	7.8	-95.4	-26.9	-173.0	-147.1	-107.3	-137.8	-146.6
Liabilities	23.1	7.1	4.9	13.2	14.2	8.9	-13.7	-40.6	-35.7	-33.8
Of which: IMF (net)	4.8	2.6	31.4	14.7	14.5	12.0	-10.3	-37.1	-32.6	-33.8
Purchases/drawings	26.6	31.5	31.4	31.4	31.0	31.3	15.8	0.0	0.0	0.0
Repurchases/repayments	21.8	29.0	0.0	16.7	16.5	19.3	26.1	37.1	32.6	33.8
Financing gap	0.0	0.0	0.0	0.0	93.7	31.0	0.0	0.0	0.0	0.0
Of which: IMF ECF Augmentation	…	…	…	…	12.9	26.0	…	…	…	…
World Bank	…	…	…	…	70.0	0.0	…	…	…	…
Others	…	…	…	…	10.0	5.0	…	…	…	…
Memorandum items:										
Gross official reserves	757.9	695.3	750.1	790.7	777.0	950.0	1,097.1	1,204.4	1,342.2	1,488.8
Months of imports[3]	3.1	2.9	2.9	3.2	2.9	3.3	3.6	3.8	4.0	4.1
Net International Reserves	533.9	428.6	486.2	510.8	486.7	624.7	785.5	933.4	1,106.8	1,287.3
Current account balance (percent of GDP)										
Excluding official transfers	-22.5	-9.3	-20.5	-8.7	-18.9	-17.2	-16.8	-15.7	-14.8	-14.0
Excluding project related imports	-19.0	-7.1	-18.6	-4.8	-16.5	-14.9	-14.3	-13.0	-12.1	-11.3
Excluding official transfers and project related imports	-19.2	-7.1	-18.6	-5.9	-16.5	-14.9	-14.3	-13.0	-12.1	-11.2
Import price index (2005 = 100)	115.1	126.8	123.3	127.6	122.0	120.8	120.8	121.3	122.2	123.8
Import volume (percent change)	6.3	-5.4	-2.0	4.9	8.0	7.4	6.1	3.6	4.4	4.3
REER (percent change)	4.5	…	7.6	…	…	…	…	…	…	…
Terms of trade (percent change)	-2.0	-4.1	-6.2	-0.9	2.4	0.5	0.6	0.0	-0.7	-1.2
Nominal GDP (millions of U.S. dollars)	6,230.0	6,820	6,902.4	7,257	7,635.7	8,289.7	8,787.2	9,379.5	10,070.4	10,797.5

Sources: Malawian authorities; and IMF staff estimates and projections.

[1] Based on the findings of recent technical support missions, confirming the reliability of the trade data produced by the Malawi National Statistics Office (NSO), the IMF has now adpoted the NSO's current account data. Previously, the series reported by the IMF was based on staff estimates. Errors and omissions were adjusted by large offsetting amounts, leaving the overall balance unchanged for historical data. Errors and omissions are projected at zero and short-term capital and other inflows projections are adjusted in the financial account. Future TA missions on capital and financial accounts' statistics will seek to better identify the offsetting flows to the current account adjustment.

[2] Includes estimate for project grants not channeled through the budget.

[3] In months of imports of goods and nonfactor services in the following year.

Table 4b. Malawi: Balance of Payments, 2017–24

(Percent of GDP)

	2017	2018		2019		2020	2021	2022	2023	2024
	Est.	1st.	Est.	1st.	Proj.			Proj.		
Current account balance[1]	-22.3	-9.3	-20.6	-7.6	-18.9	-17.2	-16.8	-15.7	-14.8	-14.0
Merchandise trade balance	-25.0	-8.7	-24.1	-8.3	-22.7	-21.7	-21.5	-20.4	-19.5	-18.9
Exports	14.4	25.0	13.5	25.0	13.6	13.8	14.1	14.3	14.4	14.6
Of which: Tobacco	7.8	8.6	6.2	8.6	5.5	5.4	5.3	5.2	5.2	5.1
Imports	-39.4	-33.6	-37.6	-33.3	-36.3	-35.6	-35.6	-34.7	-34.0	-33.5
Of which: Petroleum products	-4.9	-6.5	-5.0	-6.6	-4.5	-4.1	-4.0	-4.0	-4.1	-4.1
Project related	-3.3	-2.2	-1.9	-2.8	-2.4	-2.3	-2.6	-2.7	-2.8	-2.7
Services balance	-4.8	-6.0	-4.6	-5.7	-4.2	-3.5	-3.6	-3.4	-3.3	-2.9
Interest public sector (net)	-0.2	-0.3	-0.1	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Other factor payments (net)	-2.2	-1.9	-2.2	-1.8	-2.1	-2.0	-2.0	-2.0	-2.0	-2.0
Nonfactor (net)	-2.3	-3.8	-2.2	-3.6	-1.8	-1.2	-1.3	-1.1	-1.0	-0.7
Receipts	2.5	2.1	2.6	2.3	2.6	2.7	2.8	2.9	2.9	3.0
Payments	-4.9	-5.9	-4.8	-5.9	-4.4	-3.9	-4.0	-4.0	-4.0	-3.7
Unrequited transfers (net)	7.5	5.3	8.1	6.4	8.0	8.1	8.2	8.1	8.0	7.8
Private (net)	7.2	5.3	8.1	5.3	8.0	8.1	8.2	8.1	8.0	7.8
Official (net)	0.2	0.0	0.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Receipts	0.3	0.0	0.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Budget support	0.3	0.0	0.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Payments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital account balance	5.1	4.1	3.8	4.8	4.3	4.8	5.2	5.4	5.5	5.4
Project and dedicated grants	3.0	1.8	1.3	2.3	1.5	1.9	2.3	2.5	2.6	2.4
Off-budget project support[2]	2.1	2.4	2.5	2.4	2.8	2.9	2.9	2.9	2.9	2.9
Financial account balance	6.1	4.2	11.4	4.0	13.6	14.0	13.5	11.9	11.1	10.3
Medium- and long-term flows (net)	3.3	0.6	1.1	1.4	1.1	1.0	1.1	1.1	1.1	1.2
Disbursements	3.9	1.7	1.8	2.1	1.8	1.6	1.8	1.8	1.8	1.9
Budget support and other program loans	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project support loans	2.1	1.7	1.6	1.9	1.7	1.5	1.7	1.6	1.7	1.8
Other medium-term loans	0.4	0.0	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Amortization	-0.5	-1.1	-0.7	-0.7	-0.7	-0.6	-0.7	-0.7	-0.7	-0.7
SDR allocation	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign direct investment and other inflows	2.1	2.0	2.0	2.1	2.3	2.7	3.0	3.4	3.7	3.8
Short-term capital and other inflows	0.8	0.7	6.8	0.5	10.5	10.3	9.3	7.5	6.4	5.3
Commercial banks net foreign assets	-0.1	0.9	1.6	0.0	-0.4	0.0	0.0	0.0	0.0	0.0
Errors and omissions	13.1	0.0	5.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	2.1	-1.0	-0.2	1.1	-1.1	1.6	1.8	1.6	1.7	1.7
Financing	-2.1	1.0	0.2	-1.1	-0.2	-2.0	-1.8	-1.6	-1.7	-1.7
Gross reserves (- increase)	-2.5	0.9	0.1	-1.3	-0.4	-2.1	-1.7	-1.1	-1.4	-1.4
Liabilities	0.4	0.1	0.1	0.2	0.2	0.1	-0.2	-0.4	-0.4	-0.3
Of which: IMF (net)	0.1	0.0	0.5	0.2	0.2	0.1	-0.1	-0.4	-0.3	-0.3
Purchases/drawings	0.4	0.5	0.5	0.4	0.4	0.4	0.2	0.0	0.0	0.0
Repurchases/repayments	0.3	0.4	0.0	0.2	0.2	0.2	0.3	0.4	0.3	0.3
Financing gap	0.0	0.0	0.0	0.0	1.2	0.4	0.0	0.0	0.0	0.0
World Bank	...	...	...	...	0.9	0.0	...	...	...	...
Others	...	...	...	...	0.1	0.1	...	...	...	...
Memorandum items:										
Gross official reserves	12.2	10.2	10.9	10.9	10.2	11.5	12.5	12.8	13.3	13.8
Months of imports[3]	3.1	2.9	2.9	3.2	2.9	3.3	3.6	3.8	4.0	4.1
Current account balance (percent of GDP)										
Excluding official transfers	-22.5	-9.3	-20.5	-8.7	-18.9	-17.2	-16.8	-15.7	-14.8	-14.0
Excluding project related imports	-19.0	-7.1	-18.6	-4.8	-16.5	-14.9	-14.3	-13.0	-12.1	-11.3
Excluding official transfers and project related imports	-19.2	-7.1	-18.6	-5.9	-16.5	-14.9	-14.3	-13.0	-12.1	-11.2
Value of exports of GNFs (percent change)	-10.7	10.6	5.6	7.5	11.4	10.2	8.6	8.7	8.6	8.7
Value of imports of GNFs (percent change)	13.0	4.0	6.2	5.6	6.2	5.2	6.6	4.1	5.2	5.1

Sources: Malawian authorities; and IMF staff estimates and projections.

[1] Based on the findings of recent technical support missions, confirming the reliability of the trade data produced by the Malawi National Statistics Office (NSO), the IMF has now adpoted the NSO's current account data. Previously, the series reported by the IMF was based on staff estimates. Errors and omissions were adjusted by large offsetting amounts, leaving the overall balance unchanged for historical data. Errors and omissions are projected at zero and short-term capital and other inflows projections are adjusted in the financial account. Future TA missions on capital and financial accounts' statistics will seek to better identify the offsetting flows to the current account adjustment.

[2] Includes estimate for project grants not channeled through the budget.

[3] In months of imports of goods and nonfactor services in the following year.

Table 5. Malawi: Selected Banking Soundness Indicators, 2013–19

Key ratios	Dec-13	Dec-14	Dec-15	Dec-16	Dec-17	Dec-18	Jan-19	Mar-19	Jun-19	Jul-19
Capital Adequacy										
1. Regulatory Tier 1 capital to risk weighted assets	16.2	13.5	12.4	13.8	15.3	15.5	16.9	17.2	16.4	16.2
2. Regulatory total capital to risk weighted assets	19.1	17.1	15.8	17.0	19.4	19.0	20.2	20.7	20.4	20.1
3. Total capital to total assets	15.4	17.6	17.1	16.7	15.9	14.7	15.6	16.4	16.2	16.4
Asset composition and quality										
1. Non-performing loans to gross loans and advances	15.4	14.9	10.6	17.0	15.7	6.1	6.2	6.1	4.8	4.5
2. Provisions to non-performing loans	29.1	31.8	25.7	25.5	34.5	42.4	46.0	48.7	55.0	54.4
3. Total loans and advances to total assets	40.5	40.3	40.0	34.8	28.06	30.5	29.5	30.3	32.6	34.9
4. Foreign currency loans to total loans and advances	13.5	19.1	28.6	21.8	27.9	24.3	26.9	16.9	23.4	20.9
Earnings and profitability										
1. Return on assets (ROA)	4.8	4.0	3.1	2.7	2.3	2.2	1.8	1.9	2.8	2.8
2. Return on equity (ROE)	37.5	26.8	19.2	18.4	15.7	16.6	14.3	14.6	21.2	21.3
3. Non-interest expenses to gross income	39.7	45.4	51.4	50.0	49.7	52.1	54.0	53.0	52.0	51.8
4. Interest margin to gross income	39.7	---	50.2	47.8	50.8	46.5	46.1	51.1	50.2	49.6
5. Non-Interest Income to Revenue	31.8	37.8	30.5	28.0	27.3	34.2	31.5	29.0	32.6	33.0
6. Net Interest Income to Assets	9.1	8.4	9.7	9.7	8.7	7.9	0.7	2.1	4.4	5.2
7. Personnel expenses to non-interest expenses	45.4	45.1	45.3	43.8	46.5	42.9	44.9	44.1	43.9	44.0
Liquidity										
1. Liquid assets to deposits and short-term liabilities	59.1	62.4	59.0	72.3	77.0	63.3	64.8	60.7	59.1	56.4
2. Total loans to total deposits	56.6	58.3	58.5	54.2	45.1	47.4	46.6	46.9	51.0	54.5
3. Liquid Assets to total assets	43.7	48.8	43.3	50.4	55.0	44.8	46.1	42.2	41.7	39.6
4. Foreign exchange liabilities to total liabilities	26.3	---	26.1	19.7	19.8	13.8	17.6	26.1	18.7	19.1

Source: Reserve Bank of Malawi.

Table 6. Malawi: External Financing Requirement and Source, 2017–24

(Millions of USD)

	2017	2018	2019	2020	2021	2022	2023	2024
Total requirement	-1589	-1460	-1520	-1652	-1685	-1643	-1701	-1729
Current account, excluding official transfers	-1404	-1418	-1442	-1426	-1479	-1470	-1493	-1508
Debt amortization	-32	-50	-51	-54	-58	-66	-70	-75
Gross reserves accumulation (- increase)	-153	8	-27	-173	-147	-107	-138	-147
Total sources	1589	1460	1520	1652	1685	1643	1701	1729
Expected disbursements (official)	573	389	544	536	614	668	728	781
Grants	333	262	406	403	457	504	549	578
Medium- and long-term loans	240	127	138	133	157	165	179	203
Private sector (net)	1007	1041	949	1078	1082	1012	1006	982
IMF (net)	5	31	27	38	-10	-37	-33	-34
Drawings	27	31	44	57	16	0	0	0
Repayments	22	0	16	19	26	37	33	34
Financing gap	0	0	0	0	0	0	0	0
Gross official reserves	758	750	777	950	1097	1204	1342	1489
Months of imports	3.1	2.9	2.9	3.3	3.6	3.8	4.0	4.1

Source: IMF staff estimates.

Table 7. Malawi: Schedule of Disbursements Under ECF Arrangement, 2018–21[1]

(Millions of SDR)

Amount	% of Quota[2]	Availability date	Conditions Necessary for Disbursement[3]	Status
11.15	8.033	April 30, 2018	Executive Board Approval of Three Year ECF arrangement.	Disbursed
11.15	8.033	October 15, 2018	Observance of performance criteria for June 30, 2018 and completion of first review.	Disbursed
11.15	8.033	October 15, 2019	Observance of performance criteria for December 31, 2018, and completion of second review.	
20.40	14.697	October 15, 2019	Observance of performance criteria for June 30, 2019, and completion of third review.	
20.40	14.697	April 15, 2020	Observance of performance criteria for December 31, 2019, and completion of fourth review.	
20.41	14.705	October 15, 2020	Observance of performance criteria for June 30, 2020, and completion of fifth review.	
11.175	8.051	April 15, 2021	Observance of performance criteria for December 31, 2020, and completion of the sixth review.	
105.835	**76.250**	**Total for the ECF**		
Memorandum item:				
Malawi's Quota (in millions SDR)			138.80	

Source: IMF staff estimates.

[1] Includes proposed augmentation.

[2] Using Malawi's current quota after effectiveness of the 14th General Review of Quotas.

[3] Each review is also subject to obervance of standard continuous performance criteria.

Table 8. Malawi: Indicators of Capacity to Repay the Fund, 2019–32

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Projected Payments based on Existing Drawings:														
(SDR millions)														
Principal	3.3	13.8	18.44	25.81	22.37	23.11	20.51	13.78	6.41	3.35	0.00	0.00	0.00	0.00
Charges and interest	0.14	0.54	0.54	0.54	0.54	0.54	0.54	0.54	0.54	0.54	0.54	0.54	0.54	0.54
Projected Payments based on Prospective Drawings:														
(SDR millions)														
Principal	0	0	0	0	0	0	8.35	15.59	16.71	16.71	16.71	8.36	1.12	0.00
Charges and interest	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Projected Payments based on Existing and Prospective Drawings:														
SDR millions	3.44	14.34	18.98	26.35	22.91	23.65	29.40	29.91	23.66	20.60	17.25	8.90	1.66	0.54
US$ Millions	4.76	19.75	26.27	36.66	32.01	33.22	41.30	42.01	33.23	28.93	24.23	12.50	2.33	0.76
Percent of exports of goods and services	0.38	1.45	1.77	2.28	1.83	1.75	2.02	1.90	1.40	1.13	0.88	0.42	0.07	0.02
Percent of debt service	5.41	20.97	24.63	29.07	25.06	24.63	29.21	28.69	21.89	18.30	15.07	7.92	1.49	0.49
Percent of quota	2.48	10.33	13.67	18.98	16.51	17.04	21.18	21.55	17.05	14.84	12.43	6.41	1.20	0.39
Percent of gross official reserves	0.61	2.08	2.39	3.04	2.38	2.23	2.52	2.35	1.71	1.38	1.07	0.51	0.09	0.03
Percent of GDP	0.06	0.24	0.30	0.39	0.32	0.31	0.36	0.34	0.25	0.21	0.16	0.08	0.01	0.00
Projected Level of Credit Outstanding based on Existing and Prospective Drawings:														
SDR millions	179.1	206.1	198.9	173.1	150.7	127.6	98.7	69.4	46.2	26.2	9.5	1.1	0.0	0.0
US$ Millions	246.3	284.6	275.9	241.2	211.1	179.6	139.0	97.6	65.1	36.9	13.3	1.6	0.0	0.0
Percent of exports of goods and services	19.9	20.8	18.6	15.0	12.1	9.4	6.8	4.4	2.7	1.4	0.5	0.1	0.0	0.0
Percent of debt service	280.0	302.1	258.6	191.3	165.3	133.2	98.3	66.7	42.9	23.3	8.3	1.0	0.0	0.0
Percent of quota	129.0	148.5	143.3	124.7	108.6	91.9	71.1	50.0	33.3	18.9	6.8	0.8	0.0	0.0
Percent of gross official reserves	31.7	30.0	25.1	20.0	15.7	12.1	8.5	5.5	3.4	1.8	0.6	0.1	0.0	0.0
Percent of GDP	3.2	3.4	3.1	2.6	2.1	1.7	1.2	0.8	0.5	0.3	0.1	0.0	0.0	0.0
Memorandum items:														
Exports of goods and services (millions of U.S. dollars)	1,239	1,365	1,482	1,611	1,749	1,902	2,049	2,208	2,379	2,560	2,754	2,963	3,188	3,430
Debt service (millions of U.S. dollars)	88.0	94.2	106.7	126.1	127.7	134.9	141.4	146.4	151.8	158.1	160.8	157.8	156.2	155.6
Quota (SDR millions)	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8
Gross official reserves (millions of U.S. dollars)	777	950	1,097	1,204	1,342	1,489	1,636	1,787	1,943	2,098	2,260	2,462	2,653	2,849
GDP (millions of U.S. dollars)	7,636	8,290	8,787	9,380	10,070	10,798	11,552	12,306	13,127	13,985	14,922	15,912	16,945	18,097

Source: IMF staff projections.

Table 9. Malawi: Projected External Borrowing

(January 1, 2019–December 31, 2019)

PPG external debt contracted or guaranteed[1]	Volume of new debt (US$ million)	PV of new debt (US$ million)
Sources of debt financing		
Consessional debt, of which [2]	**124**	**60**
Multilateral debt	124	60
Bilateral debt	0	0
Non-concessional debt, of which [2]	**0**	**0**
Semi-concessional[3]	0	0
Commercial terms[4]	0	0
Use of debt financing		
Infrastructure	124	60
Budget Financng	0	0
Memo Items		
Indicative projections		
2020	59	30-38
2021	44	23-29

Source: IMF staff projections.

[1] Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate.

[2] Debt with a grant element of at least 35 percent.

[3] Debt with a positive grant element below 35 percent.

[4] Debt without a positive grant element. For commercial debt, the present value would be defined as the nominal/face value.

Table 10. Malawi: Quantitative Targets, 2018–20[1]

	Target type [2]	2018				2019								2020		
		End-Dec.				End-Mar.		End-Jun.				End-Sept	End-Dec.	End-Mar.	End-Jun.	End-Sept.
		Prog. (Country Report 18/336)	Adj. Prog.	Est.	Status	IT (Country Report 18/336)	Est.	Prog. (Country Report 18/336)	Adj. Prog.	Est.	Status	IT (Country Report 18/336)	Prog.	IT	Prog.	IT
I. Monetary targets (millions of kwacha)																
Reserve money (ceiling on stock) (upper bound)[3]	PC	326,115		298,112	Met	308,798	281,997	346,236		318,376	Met	340,175	324,219	318,529	343,225	362,598
Reserve money (ceiling on stock)[3]		316,617		289,429		299,804	273,784	336,151		309,103		330,267	314,776	309,251	333,228	352,037
Reserve money (ceiling on stock) (lower bound)[3]		307,118		280,746		290,810	265,570	326,067		299,830		320,359	305,333	299,974	323,231	341,476
II. Fiscal targets (millions of kwacha)																
Primary balance (floor)[5,6,11]	PC	-4,456	-3,770	-83,657	Not Met	-2,684	-168,145	89	7,657	-125,614	Not Met	-1,236	-101,537	-93,418	-48,574	-14,061
Domestic primary balance (floor)[4,6,11]	PC			-37,872			-92,565			-66,909			-42,339	-12,976	53,112	16,739
RBM financing of central government (ceiling)[6,7]	PC	0	93,710	25,418	Met	0	-150,228	0		0	Met	0	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0		0	Met	0	0	0		0	Met	0	0	0	0	0
Social spending (floor)[6,9]	IT	182,207		208,717	Met	273,310	318,515	364,413		406,385	Met	103,104	229,991	350,619	449,469	126,966
III. External sector targets (US$ millions, unless otherwise indicated)																
Net international reserves of the RBM (floor)[5,8]	PC	428.6	429.5	486.2	Met	436.6	503.0	460.4	470.8	487.8	Met	473.1	486.7	523.4	557.0	597.2
Accumulation of external payments arrears (ceiling)[6,10]	PC	0		0	Met	0	0	0		0	Met	0	0	0	0	0
Contracting or guaranteeing of non-concessional external debt (ceiling)[6,10]	PC	0		0	Met	0	0	0		0	Met	0	0	0	0	0
Net foreign borrowing of the central government (ceiling)[6]	IT									77.3			48.9	61.0	72.8	25.7
Memorandum items:																
Net foreign assets of the RBM (US$ millions, end of period)[6]		316.0		428.4		324.0	444.2	347.8		422.9		360.4	373.8	410.5	444.1	484.3
Budget support (US$ millions)[6]		0.0		0.0		0.0	0.0	0.0		40.8		0.0	0.0	0.0	0.0	0.0
Budget support (millions of kwacha)[6]		0.0		0.0		0.0	0.0	0.0		30,704.7		0.0	0.0	0.0	0.0	0.0
Limits on disbursements of foreign concessional contracted and guaranteed loans (US$ millions)[6]		53		62		79	103	105.1		121.3		49.4	79.0	106.9	134.4	39.2
Debt service payments to the World Bank and AfDB (US$ millions)[6]		19.8		7.3		24.9	12.8	30.1		21.6		5.2	3.2	5.4	5.4	5.4
Debt service payments to the World Bank and AfDB (millions of kwacha)[6]		14,680		5,374		18,842	9,400	23,137		16,241		4,041	2,414	4,107	4,176	4,245
Joint Fund on Health receipts (millions of kwacha)[6]		4,577		4,577		6,865	6,865	9,153		9,153		1,831	3,661	5,492	7,323	
Joint Fund on Education receipts (millions of kwacha)[6]		8,656		8,656		12,983	12,983	17,311		17,311		2,000	4,000	6,000	8,000	
Program exchange rate (kwacha per US$)		732		732		732	732	732		732		732	732	732	732	732

Source: IMF staff projections.

[1] Targets are defined in the technical memorandum of understanding (TMU).

[2] "PC" means Performance Criterion and "IT" means Indicative Target. The PC test date for the 2nd Review is end-December 2018 and for the 3rd Review is end-June 2019. Test dates for future reviews will be end-June and end-December. End-September and end-March targets are ITs.

[3] PC applies to upper bound only. See TMU for details.

[4] Targets are subject to an adjustor for budget support, as specified in the TMU.

[5] Targets are subject to an adjustor for budget support and debt service payments and donor-funded social sector expenditures, as specified in the TMU.

[6] Defined as a cumulative flow, starting from the beginning of the fiscal year.

[7] Targets are subject to an adjuster equivalent to 10 percent of the average of the inflation adjusted domestic revenues of the previous three fiscal years, as specified in the TMU.

[8] Defined as stocks.

[9] Priority social spending as defined in the TMU and quantified in the authorities' budget.

[10] Evaluated on a continuous basis.

[11] The domestic primary balance will replace the primary balance as a PC, beginning with the end-December 2019 PC.

Table 11a. Malawi: Structural Benchmarks, 2018–19

Structural benchmark	Target date	Macro Rationale	Status	
			End-December 2018	End-June 2019
Nominal GDP (billions of Kwacha)				
Submission to the MoF of five reports by the MDAs[1] by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted and published 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance.	Continuous (monthly from May 15, 2018)	Improve fiscal transparency; prevent accumulation of new domestic arrears; reduce vulnerabilities to corruption.	Not Met *Implemented with Delay*	Met
Maintain a transparent commitment control system for all MDAs; MoF to centrally compile consolidated commitments of the government by end of the following month and place it on the MoF website. Classify bills overdue for more than 90 days by age. ST to apply sanctions to the controlling officers of the MDAs for incurring arrears without the approval of the Minister of Finance.	Continuous (monthly from May 31, 2018)	Better control on all government commitments and arrears, if any.	Met	Met
Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within six months after the end of each quarter in the first year and within 90 days after the end of each quarter in following years. The financial reports should be certified by the Auditor General.	Continuous (quarterly from March 31, 2019)	Improve fiscal transparency and integrity of the accounting system; routinize reconciliation of all bank accounts; strengthen cash planning; reduce vulnerabilities to corruption.	N/A	Not Met *Implemented with Delay*
Reconcile all bank accounts MG1 and six operating accounts (except salary accounts until September 2019) and ways and means transactions within 90 days after the end of each month signed by the Accountant General and Secretary to the Treasury. The reconciliation should clear all the backlog and have a track record of three consecutive months.	Continuous (monthly from July 29, 2018)	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.	Not Met *Implemented with Delay*	Not Met *Implemented with Delay*
Reconcile all debt data between the MOF and RBM.	Continuous (monthly from April 30, 2018)	Enhance debt management; improve transparency and monitoring of public debt.	Not Met *Implemented with Delay*	Not Met *Implemented with Delay*
CMU undertakes variance analysis on forecasting errors every three months, reports a summary of minutes of the meeting, and takes actions to improve MDA submissions.	End-December 2018	Strengthen cash and debt management; timely implementation of the budget; reduce vulnerabilities to corruption.	Met	N/A
Finalize and issue the draft regulations, policies and guidelines covering issues of ownership, payment of dividend and surplus, and preparation of PMPBs.[2]	End-December 2018	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.	Not Met *Implemented Except Dividend Policy*	N/A
Pilot ex-post reviews/performance audits of some major capital projects in collaboration with the NAO.	End-June 2019	Improve efficiency of public investment.	N/A	Not Met Two of three project reviews completed.
Submit to Parliament a report on the pilot audit of the main public corporations in collaboration with the NAO.	End-June 2019	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.	N/A	Not Met *Implemented with Delay*
Move from monthly to quarterly budget release (set in a conservative manner), and allow MDAs to commit, through IFMIS, up to the released budget.	End-June 2019	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; and achieve comprehensive coverage in IFMIS.	N/A	Not Met
Bring all TSA sub-accounts into IFMIS including projects, receipts and payments.	End-June 2019	Enhance cash management; achieve comprehensive coverage in IFMIS; and strengthen controls on bank reconciliation and reporting; reduce vulnerabilities to corruption.	N/A	Met
Use IFMIS to record commitments or all types of expenditure (based on purchase orders or contracts) prior to the submission of new contracts to the ST for vetting (includes linking HRMS and IFMIS) and all domestic debt commitments, expenditures, and payments in real time. Disclose on the MoF website information on (i) accumulated commitments against the budget allocation and (ii) outstanding bills classified by age, on a monthly basis, 30 days after the reference period.	End-August 2019	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption.	N/A	Not Met
Audit of the Public-Sector Investment Program (PSIP) database, including the efficiency and timeliness of its processes, and its coverage.	End-December 2019	Improve efficiency of public investment.	N/A	Met
Financial sector				
Develop a strategy to pace the unwinding of RBM holdings of government securities that minimizes adverse effects on public debt management and monetary policy implementation.	End-September 2019	Improve debt management and governance.	N/A	Met

Sources: IMF staff and Malawian authorities.
[1] Ministry, department, and agency.
[2] Performace mangement plan and budget.

Table 11b. Malawi: Structural Benchmarks, 2019–20

Structural benchmark	Target date	Macro Rationale
Public financial management		
Submission to the MoF of five reports by the MDAs[1] by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance.	Continuous (monthly from May 15, 2018)	Improve fiscal transparency; prevent accumulation of new domestic arrears; reduce vulnerabilities to corruption.
Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within four months after the end of each quarter in FY 2019/20 and within 90 days after the end of each quarter in following years. The financial reports should be certified by the Auditor General.	Continuous (quarterly from March 31, 2019)	Improve fiscal transparency and integrity of the accounting system; routinize reconciliation of all bank accounts; strengthen cash planning; reduce vulnerabilities to corruption.
Reconcile all debt data between the MOF and RBM.	Continuous (monthly from April 30, 2018)	Enhance debt management; improve transparency and monitoring of public debt.
Cabinet approval of the dividend policy relating to SOEs.	End-December 2019	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Ensure DAD front office operations include more active engagement in domestic debt management policies and operations in collaboration with the RBM.	End-December 2019	Enhance debt management; improve transparency and monitoring of public debt.
Submit to Parliament and publish on the MoFEPD website a consolidated annual report on SOEs (including case studies for ENGENCO, NOCMA, ADMARC, and Blantyre Water Board).	End-March 2020	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Develop a domestic revenue mobilization strategy.	End-March 2020	Increase domestic revenues in an efficient and equitable manner.
EFT adoption and TMS implementation (five pool bank accounts) facilitating the move toward automated monthly reconciliation of all bank accounts. TMS implementation of two accounts will be targeted for end-2019 and the remaing three for end-March 2020.	End-June 2020	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.
Financial sector		
Develop a roadmap for increasing access to finance.	End-December 2019	Increase financial sector intermediation.
The research department of the RBM will review and prepare a report on the obstacles to FX market development.	End-June 2020	Deepen the interbank FX market, improve market functioning, efficiency in intermediation with improved liquidity.

Sources: IMF staff and Malawian authorities.
[1] Ministry, department, and agency.

Annex I. Risk Assessment Matrix[1]

Source of Risk	Relative Likelihood in next 1–3 years	Impact if Realized	Policy advice[2]
Global Risks			
Rising protectionism and retreat from multilateralism.	**High**	**Medium** Escalated global trade tensions could depress export demand and raise import costs.	Increase exchange rate flexibility to absorb shocks, strengthen FX reserve buffer to facilitate adjustment, and step-up structural reforms to support economic diversification and competitiveness.
Weakening demand in key partner economies.	**Medium/High**	**Medium** Weak external demand dampens exports and donor financing, depressing real GDP growth.	Adopt policies to increase fiscal space to respond to contingences, tighten monetary policy and increase exchange rate flexibility to absorb shocks, strengthen FX reserve buffer to facilitate adjustment, and continue efforts to diversify the export base.
Sharp rise in risk premia and increased financial vulnerability.	**High**	**Medium** Sharp rise in funding costs reduce financial flows, raise debt service costs and refinancing risks, elevates inflationary pressures and undermines growth prospects. Build-up of financial vulnerability encouraged by lose monetary policy and excessive risk-taking could reduce resilience to external shocks.	Keep fiscal discipline and ensure monetary policy is consistent with growth and inflation objectives, maintain adequate foreign reserves, and smooth short-term exchange rate volatility.
Energy price volatility.	**Medium**	**Medium** Energy price fluctuations stemming from supply and demand shocks can add to balance of payments pressures and increased domestic production costs.	Tighten monetary policy, increase exchange rate flexibility, strengthen FX reserve buffer, gradually adjust electricity prices to reflect market prices, apply the automatic fuel price adjustment mechanism and replenish the fuel price stabilization fund to ensure adequate energy supplies and contain additional fiscal cost/contingent liabilities.
Higher frequency and severity of natural disasters.	**Medium**	**High** Frequent natural disasters can hamper production capacity, impose additional burden on public debt and cause severe economic damage.	Improve infrastructure quality, invest in modernizing disaster reduction measures, relocate people from vulnerable areas, allow fiscal buffer for future disasters and secure multiple trade corridors.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline scenario path, which is most likely to materialize in the view of IMF staff. The Relative Likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline scenario.
[2] The policy response suggested by Fund staff assumes all other circumstances remain unchanged.
For a combination of shocks, policy responses would need to be modified to avoid conflicts.

Regional and Domestic Risks			
Expansionary fiscal policies.	**High**	**High** Domestic borrowing for unduly high fiscal deficits leads to inflationary pressures, crowding out the private sector; there is a risk of reemergence of payment arrears.	Pursue restrictive fiscal policies, adopt corrective measures to limit spending, exert an effective commitment control system, and increase revenue mobilization.
Delayed PFM reforms and lacking expenditure control.	**High**	**High** Uneven progress of PFM reform and deficient expenditure control undermine confidence in budgetary processes and efforts to effectively and transparently manage expenditure.	Accelerate implementation of PFM reform programs, strengthen corruption control, and communicate regularly and transparently.
Slow growth.	**Medium**	**High** Insufficient jobs for new entrants into the labor market, given Malawi's fast-growing population, would result in higher unemployment rates.	Step-up structural reforms to support economic diversification and competitiveness, access to finance, and resilience to climate change.
Excessive external borrowing.	**Medium**	**High** Implementing an over-ambitious capital investment program, especially, if financed with non-concessional external loans, debilitates the precarious medium to long-term debt sustainability position.	Elaborate a prudent and well appraised public investment program, secure concessional financing, and assess the impact of borrowing on debt sustainability.
Deficient conduct of monetary policy.	**Medium**	**Medium** Conflicting signals on policy intentions confuse market participants' confidence.	Continue improving the communication of monetary policy and adopt a clear and effective monetary operational framework.
Deteriorating financial stability.	**Medium**	**Medium** Increasing non-performing loans and deteriorating financial positions threaten financial sector stability.	Strengthen banking supervision and inspection to contain emerging risks by developing early warning systems and countervailing measures, eliminate domestic arrears accumulation.

Appendix I. Letter of Intent

November 1, 2019

Madame Georgieva
Managing Director
International Monetary Fund
700, 19th Street, N.W.
Washington, D.C. 20431
United States

Dear Madame Georgieva:

1. On November 21, 2018, the Executive Board of the International Monetary Fund (IMF) completed the first review under the three-year Extended Credit Facility (ECF) arrangement for Malawi. This letter and the attached Memorandum of Economic and Financial Policies (MEFP) report on recent economic developments and performance under the ECF arrangement since that time as well as on the policies we plan to implement during FY 2019/20 and over the medium term.

2. We have made solid progress towards our program objectives under the ECF, notwithstanding continued challenges from climate shocks—including devastating flooding from Cyclone Idai in March 2019—power shortages, and election-driven spending pressures.

3. All but one continuous as well as end-December 2018 and end-June 2019 quantitative performance criteria (QPC) were met. The QPC on the primary fiscal balance target (adjusted for deviations in budget support, dedicated grants, and debt service payments relative to the first review under the ECF) was missed in December 2018 due to front-loading of planned spending for the year; and it was missed in June 2019 primarily due to (i) shortfalls in tax revenues (reflecting the slowdown in businesses affected by the cyclone, election uncertainties, and demonstrations) (ii) lower than anticipated dividends (iii) unexpected goods and services spending to support post-cyclone disaster relief, increased spending to ensure safety during elections and post-election demonstrations; and (iv) spending pressures ahead of the elections which resulted in bringing forward domestic development projects planned for FY 2019/20 and raising investment in rural electrification. Strong remedial actions are being taken. Notwithstanding, significant spending needs for post-cyclone reconstruction and for ensuring safety during demonstrations and other political events, the FY 2019/20 stance will be tightened relative to FY 2018/19 (and remain broadly unchanged relative to the FY 2019/20 stance agreed at the time of the first review under the ECF). We are actively improving efficiency in tax and non-tax collection, project management and capacity as well as coordinating with donors to improve the accuracy of our information on donor flows.

4. Some structural benchmarks (SBs) were met on time. Most of the remaining end-December 2018 SBs were delayed due to unexpected capacity constraints and were completed by end-March 2019. Of the remaining end-June 2019 SBs, some were completed by end-March 2019 and most of the rest are expected to be complete by end-2019. The indicative targets (ITs) on social spending and on no new domestic arrears were met for both end-December 2018 and end-June 2019. Highlighting our commitment to improving project management and forecasting use of foreign project financing, the end-December 2019 structural benchmark on performing an audit of the Public-Sector Investment Program (PSIP) database was already completed in June 2019; and we have begun implementing the audit's recommendations.

5. We are actively entrenching macroeconomic stability and enhancing more inclusive and resilient growth, in line with the Malawi Growth and Development Strategy (MGDS) III and the policies agreed in our macroeconomic program supported by the ECF. Despite growing inflationary pressures, we have contained inflation to single digits. Economic growth is expected to accelerate from just above 3 percent in 2018 to around 4.5 percent in 2019 and to 6-7 percent over the medium term.

6. We are committed to maintaining debt sustainability while pursuing our ambitious infrastructure development plans. We will continue to ensure that new loans are concessional and accompanied by solid feasibility studies (by an independent third party when required for donor-funded projects) and that the macroeconomic implications (including on debt) are carefully considered.

7. Program implementation will be monitored through quantitative performance criteria, structural benchmarks and indicative targets as described in the Technical Memorandum of Understanding (TMU), Attachment II.

8. Based on the strength of the policies outlined in this letter and the MEFP and considering our performance under the program we request (i) waivers of non-observance for the QPC on the primary fiscal balance for end-December 2018 and end-June 2019; (ii) the introduction of a new QPC on the domestic primary balance to replace the existing QPC on the primary balance; (iii) modification of the end-December 2019 and end-June 2020 PCs on reserve money and net international reserves of the RBM; (iii) completion of the second and third reviews under the ECF; and (iv) an augmentation of access of 20 percent of quota under the ECF arrangement to support resilient reconstruction in the aftermath of Cyclone Idai.

9. We are confident that the policies contained in the attached MEFP are adequate to achieve the objectives of our program, but we will take any further measures that may be needed to attain these objectives. The Government of Malawi will consult with the Fund staff on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP, in accordance with Fund policies on such consultations. Malawi will provide the Fund staff with any information that may be necessary for monitoring the implementation of the measures to achieve program objectives.

10. The Government of Malawi authorizes the IMF to make this letter and the attached MEFP and TMU, as well as the related Staff Report available to the public, including through the IMF internet website.

Yours sincerely,

/s/	/s/
Hon. Joseph M. Mwanamvekha, M.P Minister of Finance, Economic Planning and Development	Dr. Dalitso Kabambe Governor of the Reserve Bank of Malawi

Attachments:

1. Memorandum on Economic and Financial Policies (MEFP)
2. Technical Memorandum of Understanding (TMU)

Attachment I. Memorandum of Economic and Financial Policies

November 1, 2019

I. RECENT ECONOMIC DEVELOPMENTS

1. **In March 2019, Tropical Cyclone Idai devastated southern Malawi.** Flooding from the cyclone took more than 60 lives, destroyed crops, homes, hospitals, schools, roads, and other critical infrastructure. Our Post-Disaster Needs Assessment estimates resilient reconstruction costs at 5 percent of GDP (about $370 million). We are grateful to our development partners for their assistance in providing immediate disaster relief and are now appealing for support in financing resilient reconstruction. To this end, the World Bank has disbursed $40 million of budget support and approved $50 million of project financing. We are requesting IMF assistance through an augmentation of access equivalent to 20 percent of quota.

2. **Moderate growth is expected for Malawi's economy despite the devastating impact of the cyclone.**

- The economy is expected to grow at 4.5 percent in 2019, up from 3.2 percent last year. The improvement reflects post-cyclone reconstruction and an agricultural rebound. Cyclone-related agricultural losses were more than compensated by bumper harvests in the rest of the country. As a result, agricultural production was significantly higher than in 2018, where widespread drought and insect infestations destroyed much of the agricultural output. Continued macroeconomic stability is supporting confidence. However, lower global tobacco demand hurt tobacco exports (our main export) and on-going electricity shortages continue to weigh on manufacturing and wholesale and retail trade.

- Inflation remains in single digits and on a declining trend. Non-food inflation fell from 8.2 percent at end-2018 and is expected to end 2019 around 5.7 percent, in part, reflecting improved inflation expectations following two years of single digit inflation. However, food prices remain elevated as the cyclone disrupted supply chains and suppliers stocking maize in case of future weather shocks. As a result, average headline inflation is expected at 9.1 percent in 2019—similar to the 2018 rate of 9.2 percent.

- The current account deficit persists in 2019. Cyclone Idai and slowing global demand for our key export weighed on exports while import needs remain high, including for post-cyclone reconstruction materials and election-related spending.

3. **Fiscal policy faced challenges in FY 2018/19.**

- At the time of the first review in November 2018, we had set a zero primary balance target for FY 2018/19 under the ECF arrangement, corresponding to an end-December 2018 target of -0.1 percent of GDP (performance criterion). By end-December 2018, the primary balance target (adjusted for deviations in budget support, dedicated grants, and debt service payments relative to the first review under the ECF) was missed by 1.5 percent of GDP primarily due to front-loading of planned spending for the year. However, by end-June 2019 the primary balance target (adjusted for shortfalls in grants) was missed by 2.5 percent of GDP due to (i) a shortfall in corporate income tax (0.6 percent of GDP) reflecting the slowdown in businesses affected by the cyclone, election uncertainties, and post-election demonstrations; (ii) weak dividend collection (0.4 percent of GDP); (iii) unexpected goods and services spending to support post-cyclone disaster relief and rehabilitation and increased spending to ensure safety during elections and post-election demonstrations (0.4 percent of GDP); (iv) raising salaries to settle strikes by university staff (0.1 percent of GDP); (v) payment of arrears arising from court rulings (0.1 percent of GDP); and (v) spending pressures ahead of the elections which resulted in bringing forward domestic development projects planned for FY 2019/20, implementing new ones, and raising investment in rural electrification (1.3 percent of GDP). However, foreign-financed development spending was less than anticipated (0.6 percent of GDP) reflecting shortfalls in grants (0.9 percent of GDP) that were only partially offset by increased project-based concessional foreign borrowing (0.2 percent of GDP). We did not incur any external payment arrears or contract or guarantee new non-concessional external debt (performance criteria).

- The domestically-financed portion of the fiscal deficit was financed by banks and non-banks and there was no net financing by the Reserve Bank of Malawi (RBM).

4. **We loosened monetary policy in line with reduced inflationary pressures.** After observing a trend decline in non-food inflation, reduced international fuel prices, and declines in average Treasury bill yields (for all tenors), the policy rate was reduced by 150 basis points in January and another 100 basis points in May to 13.5 percent. Given upward pressures on food prices, the policy rate has remained unchanged in the second half of the year. In January, the reserves requirements were reduced by 250 and 375 basis points to 5 and 3.75 percent on local currency and foreign currency deposits, respectively, and the Lombard rate by 310 basis points to 14.9 percent. The interbank rate immediately fell below the corridor's lower bound and was re-aligned with the policy rate in April when the system's excess liquidity was absorbed though commercial banks' purchase of government securities from the RBM and a pick-up in credit growth from 11.5 percent at end-2018 to 17.1 percent in June 2019. In September, the interbank rate fell below the corridor's lower bound due to lower uptake of government securities by the market. Efforts are being made to realign the interbank rate with the policy rate. The stock of reserve money for both end-December and end-June 2019 remained within the upper bound set under the ECF arrangement (performance criteria).

5. **For the first time in two years, the Kwacha fluctuated substantially against the US dollar.** A 6 percent depreciation in the second quarter of 2019—the largest since mid-2016—was followed by a 5.5 percent appreciation in the third quarter of 2019. While the net depreciation across the three quarters is small, it underlines our commitment to exchange rate flexibility which we consider critical for cushioning shocks and enhancing competitiveness. The real effective exchange

rate appreciated by around 13 percent over the past twelve months (August 2018-August 2019). Net international reserves overperformed its end-December 2018 and end-June 2019 targets (performance criteria) by $57 and $17 million, respectively.

6. **Banking system resilience continues to improve.** On aggregate, the banking system has been well capitalized and profitable. Over the past two years, non-performing loans (NPLs) have declined from 15.7 percent at end-2017 to 4.8 percent in June 2019, largely due to write offs and loan recovery and overall growth in bank lending. Over the same period, with the adoption of IFRS9 requirements, provisioning has increased from 34.5 to 54.4 percent. One small bank with a negative capital adequacy ratio was able to recapitalize and another loss-making bank is looking for a partner to inject capital and may otherwise exit the market. The RBM's June 2019 stress test showed that overall, the banking system is resilient to interest rate and income risk shocks but vulnerable to some credit and liquidity risk shocks.

II. ECONOMIC OUTLOOK AND POLICIES

A. Economic Outlook

7. **Economic growth is expected to strengthen to around 5 percent in 2020 and towards 6.5 percent over the medium.** In the near term, economic activity will be driven by post-cyclone reconstruction, investment in more climate-change resilient infrastructure, and improved electricity generation—from new electricity sources coming on line—which will support increased manufacturing and wholesale trade activity. Over the medium term, growth will be supported by greater access to finance, crop diversification (e.g., cassava and sweet potatoes), and more resilient infrastructure—including enhanced electricity generation and distribution, better quality and coverage of irrigation, and improved telecommunications and road networks. Combined with on-going stabilization, reform programs such as those to improve competitiveness and governance as well as increased investment will solidify confidence, spur economic diversification, and support higher and more sustained inclusive growth and increase job and business opportunities for our young and dynamic population. Inflation is expected to moderate to around 8.5 percent in 2020 with lower food and international fuel prices. Over the medium-term, it is expected to gradually converge to our objective of 5 percent in line with strong fiscal and monetary policy implementation and contained food and international fuel prices.

8. **Short-term risks are tilted to the downside.** Malawi's agriculture-driven economy is vulnerable to adverse weather conditions, which are being intensified by climate change, and to pest infestations. Food security should be preserved by the already accumulated substantial food reserves and we are closely monitoring the situation. Escalated global trade tensions could depress export demand and raise import costs. This combined with volatile tobacco exports could induce stress on the exchange rate. A slower than expected disinflation process could raise interest rates, increasing the government's interest bill and hampering access to finance. On the upside, better

than expected harvests and higher than expected export commodity prices could boost medium-term growth.

B. Monetary and Financial Sector Policies

9. **Monetary policy will continue focusing on entrenching disinflation**. It will aim to maintain single digit inflation in order to achieve the medium-term objective of 5 percent. Our monetary policy formulation and implementation will be consistent with this objective.

10. **We will complete the transition to an interest rate-based operational framework and aim to adopt inflation targeting over the medium-term**.

- As laid-out in the RBM's 2019-21 strategic plan, full-fledged inflation targeting continues to be our medium-term strategic objective, and we are committed to further improve our interest-rate based monetary policy framework. To this end, we will continue to improve primary and secondary market operations to further strengthen monetary policy transmission. With a view to strengthening the transmission mechanism along the yield curve, and in consultation with the market, we have modified the reference rate for base lending rates of commercial banks from the Lombard rate to the weighted average of the Lombard rate, the Interbank rate, all types of Treasury bill rates, and the savings rate. We will continue to monitor its implementation and review as and when necessary in consultation with the IMF. We will continue to expand capacity in developing high frequency data, liquidity forecasting, and the forecasting and policy analysis system (FPAS) modeling.

- In line with a favorable economic outlook, the RBM adjusted downwards the policy rate, the liquidity reserve requirements (LRR), and the Lombard rate in early-2019. Going forward, the RBM will continue to review the economic conditions and take necessary decisions consistent with the 5 percent medium-term inflation objective. This may include re-aligning the foreign currency LRR with the local currency LRR.

- We will take steps to further improve the government securities market. To avoid market distortions and sustain policy effectiveness, we will ensure that interest rates on all government securities continue to be determined through auctions. To deepen the secondary securities market, we will disclose volumes to be offered in auctions, avoid cancelation of auctions. We will improve on the planning for government security issuance by establishing an annual borrowing plan with updates as necessary and an issuance plan. The issuance calendar will include the volume of securities to be issued in each auction.

- While recognizing the urgency of stemming the cost of borrowing, we believe that the fundamental solution lies in addressing structural barriers: promoting mobile technology, managing risks and reducing the cost of doing business for banks, strengthening financial frameworks, and improving property rights. In view of this, we will develop a road map to improve access to finance by December 2019 (structural benchmark).

11. **We will continue to bolster the RBM's independence and effectiveness.**

- We have successfully repealed and replaced the RBM Act with a new RBM Act 2018 to enhance the mandate of the RBM—including its autonomy and eliminating avenues for monetary financing of the government debt by prohibiting it from purchasing government securities in the primary market and by limiting credit to the government to short-term advances that must be repaid in cash. The RBM will not convert ways and means cash advances to the government into government securities. We will also ensure that the revisions to the PFM Act, aimed at modernizing and strengthening the PFM legal framework, will be aligned with the amended RBM Act.

- The RBM's holdings of government securities have been reduced (by 12 percent since end-2017), mainly through sales in the secondary market, without any adverse effects on monetary policy implementation and public debt management. In particular, the RBM's share of the total stock of Treasury notes fell from 76 to 39 percent between end-December 2017 and end-June 2019; and its share of Treasury bills fell from 2.6 to 0.1 percent during the same period. Going forward, a strategy to guide future unwinding of RBM holdings of government securities has been developed. This strategy centers around targeting the appropriate level and composition of government securities to be held by the RBM for monetary policy purposes; and ensuring the transition to this target minimizes any adverse effects on the yield curve and market appetite for primary issuance by the government and is mindful of any adverse effect on the RBM's profitability.

12. **Financial sector stability will continue to be safeguarded.**

- All banks are fully compliant with IFRS9 standards, which went into effect in January 2018. We will ensure that all banks continue having adequate provisioning in line with the IFRS9 standards and ensure that their NPLs remain within the regulatory requirement. To reduce the time required to recover collateral associated with NPLs, we will encourage banks to enhance their loan recovery efforts. Banks will also be encouraged to improve analysis of collateral quality, including enhancing the collateral registry.

- To improve banking system efficiency, we have taken measures to reduce the banking system's overhead costs (e.g., credit referencing system and the national ID registry). Going forward, as T-bill rates decline, banks that have been relying on government securities for their profit margins will need to modify their business models and reduce interest rate spreads. To address loan concentration risks, we will continue close monitoring, surveillance of large borrowers, and enforcement of the single borrower exposure limit. Regulations aimed at enhancing the Domestic Systemically Important Banks supervision took effect in June 2019.

- Given rising bank lending in foreign currency, we will remain vigilant and ensure that all banks meet the net open position requirement and that lending in foreign currency is made particularly to clients with sources of foreign currency earnings. In this context, we will continue to review our prudential toolkit.

13. **New initiatives are gradually being implemented.** Regulations related to the revised AML/CFT framework that was enacted in 2017 were developed and gazetted in 2018. We will encourage commercial banks to develop skills in the banking sector and increase financial literacy amongst the population. We will further improve financial infrastructure, including facilitating mobile banking infrastructure and increasing non-bank financial intermediation. We will continue to increase protection of creditors' and borrowers' rights by improving contract enforcement.

14. **We will keep strengthening the regulatory framework of the financial system**. To this end, we will re-submit to Parliament, before end-2020, amendments to the Banking Act of 2010 for eventual enactment. These amendments, which were informed by IMF technical assistance recommendations, will align the legal framework for bank resolution closer to best practices and provide more options for dealing with problem banks. We are developing a consumer protection bill to be submitted to Parliament by end-2020.

15. **We are fully committed to the floating exchange rate regime.** We see this as a fundamental precondition for the success of our economic policies as it cushions shocks and supports economic diversification and the RBM will continue to intervene only to dampen excess volatility and accumulate reserves. In support of greater exchange rate flexibility, we will focus on deepening the interbank FX market. Going forward, the research department of the RBM will undertake a comprehensive study, which will include consulting other central banks in the region and private sector participants, to determine obstacles to FX market development (a report will be prepared by June 2020, structural benchmark) and the best framework for intervening in the FX market.

C. Fiscal Policy

16. **Our fiscal policy stance will support disinflation and help reduce debt vulnerabilities**. To this end, we strive to increase domestic revenues and contain spending within available resources, avoid accumulation of domestic and external arrears, and avoid non-concessional external borrowing. Continued implementation of prudent fiscal policies in the near- and medium-terms is necessary to keep the public debt-to-GDP ratio on a downward trajectory and prevent the private sector from being crowded out and productive government expenditure from being replaced by debt servicing costs.

17. **Cognizant of fiscal slippages in recent years, in FY 2019/20, we will aim to restore budget balance.** The approved FY 2019/20 budget foresees a primary surplus of 1.5 percent of GDP. As this is largely based on optimistic revenue growth, we plan to backload spending in the second half of the year and only spend as revenues materialize. In this way, at a minimum, a domestic primary surplus of 0.9 percent of GDP (which translates to a primary deficit of 0.8 percent of GDP) will be targeted in order to continue entrenching macroeconomic stability while prioritizing post-cyclone rehabilitation and reconstruction. Relative to FY 2018/19, this represents a tightening

of the domestic primary balance by 2.1 percent of GDP and the overall primary balance by 1.5 percent of GDP—including partial corrections for last year's revenue shortfalls and expenditure overruns. Important measures we will adopt to achieve this target include:

- Raise tax revenues including through introducing excises on plastic bags, pipes, and packaging, adjusting excise rates for inflation and applying it on sales price, and introducing a presumptive tax on commercial passenger vehicles, carbon tax on motor vehicles, and an import surcharge on select goods (such as alcohol, cigarettes, and some foods) and a withholding tax on interest earned by Trust Funds and commissions to mobile network operators—altogether adding at least 0.3 percent of GDP relative to the outturn in FY 2018/19. Increased imports will widen the tax base (0.2 percent of GDP). We will also freeze the current PIT schedule (including keeping the tax-free bracket in line with the minimum wage), refrain from introducing further exemptions, allowances and rate reductions and ensure enough funds for paying timely VAT refunds.

- Continue enhancing tax administration efforts based on more efficient use of risk analysis and enhanced monitoring, risk-based audits, rolling out the Integrated Tax Administration System (ITAS), improving the registration system, on-time filing and payment compliance, better enforcement of tax penalties and more effective use of the ASYCUDA World system for enforcement of trade taxes. Gains of at least 0.1 percent of GDP is expected from these on-going improvements in tax administration.

- Increase user fees and charges to adjust for inflation and progress toward marginal cost pricing and improve their enforcement. We will also introduce road tolling fees.

- Implement dividend policy to ensure profits and surpluses realized by SOEs and statutory bodies are duly remitted to the government; the share of dividends due to government will be increased and investment needs of statutory bodies will be met through budget appropriation rather than retention of surpluses.

- Limit wage and pension increases to inflation and limit new hiring to essential staff. The recent 40 percent increase in the minimum wage is not expected to affect the government wage bill as most government salaries are already well above the minimum wage.

- Reduce the maize procurement budget (assuming no extraordinary needs during FY 2019/20) and limit coverage of the Farm Input Subsidy Program.

- Reduce transfers to public entities by improving their revenue generating capacity.

- Reduce goods and services spending in non-priority areas—including on staff travel, purchase of motor vehicles, and office equipment—and channel those savings towards supporting cyclone victims and rehabilitation and security in a volatile post-election environment; non-essential recurrent spending will also be strictly limited.

- Increase social spending (in line with implementation capacity) with a significant portion targeted towards supporting cyclone victims and rehabilitation.

- Reorient spending on development projects towards post-cyclone resilient reconstruction, which will replace planned spending that was brought forward in FY 2018/19. Additional space will be created by reducing or delaying planned spending and better targeting of the iron sheet subsidy.

18. **We plan to step up measures to enhance the oversight of state-owned enterprises (SOEs).** Weak oversight and financial reporting are a challenge to adequate monitoring and management of risks to the budget and public debt from the SOEs. In this regard, we finalized and issued guidelines on issuance of guarantees, letters of consent and comfort, and indemnities in August 2018. Regulations related to ownership of SOEs were finalized in April 2019 and guidelines on the preparation of performance management plans and budgets were finalized in May 2019. Dividend and surplus policy have advanced and will be finalized by the Cabinet by end-2019 (structural benchmark). The mandate of the Public Finance Management Systems (PFMS) will be revised in line with revisions to the PFM Act with a view to strengthening its role in parastatal oversight. Pilot audits of the largest SOEs have been completed in collaboration with National Audit Office (NAO) and the report was submitted to Parliament in September 2019. By March 2020, we plan to submit to Parliament and publish on the Ministry of Finance (MoF) website a consolidated annual report on SOEs, including risk analysis case studies on ENGENCO, NOCMA, ADMARC, and the Blantyre Water Board that are in line with the recommendations of the IMF's technical assistance in this area (structural benchmark). We will conduct a risk analysis case study on ESCOM and publish on the MoF website by June 2020. We will also develop a prototype SOE database by end-2019.

19. **As part of our efforts to raise spending efficiency, we aim to enhance our public investment management.** We will prioritize (with rankings) the largest public investment projects based on rigorous cost-benefit analysis, absorptive capacity, growth, poverty reduction, and debt sustainability considerations. Large projects (concessional and potentially non-concessional) under consideration are listed in Table 3. We have piloted ex-post reviews/performance audits of two major capital projects in collaboration with the NAO and the reports were finalized in September 2019. The audit of a third project is also underway and will be finalized by June 2020. To increase the usefulness of the Public-Sector Investment Program (PSIP) database as a platform for the oversight and monitoring of investment projects, an audit of the PSIP database's coverage and the efficiency and timeliness of its processes was recently completed with the support of IMF technical assistance (structural benchmark). As a next step, we will begin implementing the findings of the audit (especially project rationalization) and continue building capacity (including through extensive training). We have also strengthened PSIP linkages to the budgeting and budget execution processes, including the publication of the PSIP as part of the budget documentation (Document no. 6) and will be recording multi-year commitments from FY 2020/21. In addition to raising efficiency, our efforts to improve public investment management (including project management and capacity), will support more accurate projections of project-based donor support disbursements.

20. **Over the near- and medium-terms, we are committed to implementing broad-based tax reforms to foster an efficient, transparent, and fair tax system as well as enhance revenue mobilization, compliance, and the business environment.**

- We will undertake a comprehensive review of our tax system with a view to further mobilizing domestic revenues and increasing the efficiency and equity of taxation. By end-March 2020, we will develop a domestic revenue mobilization strategy (structural benchmark) and start implementing it in FY2020/21. The strategy will aim to streamline tax incentives, including the industrial rebate scheme; expand the VAT base by removing unnecessary exemptions; improve the efficiency of excise taxation, including through more comprehensive taxation of passenger vehicles; increase income tax productivity and its resilience to base erosion (especially corporate income tax); improve SME taxation; and introduce recurrent property taxes. The strategy will include plans for implementing more progressive tax policies, including unwinding of past regressive tax measures. These measures should yield, on a net basis, at least 0.3 percent of GDP in FY 2020/21 and 0.4 percent of GDP over FY2021/22-22/23. They will be used to finance post cyclone reconstruction and build greater resilience to climate change.

- To strengthen tax administration, we will (i) continue to advance a risk-based approach to tax compliance through increased data analysis; (ii) enhance the tax registry and improve the registration system (under 50 percent of the TINS issues are active taxpayers); (iii) continue enforcing stiff penalties on malpractice of the use of EFDs and other instances of non-compliance, including due to abuse of transfer-pricing regulations; (iv) target improvement of on-time filing and payment compliance across all tax types to at least 50 percent; (v) continue increasing efficiency of customs, including by effective use of the ASYCUDA World system and its further integration with other agencies' IT systems; and (vi) by February 2020, adopt an integrated tax administration system (ITAS)—including full adoption in the large taxpayer office and the two other offices (in Blantyre and Lilongwe)—which will also improve transparency of business processes and reduce corruption. Some key milestones in the rollout of ITAS include (i) procurement of hardware by end-November 2019; (ii) begin piloting test ITAS in two tax offices (Blantyre and Mzuzu stations) by end-December 2019; and (iii) data cleaning and migration for all active taxpayers by March 2020. Through these measures we intend—at the minimum—to enhance revenues by 1 percent of GDP cumulatively over FY 2020/21-22/23.

- To improve non-tax revenues, especially various fees and charges collected by MDAs, we will enhance the Treasury oversight role, conduct a business process review in MDAs in terms of revenue collection and management processes and ensure efficiency enhancement by leveraging the use of technology. We will also keep adjusting user fees and charges for inflation and periodically undertake a comprehensive review to make progress towards marginal cost pricing and better enforcement. These efforts are expected to gradually increase fees collections (departmental receipts) by at least 0.1 percent of GDP cumulatively during FY 2020/21-22/23. We will also install toll gates in strategic locations and introduce toll fees to mobilize more revenue for road infrastructure rehabilitation.

- We are also committed to working with donors to improve the accuracy of information on donor flows, especially the disbursements. This will be done through enhanced use of the aid management platform and joint portfolio reviews.

21. **Our near- and medium-term budgeting plans include enhancing the composition and quality of government spending, while containing fiscal slippages.** Unbudgeted expenditures (e.g., in goods and services) will be avoided and we will only recruit critical personnel, while wage and pension increases will be limited to the inflation rate. We seek to reduce the wage bill through public sector employment reforms—a recent pilot review revealed gaps in grading and promotion policies. Any shortfalls in budget grants will be partly compensated by cutting non-priority spending (contingency items in the budget include limiting external travel and deferral of non-priority maintenance and investment projects, altogether about 0.2 percent of GDP). The composition of public investment will continue focusing on pro-growth and poverty reducing expenditures. With high development needs and limited fiscal space, raising efficiency of spending in priority areas such as social spending will be at the core of our medium-term budgeting plan. SOEs will not be required to undertake public investment spending (off-budget financing). We will avoid arrears in paying contractors, especially to SMEs. To do so, we shall put into place measures to enhance the allocational mix of health and education budgets, improve fiscal transparency and accountability at the national and sub-national levels, strengthen program-based budgeting, and engender efficiency in frontline service delivery. Beginning in FY 2020/21, we plan to achieve additional savings of at least 0.1 percent of GDP per year by reviewing and further limiting the eligibility and voucher value in the Farm Input Subsidy Program and limiting transfers by at least 0.2 percent of GDP by FY2021/22 by improving management of universities and statutory bodies and rationalizing their administrative staff and increasing the role of private sector where possible.

22. **We will also develop a plan to address the challenges involved in the current decentralization process.** This will include addressing issues of capacity and controls at the local level and eventually adopting a legal framework for budget systems and fiscal policy coordination.

D. Public Financial Management Reform

23. **We continue to make strides in public financial management reforms**. We have routinized monthly bank reconciliation of the payment bank accounts, except for salary accounts which will be routinely reconciled from July 2020 (with all backlog for FY 2016/17-2019/20 cleared). The automated transfer system reconciliation covering the payments of net salaries to all employee bank accounts (60 percent of gross pay) is already performing and the current year's payments of deducted amounts will be routinely matched by end-December 2019. We will continue to maintain fully reconciled domestic debt data across the responsible units in the RBM and the responsible unit in MoF (structural benchmark). To improve control and accountability, we have routinized monthly submission by MDAs of fiscal reports on the monthly funding release and publication of the report summaries on the MoF website (structural benchmark). We will continue to strengthen the quality control of these reports (including sanctions on controlling officers in MDAs for misreporting or non-compliance). We are publishing consolidated monthly statements of the government's declared

commitments and payment arrears on the MoF website including information on overdue (for more than 90 days) payments. More systematic commitment controls, constrained by forecasts of cash availability, will help prevent the accumulation of new payment arrears; more comprehensive reporting on payment arrears will help provide early warning and resolution of commitment control failures and enable sanctioning of controlling officers who incurred them.

24. **Building on recent advances, we plan to further improve our financial reporting**. We have begun producing quarterly consolidated financial reports based on reconciled bank accounts and certified by the Auditor General within six months after the end of the quarter. In FY 2019/20, we plan to produce them within four months after the end of each quarter; and beginning in FY 2020/21, we plan to produce them within 90 days after the end of each quarter (structural benchmark). We plan to regularly publish them on the MoF website. The first quarter FY 2018/19 financial reports were submitted to the Auditor General for certification in February 2019; the certification was completed in March 2019. The second quarter FY 2018/19 financial reports were submitted to the Auditor General for certification in May 2019; the certification was completed and the report published in September 2019. The third quarter FY 2018/19 financial reports were submitted to the Auditor General for certification in June 2019; the certification was completed and the report published in September 2019. In the same vein, we will continue producing and publishing on the MoF website monthly budget execution reports by vote and economic classification. Progressively, expenditure reporting will be based on actual payments and not funding. The annual consolidated financial statements for 2017/18 were submitted for audit within the statutory 4 months following the end of the financial year; an unqualified audit opinion was issued in January 2019. Timely reporting will mean that Parliament will discuss reports that are not only reliable but also relevant. In addition, we will adopt the electronic fund transfer (EFT) as the government's main payment method by end-June 2020 (structural benchmark). To this end we will complete a pilot of EFT transaction processing by end-March 2020 prior to extending EFT to Other Recurrent Transaction (ORT) and development payments. We will also implement TMS, as the current IFMIS bank reconciliation module, to the MG1 and losses and compensation accounts by end-December 2019 and the remaining three pool accounts by end-March 2020(structural benchmark). The early adoption of EFT and implementation of TMS will facilitate the move toward automated monthly reconciliation of all bank accounts.

25. **Improved financial reporting will provide a good basis for migrating to a new IFMIS.** In March 2019, the contract for a new IFMIS was issued and the supplier team has since been mobilized. The new IFMIS will allow for better financial reporting, transaction efficiencies, enhanced budget formulation and execution controls and security. An IFMIS steering committee, under the chair of the Secretary to the Treasury, has been constituted to oversee the planning, progress and implementation of the new IFMIS. Important preparatory work, including an agreement on the chart of accounts and bank account structures to be supported by the new IFMIS is almost complete. Drawing on the IMF's technical assistance and the World Bank's advice, we will put in place a realistic and comprehensive implementation plan (e.g., a phased approach supported by government teams and strong project management), a transparent governance framework, credible quality assurance, and a robust strategy to assure readiness (e.g., network/data center and business

process re-engineering) ensuring that maximum benefits are achieved from the investments. Recognizing that implementing a new IFMIS will take time and will benefit from those good practices already in place, we will continue allocating resources towards maintenance of the current IFMIS and expand most of its real time coverage to include all major TSA sub-accounts (including non-donor funded projects, receipts, and debt servicing payment) and important interfaces (notably, linking HRMIS and IFMIS) and debt transactions by end-2019. We will shift from monthly to quarterly budget release for commitment purposes, combined with monthly cash release, and require MDAs to commit against the released budget through IFMIS beginning in July 2020 From January 2020, we will pilot using IFMIS to record commitments of all types of expenditure (based on purchase or order contracts), prior to the submission of new contracts to the Secretary of Treasury for vetting and all domestic debt commitments, expenditures, and payments in real time; we intend to publish commitments against budget allocation as well as outstanding bills.

26. **Operations of the Cash Management Committee have been strengthened.** This was done by establishing a functional Cash Management Unit under the Secretary to the Treasury. The unit has been preparing a cash forecast of the next twelve months (soon after parliamentary approval of the budget) and it will be regularly updated. The unit prepares a variance analysis on forecasting errors every three months, reports a summary of the meeting minutes, and takes actions to improve MDA submissions—which was done for the first time in December 2018 and has since become a regular practice. By March 2020, we will review our banking arrangements and develop a strategy for building on the current core-Treasury Single Account (TSA) structure. We will continue identifying and closing dormant bank accounts and bringing all major balances within the core-TSA.

27. **We are developing a medium-term strategy that aims at solidifying the present gains**. We will embark on building human capacity through training to ensure that the reforms being implemented are sustained. A review of the PFM Act, currently underway, aims to ensure that laws and regulations are brought in line with the reforms that are taking place and emphasize a performance-based rewards and sanctions regime. Strengthening of oversight institutions such as the National Audit Office, Central Internal Audit Unit and the Public Accounts Committee of Parliament will continue under the medium-term strategy that is being developed. We will also strengthen medium-term performance and efficiency of our budget by better linking MDA strategic planning and budgeting, improving the credibility of the Medium-Term Expenditure Framework, and strengthening the framework for engaging key stakeholders. Building on the enactment of a new Public Procurement and Disposal of Assets Authority Act, which closes various loopholes under the old act, we intend to improve our procurement framework continuously, to enhance transparency, control, and accountability. We have already started by publishing all procurement information on the Public Procurement and Disposal of Assets Authority website. A recently completed diagnostic study on procurement will inform future reforms. We will also use the performance contract with controlling officers to hold them accountable for adhering to relevant rules and procedures and strengthen procurement audits. Over time, we will consider gradually moving to an e-procurement system.

E. Structural Reforms

28. **The Malawi Growth and Development Strategy (MGDS III) envisages a significant improvement of Malawi's business climate**. The objective of building productivity and competitiveness will require unlocking private sector potential. To this end, we will continue to improve the business environment, including by easing procedures to start a business and deal with construction permits, strengthening contract enforcement, and enhancing insolvency processes.

29. **We will also implement deep reforms in agricultural regulations and market intervention systems, agricultural subsidies, and land management systems:**

- ***ADMARC:*** A comprehensive strategic review of ADMARC (Agricultural Development and Marketing Corporation) has been completed. Based on this review's findings, we will implement a reform program to better balance maize price stabilization against fiscal sustainability and improve transparency and efficiency in this area. Concrete steps will be taken to strengthen ADMARC's financial sustainability, e.g., by separating the social and commercial functions within ADMARC.

- ***Control of trade:*** The Control of Goods Act has been amended to conform to international trade best practices and efforts are underway to finalize subsidiary legislation which will adequately define the public interest grounds needed to determine the thresholds for intervention. New bans or review of existing bans will be reviewed in consultation with stakeholders.

- ***FISP:*** We will continue FISP reform, focusing on containing its budget impact, an increased role for the private sector, better governance, and better beneficiary targeting.

- ***Land reform:*** We will continue implementing new land laws based on the lessons learned from our pilot programs.

F. Debt Management

30. **Malawi is classified as being at moderate risk of external debt distress and at high overall risk of debt distress due to high domestic debt**. We will limit our external borrowing to high priority projects which are in line with the MGDS III and maximize the grant element of external borrowing to ensure that total debt (and guarantees) contracted is consistent with debt sustainability. While MGDS III lays out ambitious goals for critical infrastructure projects, we are committed to ensuring that their financing preserves debt sustainability.

31. **We plan to strengthen debt management and monitoring**. We have developed a comprehensive medium-term debt strategy and will keep updating it. The Debt Management Committee is operational and will assess both domestic and external borrowings. The committee will ascertain loan concessionality and ensure debt sustainability taking into consideration the entire

borrowing plan and the medium-term debt strategy. Borrowing in the FY 2019/20 budget will be consistent with our objectives of social development and poverty reduction and debt sustainability. We will ensure that new loans are concessional and accompanied by solid feasibility studies (by an independent third party when required for donor-funded projects) and that the macroeconomic implications (including on debt) are carefully considered. We will further improve our debt monitoring by allocating sufficient resources and increase training.

32. **We will take steps to improve coordination of debt and liquidity management as well as deepen the domestic debt market.** By end-2019, MoF's Debt and Aid Management Division's front office operations will have more active engagement in domestic debt management policies and operations in collaboration with the RBM (i.e., the division will lead preparation of the DSA and formulation of the MTDS, the division will be an active participant in weekly meetings of the short-term borrowing committee, and prepare an annual borrowing plan—reflected by the planned financing for the year and an issuance calendar; structural benchmark). Better cash flow forecasts (as outlined above) are helping to improve debt and liquidity management coordination. We are gradually lengthening the maturity of government securities and developing a government securities benchmark issuance policy that will concentrate the amounts of benchmark tenors in maturity buckets of 3, 5, 7, and 10-years to develop the government securities yield curve. We will continue to develop the Treasury Bill yield curve by issuing 91, 182, and 364-day maturities in auctions. We will continue to publish the indicative amounts in an issuance calendar that will be confirmed closer to auctions through announcements, and we will adhere to these announced auction schedules.

G. Fuel Pricing and Import Regime

33. **We will continue to improve our fuel security situation.** We have three fuel storage depots (capable of holding about 25 percent of annual consumption) and guidelines for their operation which clarifies the framework for collaboration between the storage operator and fuel importers or distributors. The framework has been running well with fuel importers who are in the process of integrating the facilities as a part of their logistics chain. It will enable the augmented storage cost to be fully passed on to the pump price. Since 2013, our fuel import regime had been based on private sector imports with cost recovery guaranteed by the automatic fuel pricing mechanism. Fuel imports were done jointly by a traditional private sector consortium (PIL) and NOCMA, based on their 2013 MOU, which expired in June 2018. Two new pieces of legislation have been promulgated to develop the wholesale and retail markets and have been strictly enforced since February 2019.

34. **The fuel import regime will remain unchanged for the rest of the 2019/20 fiscal year.** However, we will continue to evaluate the balance of security and efficiency under the current regime as more experience is gained. In particular, we are committed to ensuring a level-playing field for all market participants, while also putting in place a safeguard against, potentially disastrous, supply disruption. Given the importance of safeguarding governance risks in the sector, any further change in the fuel import regime or operation of the facility will be done in a transparent

manner, with full private sector participation. We will produce, publish, and discuss with all stakeholders a fully-costed and well-thought out proposal for any change prior to implementation.

35. **We remain committed to retaining and implementing the fuel price automatic adjustment mechanism.** This mechanism has enabled full cost recovery by fuel importers while precluding government subsidy. The rule is that over ±5 percent change in the formula-based underlying price triggers a price adjustment; and all other price changes are absorbed by the Price Stabilization Fund (PSF). Recently, to avoid sudden or large pump price increases, discretion has been applied and the PSF has been used to subsidize fuel distributors in place of the automatic price adjustment mechanism. This led to a pause in the adjustment of prices at the pump since October 2016. However, increases in imported oil prices led the Malawi Energy Regulatory Authority (MERA) to approve significant increases in petroleum and diesel prices in 2018—although the increases were partly undone this year due to a decline in the international oil price. Going forward, we intend to exercise strict restraints on the use of discretion over the ±5 percent price adjustment rule with a view to protect the PSF and avoid a backloaded, lumpy price adjustment. To increase transparency and accountability, we will disclose more information on the aggregate use of the PSF including publishing on the MERA website the audited reports on its use and management.

H. Gender Equity

36. **We take note of the importance of addressing gender inequality in achieving inclusive growth**. Gender disparities hinder economic growth by impeding full realization of Malawi's human resource potential and aggravate economic exclusion, making it harder for women to escape from poverty. Policy interventions will continue to focus on adolescent girls given the high potential impact of breaking the cycle of deprivation at an early stage of life.

- ***Ending child marriages:*** The constitutional amendment to raise the minimum age for marriage from 15 to 18 was a critical first step. In addition, we plan to develop a comprehensive national program of action which will entail multifaceted strategic interventions—from social protection, to law enforcement, to health (particularly sexual and reproductive health), child protection, and public education.

- ***Keeping girls in school:*** We will continue to facilitate larger and more effective investment on classrooms, teachers, and education materials. We will also broaden our demand side interventions (e.g., more social assistance and targeted subsidy programs; which would be gender-sensitive).

- ***Assets and credit.*** Given the significance of a matrilineal system of land inheritence in Malawi, we are commited to the formalization of customary land rights that are key to women's access to finance. Policy interventions for access to finance, including gender neutral ones, will further help level the playing field.

- ***Labor market policies.*** We will consider non-gender-neutral policy options (e.g., childcare support) to help increase women's labor market participation.

III. STRUCTURAL PROGRAM FOR 2019-20

37. **The macroeconomic policies supported by the ECF will be complemented by a strong structural program, which will make the transmission of economic policy more efficient.** The Structural Benchmarks for 2019-20 (Table 2) signal our commitment to a strong reform agenda in key sectors of the economy.

I. Structural Benchmarks and Program for 2019

Fiscal Sector

- Submission to the MoF of five reports by the MDAs by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance (continuous).

- Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within four months after the end of each quarter in FY 2019/20 and within 90 days after the end of each quarter in following years. The financial reports should be certified by the Auditor General. (continuous).

- Reconcile all debt data between the MOF and RBM (continuous).

- Cabinet approval of the dividend policy relating to SOEs (end-December 2019).

- Ensure DAD front office operations include more active engagement in domestic debt management policies and operations in collaboration with the RBM (end-December 2019).

- Submit to Parliament and publish on the MoFEPD website a consolidated annual report on SOEs (including case studies for ENGCO, NOCMA, ADMARC, and Blantyre Water Board, end-March 2020).

- Develop a domestic revenue mobilization strategy (end-March 2020).

- EFT adoption and TMS implementation (five pool bank accounts) facilitating the move toward automated monthly reconciliation of all bank accounts. TMS implementation of two accounts will be targeted for end-2019 and the remaining three for end-March 2020 (end-June 2020).

Financial Sector

- Develop a roadmap for increasing access to finance (end-December 2019).
- The research department of the RBM will review and prepare a report on the obstacles to FX market development (end-June 2020).

IV. PROGRAM MONITORING

38. **The program will be monitored on a semi-annual basis, through quantitative targets (Table 1) and structural benchmarks (Table 2).** Quantitative targets for end-December 2019 and end-June 2020 are performance criteria while those for end-March 2020 and end-September 2020 are indicative targets. The fourth and fifth reviews under the program will be completed on or after April 15, 2020 and October 15, 2020, respectively.

Table 1. Malawi: Quantitative Targets, 2018-20[1]

	Target type [2]	2018				2019								2020		
		End-Dec.				End-Mar.		End-Jun.				End-Sept	End-Dec.	End-Mar.	End-Jun.	End-Sept.
		Prog. (Country Report 18/336)	Adj. Prog.	Est.	Status	IT (Country Report 18/336)	Est.	Prog. (Country Report 18/336)	Adj. Prog.	Est.	Status	IT (Country Report 18/336)	Prog.	IT	Prog.	IT
I. Monetary targets (millions of kwacha)																
Reserve money (ceiling on stock) (upper bound)[3]	PC	326,115		298,112	Met	308,798	281,997	346,236		318,376	Met	340,175	324,219	318,529	343,225	362,598
Reserve money (ceiling on stock)[3]		316,617		289,429		299,804	273,784	336,151		309,103		330,267	314,776	309,251	333,228	352,037
Reserve money (ceiling on stock) (lower bound)[3]		307,118		280,746		290,810	265,570	326,067		299,830		320,359	305,333	299,974	323,231	341,476
II. Fiscal targets (millions of kwacha)																
Primary balance (floor)[5,6,11]	PC	-4,456	-3,770	-83,657	Not Met	-2,684	-168,145	89	7,657	-125,614	Not Met	-1,236	-101,537	-93,418	-48,574	-14,061
Domestic primary balance (floor)[4,6,11]	PC			-37,872			-92,565			-66,909			-42,339	-12,976	53,112	16,739
RBM financing of central government (ceiling)[6,7]	PC	0	93,710	25,418	Met	0	-150,228	0		0	Met	0	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0		0	Met	0	0	0		0	Met	0	0	0	0	0
Social spending (floor)[6,9]	IT	182,207		208,717	Met	273,310	318,515	364,413		406,385	Met	103,104	229,991	350,619	449,469	126,966
III. External sector targets (US$ millions, unless otherwise indicated)																
Net international reserves of the RBM (floor)[5,8]	PC	428.6	429.5	486.2	Met	436.6	503.0	460.4	470.8	487.8	Met	473.1	486.7	523.4	557.0	597.2
Accumulation of external payments arrears (ceiling)[6,10]	PC	0		0	Met	0	0	0		0	Met	0	0	0	0	0
Contracting or guaranteeing of non-concessional external debt (ceiling)[6,10]	PC	0		0	Met	0	0	0		0	Met	0	0	0	0	0
Net foreign borrowing of the central government (ceiling)[6]	IT									77.3			48.9	61.0	72.8	25.7
Memorandum items:																
Net foreign assets of the RBM (US$ millions, end of period)[6]		316.0		428.4		324.0	444.2	347.8		422.9		360.4	373.8	410.5	444.1	484.3
Budget support (US$ millions)[6]		0.0		0.0		0.0	0.0	0.0		40.8		0.0	0.0	0.0	0.0	0.0
Budget support (millions of kwacha)[6]		0.0		0.0		0.0	0.0	0.0		30,704.7		0.0	0.0	0.0	0.0	0.0
Limits on disbursements of foreign concessional contracted and guaranteed loans (US$ millions)[6]		53		62		79	103	105.1		121.3		49.4	79.0	106.9	134.4	39.2
Debt service payments to the World Bank and AfDB (US$ millions)[6]		19.8		7.3		24.9	12.8	30.1		21.6		5.2	3.2	5.4	5.4	5.4
Debt service payments to the World Bank and AfDB (millions of kwacha)[6]		14,680		5,374		18,842	9,400	23,137		16,241		4,041	2,414	4,107	4,176	4,245
Joint Fund on Health receipts (millions of kwacha)[6]		4,577		4,577		6,865	6,865	9,153		9,153		1,831	3,661	5,492	7,323	
Joint Fund on Education receipts (millions of kwacha)[6]		8,656		8,656		12,983	12,983	17,311		17,311		2,000	4,000	6,000	8,000	
Program exchange rate (kwacha per US$)		732		732		732	732	732		732		732	732	732	732	732

Source: IMF staff projections.

[1] Targets are defined in the technical memorandum of understanding (TMU).

[2] "PC" means Performance Criterion and "IT" means Indicative Target. The PC test date for the 2nd Review is end-December 2018 and for the 3rd Review is end-June 2019. Test dates for future reviews will be end-June and end-December. End-September and end-March targets are ITs.

[3] PC applies to upper bound only. See TMU for details.

[4] Targets are subject to an adjustor for budget support, as specified in the TMU.

[5] Targets are subject to an adjustor for budget support and debt service payments and donor-funded social sector expenditures, as specified in the TMU.

[6] Defined as a cumulative flow, starting from the beginning of the fiscal year.

[7] Targets are subject to an adjuster equivalent to 10 percent of the average of the inflation adjusted domestic revenues of the previous three fiscal years, as specified in the TMU.

[8] Defined as stocks.

[9] Priority social spending as defined in the TMU and quantified in the authorities' budget.

[10] Evaluated on a continuous basis.

[11] The domestic primary balance will replace the primary balance as a PC, beginning with the end-December 2019 PC.

Table 2. Malawi: Structural Benchmarks, 2019-20[1]

Structural benchmark	Target date	Macro Rationale
Public financial management		
Submission to the MoF of five reports by the MDAs[1] by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance.	Continuous (monthly from May 15, 2018)	Improve fiscal transparency; prevent accumulation of new domestic arrears; reduce vulnerabilities to corruption.
Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within four months after the end of each quarter in FY 2019/20 and within 90 days after the end of each quarter in following years. The financial reports should be certified by the Auditor General.	Continuous (quarterly from March 31, 2019)	Improve fiscal transparency and integrity of the accounting system; routinize reconciliation of all bank accounts; strengthen cash planning; reduce vulnerabilities to corruption.
Reconcile all debt data between the MOF and RBM.	Continuous (monthly from April 30, 2018)	Enhance debt management; improve transparency and monitoring of public debt.
Cabinet approval of the dividend policy relating to SOEs.	End-December 2019	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Ensure DAD front office operations include more active engagement in domestic debt management policies and operations in collaboration with the RBM.	End-December 2019	Enhance debt management; improve transparency and monitoring of public debt.
Submit to Parliament and publish on the MoFEPD website a consolidated annual report on SOEs (including case studies for ENGENCO, NOCMA, ADMARC, and Blantyre Water Board).	End-March 2020	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Develop a domestic revenue mobilization strategy.	End-March 2020	Increase domestic revenues in an efficient and equitable manner.
EFT adoption and TMS implementation (five pool bank accounts) facilitating the move toward automated monthly reconciliation of all bank accounts. TMS implementation of two accounts will be targeted for end-2019 and the remaing three for end-March 2020.	End-June 2020	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.
Financial sector		
Develop a roadmap for increasing access to finance.	End-December 2019	Increase financial sector intermediation.
The research department of the RBM will review and prepare a report on the obstacles to FX market development.	End-June 2020	Deepen the interbank FX market, improve market functioning, efficiency in intermediation with improved liquidity.

Sources: IMF staff and Malawian authorities.

[1] Ministry, department, and agency.

Table 3. Malawi: Pipeline of Large Projects Under Consideration

Project	Potential Cost (in USD)
Construction of Chilumba to Mbeya Railway Line	978,412,162
Reconstruction and Rehabilitation of Limbe - Marka Railway Section	724,556,771
Coal Fired Power Generation Programme	777,364,865
Lake Malawi Water Supply project	438,234,959
Diamphwe Bulk Water Supply Project (DBWSP)	294,035,797
Construction of a new terminal building and reconstruction of existing runways at Chileka International Airport	194,612,120
Kaphatenga - Nkhotakota - Dwangwa rehabilitation project	154,054,054
Up-Scaling Production and Marketing of Legumes, Rice and Fruits	135,197,655
Construction of Residential Houses for Government Institutions	108,412,162
Construction of Lambilambi Dam: Implementation Phase	97,346,486
Programme for Rural Irrigation Development (PRIDE)	82,156,757
Irrigation Development Programme (IDP)	74,324,324
Provision of Residential and Office Accommodation for the Malawi Police Service	74,089,298
Balaka - Salima(period)	67,837,838
Construction of Judiciary Headquarters	66,593,153
Construction of By-Pass and Chileka Dual Carriage in Blantyre City	58,452,703
Construction of Mzimba Dam	48,736,959
Projects Under Consideration But More Analysis Required	
Chilinga - Muloza (Upgrading)	48,479,730
Detailed Design and Construction of multi-purpose Dam for Kasungu Water Supply Scheme	39,244,459
Migration of Police Communication System from Analogue to Digital Platform	38,390,640
Detailed design of Multi-purpose Surface Water Source and Constrcuion Supervision for Mponela Town	37,343,842
Malawi Rural Electrification and Construction of Power lines	31,386,838
Construction of Blantyre and Mzuzu Cancer Centres	29,252,703
Karonga Water Supply Project	28,737,162
Mchinji rb - area 18 rb - Kanengo	25,675,676
Backbone Fibre Project	22,393,959
Nkhatabay Water Supply Project	22,146,622
Construction of Staff Houses	21,588,856
Upgrading Rehabilitation and Extension of Liwonde Water Supply Project to include Balaka	19,557,095
Proposal for Extension of Mangochi Water Supply System to Lakeshore Areas	16,454,632
Chilumba Water Supply Project	15,202,703
Rumphi Water Supply Project	14,884,710
Upgrading Rehabilitation and Extension of Nchalo Water Supply Project	10,693,711
Kawere -Mkanda road project	10,270,270

Source: Malawian authorities.

Attachment II. Technical Memorandum of Understanding

November 1, 2019

I. INTRODUCTION

1. **This memorandum defines the quantitative performance criteria, benchmarks, and indicative targets for the program, as described in the Memorandum of Economic and Financial Policies (MEFP) for the period [November 22], 2019 – April 30, 2021** supported by the Extended Credit Facility (ECF) arrangement and sets out the data reporting requirements.

2. **Coverage:** The central government includes ministries, departments, and agencies, and all other units of government that exercise authority over the entire economic territory. However, in contrast to the System of National Accounts 1993 (SNA 1993) and Government Finance Statistics Manual 2001 (GFSM 2001) standards, nonprofit institutions that are controlled and financed by the central government are excluded for purposes of this memorandum. The accounts of the monetary authorities include those of the Reserve Bank of Malawi (RBM). Monetary aggregates under the program are based on the nine-bank monetary survey.

II. QUANTITATIVE PERFORMANCE CRITERIA AND INDICATIVE TARGETS

3. Quantitative performance criteria are established for December 31, 2019 and June 30, 2020 with respect to:

- Reserve money (ceiling);
- Domestic primary balance of the central government, cash basis (floor);
- RBM financing of the central government (ceiling);
- Net official international reserves (NIR) of the RBM (floor);
- Accumulation of external payments arrears (ceiling);
- Contracting and guaranteeing of non-concessional external debt (ceiling).

4. Indicative targets are established for March 31, 2020 and September 30, 2020 with respect to the above variables, and for these dates as well as December 31, 2019 and June 30, 2020 with respect to:

- New domestic arrears (ceiling);
- Social spending (floor);

- Net foreign borrowing of the central government (ceiling).

J. Targets for Monetary Aggregates

- **The Stock of Reserve Money (ceiling)**

5. **A ceiling applies to the upper bound of a reserve money band (set +/-3 percent) around a central reserve money target.**

6. **Definition.** Reserve money is defined as the sum of currency issued by the RBM, including the vault cash of commercial banks, and balances of commercial bank accounts with the RBM. It includes required reserves held for kwacha deposits, other domestic currency liabilities, and other demand and time deposits held with the RBM.

7. **Reporting requirement.** Data on reserve money will be transmitted to the IMF on a weekly basis. This transmission will include weekly balance sheet of the RBM which will show all items listed above in the definitions of reserve money.

K. Targets for Fiscal Sector

- **Domestic Primary Balance (floor)**

8. **A floor applies to the cumulative flow of domestic primary balance since the beginning of the fiscal year.**

9. **Definition.** Domestic primary fiscal balance is defined (i) domestic revenue (total revenue less grants) less (ii) the sum of current expenditures (net of domestic and foreign interest payment), domestically-financed development expenditure, and net lending plus (iii) the discrepancy (see paragraph 10). A positive (negative) discrepancy, implying underfinancing (overfinancing), raises (lowers) the domestic primary balance.

10. **Discrepancy** is defined as the negative of the sum of: (i) the sum of domestic revenue and grants, minus the sum of current expenditure, development expenditure, and net lending and (ii) the sum of net domestic borrowing (see paragraph 11) and net foreign borrowing of the central government (see paragraph 22). A positive (negative) discrepancy implies underfinancing (overfinancing).

11. **Net domestic borrowing of the central government** is measured as the sum of (i) net borrowing from the RBM (including, but not limited to, ways and means advances, loans, holdings of local registered stocks, promissory notes, and all government securities minus deposits); (ii) net borrowing from commercial banks (including, but not limited to, advances, loans, holdings of local registered stocks, promissory notes, and all government securities minus deposits); (iii) net borrowing from nonbanks (including, but not limited to, holdings of local registered stocks and all government securities); and (iv) amortization of zero-coupon promissory notes. All government

securities and locally registered stocks are valued at cost rather than face value. Transfers from extra-budgetary funds will not be considered revenues for this performance criterion. They will be treated the same as borrowing from the private sector (as their accounts are outside the definition of government) and therefore as domestic borrowing. Asset sales or privatization revenues will be accounted for under financing as a separate category, separate from domestic or foreign financing in calculating net domestic borrowing.

12. **Adjustors.** The program floor on domestic primary balance will be adjusted down by the full amount by which budget support exceeds the program baseline.

13. **Budget support** includes all grants and foreign financing not directly linked to additional budgetary expenditure. Excluded from this definition is external project financing to fund particular activities, such as financial support from the IMF, and donor inflows (in kwacha) from the U.S. dollar-denominated donor pool accounts for the Joint Funds on health, education, and agricultural, held in the Malawi banking system.

14. **Reporting requirement.** Data on domestic primary balance will be transmitted to the IMF on a monthly basis, within [4] weeks from the end of the month.

- **RBM Financing of the Central Government (ceiling)**

15. **Definition.** RBM financing of the central government is defined as net borrowing by the central government from the RBM (including through ways and means advances, loans, holdings of local registered stocks, promissory notes, and all government securities minus deposits).

16. **Adjustors.** For cash management purposes, the ceiling on RBM financing of the central government for September 2019, December 2019, and March 2020 is subject to an upward adjustment of up to 10 percent of the average inflation adjusted annual domestic revenue of the previous three financial years.

17. **Reporting requirement.** Data on the RBM financing of the central government will be transmitted to the IMF on a monthly basis within 4 weeks from the end of the month.

- **New Domestic Arrears (ceiling)**

18. **Definition.** Domestic arrears are overdue payment obligations of the central government other than external payment arrears, including on wages and salaries, pensions, transfers, domestic interest, goods and services, obligations arising from court cases, legally established compensation claims, principal payments on domestic loans, and tax refunds. Domestic interest payments are in arrears when the payment is not made on the due date. Payments on wages and salaries, pensions, transfers, court-established obligations, and compensations are in arrears when they remain unpaid for more than 30 days beyond their due date. Payments for goods and services are deemed to be in arrears if they have not been made within 90 days of the due date, or – if a grace period has been

agreed – within the contractually agreed grace period. Tax refunds are in arrears if not paid within the time limit as set forth in respective tax laws.

19. **Reporting requirement.** Data on new domestic arrears will be transmitted to the IMF on a monthly basis from the beginning of the fiscal year.

- **Social Spending (floor)**

20. **Definition.** Using functional classification of expenditure, social spending is computed as the sum of central government spending on health, education, and government social protection (comprising the government expenditures by the ministries of health, education, and gender, children, disability and social welfare; National Aids Commission and spending on FISP and maize). To maintain Malawi's commitment and progress toward poverty reduction, the social spending allocations in the government budget will not be adjusted downward to meet fiscal targets of the program.

21. **Reporting requirement.** Social spending will be reported on a monthly basis from the beginning of the fiscal year.

L. Targets for External Sector

- **Net Foreign Borrowing of the Central Government (ceiling)**

22. **Definition.** Net foreign borrowing of the central government is defined as disbursements of external debt as defined in paragraphs 35 and 36 including loans by official creditors (both multi- and bilateral creditors) minus amortization due.

23. **Reporting requirement.** Data on net foreign borrowing will be transmitted to the IMF on a monthly basis within 4 weeks from the end of the month.

- **Net International Reserves (NIR) of the RBM (floor)**

24. **Definition.** The NIR of the RBM is defined as gross reserves minus IMF and other short-term liabilities. The values of all foreign assets and liabilities will be converted into U.S. dollars at each test date using the program cross exchange rates listed in Table 1.

25. **Gross reserve assets of the RBM** are defined by the International Reserves and Foreign Currency Liquidity Guidelines for a Data Template as external assets immediately available and controlled by RBM "for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency's exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing)." (BPM6, paragraph 6.64).

26. **Gross reserve assets include the following**: (i) monetary gold holdings of the RBM; (ii) holdings of SDRs; (iii) the reserve position in the IMF; (iv) foreign convertible currency holdings; (v) foreign currency denominated deposits held in foreign central banks, the Bank for International Settlements, and other banks; (vi) loans to foreign banks redeemable upon demand; (vii) foreign securities; and (viii) other unpledged convertible liquid claims on nonresidents. It excludes the following: (i) any foreign currency claims on residents; (ii) capital subscriptions in international institutions; (iii) foreign assets in nonconvertible currencies; (iv) transfers of foreign currency claims to RBM by other institutional units in Malawi just prior to reporting dates with accompanying reversals of such transfers soon after those dates; (v) assets obtained through any derivatives liabilities (including currency swaps) with remaining maturity of one year or less; (vi) assets obtained through deposit liabilities of domestic commercial banks (including reserve requirement in foreign currency) gross reserves that are in any way encumbered or pledged, including, but not limited to: (a) assets blocked when used as collateral for third party loans and third-party payments, or pledged to investors as a condition for investing in domestic securities; (b) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and (c) foreign reserves blocked for letters of credit.

Table 1. Malawi: Cross rates for Nominal Exchange Rate and Gold Price for the 2018-21 ECF Arrangement

	31-Dec-2017
Gold bullion LBM[1] US$/troy ounce	1,257.13
SDR to US$ exchange rate	0.707
Euro to US$ exchange rate	0.845
Yuan to US$ exchange rate	6.594
Yen to US$ exchange rate	112.950
Sterling UK to US exchange rate	0.746
Australian $ to US exchange rate	1.308
Canadian $ to US exchange rate	1.278
Swiss Franc to US exchange rate	0.987
South African rand to US exchange rate	0.081
Malawian Kwacha to US$ exchange rate	732.03

Sources: IMF (International Financial Statistics) and Reserve Bank of Malawi.

[1] LBM connotes London Bullion Market.

27. **Gross reserve liabilities of the RBM** are defined as the sum of the following: (i) outstanding medium and short-term liabilities of the RBM to the IMF; (ii) all short-term foreign currency liabilities of the RBM to nonresidents with an original maturity of up to, and including, one year; (iii) foreign currency denominated liabilities arising from outstanding derivatives; and (iv) all foreign currency denominated liabilities to residents (including, for instance, foreign currency denominated deposits of domestic banks and other residents with the RBM). SDR allocations are excluded from gross reserve liabilities of the RBM.

28. **Adjustors applied to NIR program floor:**

- *Budget support*. The program floor on NIR will be adjusted upward by the full amount by which the U.S. dollar-denominated inflows from the budget support exceed the program baseline. In the event of a shortfall in budget support inflows, the downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 29. The budget support is measured as the cumulative flow from the beginning of the fiscal year. They will be recorded in the original currency of disbursement and then converted to U.S. dollars using the above defined program cross exchange rates.

- *Donor accounts for the social sector (including health and education Joint funds, and the NAC)*. The floor on the NIR of the RBM will be adjusted upward by the full amount by which the donor inflows from the U.S. dollar-denominated donor accounts for Joint funds and NAC held in the RBM are higher than the program baseline. In the event of a shortfall, the downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 29. These donor inflows are measured as the cumulative receipts by the budget from the beginning of the fiscal year. They will be recorded in the original currency of disbursement and then converted to U.S. dollars using the above defined program cross exchange rates.

- *Debt service payments (including both interest and principal)*. The floor on NIR of the RBM will be adjusted upward by the full cumulative amount by which debt service payments to the WB and the AfDB fall short of the program baseline. In the event of any excess of debt service payments to the WB and the AfDB, the downward adjustment of the NIR floor will be subject to the limitation outlined in paragraph 29. Debt service payments will be measured as the cumulative payments from the beginning of the fiscal year. They will be recorded in the original currency of payments and then converted to U.S. dollars using the above defined program cross exchange rates.

29. **The total downward adjustment to the NIR floor** from the combined impact of: (i) a shortfall of budget support relative to the program projections; (ii) a shortfall of inflows to the donor accounts for the social sector relative to the program projections; and (iii) any excess of debt service payments to the WB and the AfDB relative to the program projections, will be subject to a cumulative limit of US$65 million.

30. **Reporting requirement**. Data on foreign assets and foreign liabilities of the RBM will be transmitted on a monthly basis, including sub-components and a breakdown of assets that are pledged or encumbered. This transmission will include daily and weekly data on RBM's foreign exchange liabilities to commercial banks (including required reserves with the RBM) and the exchange rate used for their conversion into kwacha will be shown separately.

31. **Net foreign assets (NFA) of the RBM** are defined as its gross foreign assets (GFA) minus its gross foreign liabilities. Gross foreign liabilities are equal to gross reserve liabilities as defined in paragraph 25, plus any other foreign liabilities not listed in that paragraph.

32. **Gross foreign assets (GFA) of the RBM** are defined as gross reserves assets as defined in paragraph 23, plus (i) any foreign currency claims on residents; (ii) capital subscriptions in international institutions; (iii) foreign assets in nonconvertible currencies; (iv) transfers of foreign currency claims to RBM by other institutional units in Malawi just prior to reporting dates with accompanying reversals of such transfers soon after those dates; (v) assets obtained through currency swaps of less than three months duration; (vi) gross reserves that are in any way encumbered or pledged, including, but not limited to: (a) assets blocked when used as collateral for third party loans and third-party payments, or pledged to investors as a condition for investing in domestic securities; (b) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and (c) foreign reserves blocked for letters of credit.

- **Accumulation of External Payment Arrears (ceiling)**

33. **Definition.** External payment arrears consist of debt service obligations (principal and interest) of the central government or the RBM to nonresidents that have not been paid at the time they are due, as specified in contractual agreements, except on external debt subject to rescheduling or restructuring. This performance criterion will be monitored on a continuous basis.

34. **Reporting requirement.** Data on external payment arrears will be transmitted to the IMF on a monthly basis within 4 weeks from the end of the month.

- **Contracting or Guaranteeing of Non-Concessional External Debt (ceiling)**

35. **Definition of debt**, for the purposes of the TMU, is set out in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), and also includes contracted or guaranteed commitments for which value has not been received. For program purposes, the term “debt” is understood to mean a current, that is, not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debt can take several forms; the primary ones being as follows:

i. Loans, that is, advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers’ credits) and temporary exchange of assets that are equivalent to fully collateralized loans, under which the obligor is required to repay the loan funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

ii. Suppliers’ credits, that is, contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and

iii. Lease agreements, that is, arrangements under which the lessee is allowed to use a property for a duration usually shorter than that of the life of the property in question, but without transfer of ownership, while the lessor retains the title to the property. For the purposes of this guideline, the debt is the present value (at the inception of the lease) of all the lease payments expected for the period of the agreement, except payments necessary for the operation, repair, and maintenance of the property.

36. **Definition of non-concessional external debt.** Short-, medium-, and long-term debt is considered concessional if it includes a grant element of at least 35 percent[1] and non-concessional if otherwise. The grant element is defined as the difference between the nominal value of the loan and its present value, expressed as a percentage of the nominal value of the loan. The present value of the debt at the date on which it is contracted is calculated as the discounted sum of all future the debt service payments at the time of the contracting of the debt.[2] The discount rate used for this purpose is 5 percent per annum. The ceiling on non-concessional debt applies to the contracting and guaranteeing of debt with nonresidents by the central government, the RBM, and state-owned enterprises, unless an explicit selective exclusion is made. This performance criterion is monitored on a continuous basis. The ceiling applies to debt and commitments contracted or guaranteed for which value has not been received. The ceiling is measured cumulatively from the beginning of the fiscal year.

37. **Short-term debt:** Outstanding stock of debt with an original maturity of one year or less.

38. **Medium- and long-term debt:** Outstanding stock of debt with a maturity of more than one year.

39. **Excluded from the limit on non-concessional external debt** is the use of IMF resources, and any kwacha-denominated government security holdings and stock holdings by nonresidents. Excluded from the limit are also (i) debts classified as international reserve liabilities of the RBM; (ii) new debt issued to restructure, refinance, or repay existing debt up to the amount actually used for the above-mentioned purposes; (iii) normal import financing; and (iv) arrangements to pay overtime obligations arising from judicial awards to external creditors. A financing arrangement for imports is considered to be "normal" when the credit is self-liquidating.

[1] The IMF website gives an instrument (link hereafter) that allows the calculation of the grant element for a wide range of financing packages: http://www.imf.org/external/np/pdr/conc/calculator.

[2] The calculation of concessionality takes into account all aspects of the loan agreement, including maturity, grace period, schedule, commitment and management fees commissions.

III. REPORTING REQUIREMENTS

40. **For the purpose of program monitoring**, the Government of Malawi will provide the data listed in Table 2 below with monthly data within four weeks of the end of each month, and annual data as available.

41. **The authorities will inform the IMF staff in writing at least ten business days (excluding legal holidays in Malawi) prior to making any changes in economic and financial policies that could affect the outcome of the financial program.** Such policies include but are not limited to customs and tax laws (including tax rates, exemptions, allowances, and thresholds), wage policy, and financial support to public and private enterprises. The authorities will similarly inform the IMF staff of any non-concessional external debt contracted or guaranteed by the central government, the RBM, or any statutory bodies, and any accumulation of new external payments arrears on the debt contracted or guaranteed by these entities.

42. **The authorities will furnish an official communication to the IMF describing program quantitative performance and structural benchmarks within eight weeks of a test date**. The authorities will, on a regular basis, submit information to IMF staff with the frequency and submission time lag as indicated in Table 2.

Table 2. Malawi: Summary of Reporting Requirements

	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Agency
Exchange Rates	D	W	D	RBM
International reserve assets and reserve liabilities of the Monetary Authorities [2]	W	W	M	RBM
Gross international reserves and foreign exchange purchases and sales	D	W	M	RBM
Reserve/base money, OMO transactions, and RBM conversion of ways and means account to government securities	W	W	M	RBM
Broad money	M	M	M	RBM
Central Bank balance sheet	W	W	M	RBM
Consolidated balance sheet of the banking system	M	M	M	RBM
Interest rates [3]	M	M	M	RBM
Excess reserves by banks	M	M	M	RBM
Volume of transactions in the interbank money market and foreign exchange markets and sales of foreign currencies by RBM to commercial banks	D	W	W	RBM
Government securities auction results	W	W	W	RBM

Table 2. Malawi: Summary of Reporting Requirements (continued)

Spread between exchange bureau midrate and the official exchange midrate	W	M	W	RBM
Central government domestic borrowing	M	M	M	RBM
Holdings of local registered stocks, treasury bills, treasury notes and other government securities	M	M	M	RBM
Detailed issue and maturity profile for all government securities	M	M	M	RBM
Financial soundness indicators by banks	Q	Q	…	RBM
RBM foreign exchange cash flow	M	M	M	RBM
Bank statements of the agricultural SWAp account held at RBM	M	M	…	RBM
Annual financial reports of the 8 major parastatals[4]	A	A	…	MOF
Borrowing of the 8 major parastatals [4]	SA	SA	…	MOF
Quarterly report on government domestic arrears	Q	Q	…	AG
Comprehensive list of tax and non-tax revenues	M	M	M	MOF
Fiscal table (GFS based), including revenue, grants, expenditure, balance and composition of financing of the central government [5, 6, 7]	M	M	M	MOF
Expenditure for domestically financed capital projects	M	M	M	MOF

Table 2. Malawi: Summary of Reporting Requirements (concluded)

Data on Joint Funds on health and education	M	M	…	MOF
Stocks of public sector and public-guaranteed debt [6]	Q	Q	Q	MOF
New external loans contracted or guaranteed by the government and disbursement schedule [6]	Continuous	Continuous	Continuous	MOF
Quarterly external debt service (actual and projections)	Q	Q	…	MOF
Debt-service payments on domestic debt (outturn and projections)	M	Q	Q	MOF
Accumulation of new domestic government arrears	M, Q	M, Q	M, Q	MOF
Report on IMF program performance	Q	Q	…	MOF
Consumer Price Index and monthly statistical bulletin	M	M	M	NSO
Exports and Imports of Goods and services, and subcomponents.	M	M	Q	NSO
Balance of payments	A	A	A	NSO
GDP/GNP, by activity and expenditure, at constant and current prices	A	I	A	NSO

[1] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Semi-annually (SA); Irregular (I).
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Both market-based and officially-determined, including discount rates, money market rates, interbank money market rate, rates on treasury bills, notes and bonds.
[4] Agriculture Development and Marketing Corporation, Electric Supply Company of Malawi, Electricity Generation Company of Malawi, Malawi Housing Corporation, National Oil Company of Malawi, Northern Regional Water Board, Lilongwe Water Board, and Blantyre Water Board.
[5] Foreign and domestic banks, and domestic nonbank financing.
[6] Detailed information on the amounts, currencies, terms and conditions, including debt contracted or guaranteed by the RBM or any other agency on behalf of the central government.
[7] Provided no more than four weeks after the end of each month.

INTERNATIONAL MONETARY FUND

MALAWI

November 7, 2019

SECOND AND THIRD REVIEWS UNDER THE THREE-YEAR EXTENDED CREDIT FACILITY ARRANGEMENT AND REQUESTS FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA AND AUGMENTATION OF ACCESS—INFORMATIONAL ANNEX

Prepared By

The African Department
(In Consultation with Other Departments, the World Bank, and the African Development Bank)

CONTENTS

RELATIONS WITH THE FUND

(As of August 31, 2019)

Membership Status

Joined: July 19, 1965; Article VIII

General Resources Account:

	SDR Million	%Quota
Quota	138.80	100.00
Fund holdings of currency (exchange rate)	136.36	98.24
Reserve tranche position	2.44	1.76

SDR Department:

	SDR Million	%Allocation
Net cumulative allocation	66.37	100.00
Holdings	2.82	4.25

Outstanding Purchases and Loans:

	SDR Million	%Quota
ECF Arrangements	150.86	108.69

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF	04/30/2018	04/29/2021	78.08	22.30
ECF	07/23/2012	06/29/2017	138.80	138.80
ECF	02/19/2010	07/22/2012	52.05	13.88

Overdue Obligations and Projected Payments to Fund[1]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2019	**2020**	**2021**	**2022**	**2023**
Principal	3.30	13.80	18.44	25.81	22.37
Charges/Interest	0.15	0.59	0.59	0.59	0.59
Total	3.44	14.38	19.02	26.40	22.95

[1] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	December 2000
Assistance committed	
by all creditors (US$ Million)[1]	1,057.00
Of which: IMF assistance (US$ million)	45.27
(SDR equivalent in millions)	33.37
Completion point date	Aug 2006
Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	33.37
Interim assistance	11.57
Completion point balance	21.80
Additional disbursement of interest income[2]	3.82
Total disbursements	37.19

[1] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

[2] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

Implementation of Multilateral Debt Relief Initiative (MDRI):

MDRI-eligible debt (SDR Million)[1]	37.87
Financed by: MDRI Trust	14.53
Remaining HIPC resources	23.34

Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGF**	**Total**
December 2006	N/A	7.91	7.91
September 2006	10.84	19.12	29.96

[1] The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

Implementation of Catastrophe Containment and Relief (CCR): Not Applicable.

Safeguards Assessments:

The 2018 update assessment found that the financial reporting and audit mechanisms continue to adhere to international practices, as noted during the 2016 monitoring visit. However, the RBM's governance arrangements and autonomy continued to be undermined by weak legal provisions, significant credit to the government, and the presence of government officials on the Board and audit committee. Further, risks in the area of foreign reserves management remain elevated due to limits that are inconsistent with leading practices and lapses in oversight.

Implementation of recommendations from the July 2018 updated safeguards assessment has been slower than the timeline envisaged in the assessment. The assessment recommended legal amendments to strengthen the RBM's governance and autonomy which were enacted in 2019 and will be further enhanced with the elimination of the conversion of cash advances into securities as well as, following legal review, legislation needed to eliminate any ambiguity in this regard. Limited progress has been made in addressing concerns over the RBM's reserve management practices, though the authorities have informed staff that steps are being initiated with support from the World Bank. A recent lapse in the RBM's banking for the government suggests a deterioration in controls which the RBM is taking steps to address. An emergency liquidity assistance (ELA) framework is being developed. Staff is continuing to engage with the authorities on these issues.

Exchange Arrangements:

In May 2012, the government liberalized the foreign exchange regime, devalued the kwacha by about 33 percent, and adopted a de jure floating exchange rate regime. Since May 2012, the RBM has not set a target rate and allowed substantial volatility in the exchange rate. However, the U.S. dollar exchange rates showed remarkable stability between October 2016 and April 2019, at a rate of around MK 730/US$. Accordingly, the de facto exchange rate arrangement was classified as "stabilized" and this classification would change should the substantial volatility exhibited since April 2019 persist. Inflows of foreign exchange have allowed for a strong increase in international reserves. The exchange regime is free of restrictions and multiple currency practices.

Article IV Consultation:

The Executive Board concluded the last Article IV consultation with Malawi on April 30, 2018.

Financial Sector Assessment Program (FSAP), Reports on Observance of Standards and Codes (ROSCs), and Offshore Financial Center (OFC) Assessments:

A joint team of the World Bank and the International Monetary Fund visited Malawi under the FSAP program during two missions in July and December 2007. The Financial System Stability Assessment (FSSA) was issued in June 2008 (SM/08/198). An FSAP development module was conducted in mid-2017.

Corporate Governance and Accounting and Auditing ROSC missions visited Malawi in February and June 2007.

An update on the FAD mission on the fiscal transparency module was issued in March 2007. A ROSC on the data module, based on a September 2003 mission, was published in October 2004.

Technical Assistance: (January 2015—September 2019)

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
08/19	MCM	RBM	Cyber risk supervision	Mission
07/19	MCM	RBM	National payment system	Mission
07/19	FAD	MOF/RBM/NSO	Macro-fiscal forecasting	Mission
07/19	STA	NSO	Supply and use tables	Mission
04/19	MCM	RBM	Monetary policy operations	Mission
04/19	STA	NSO	External sector statistics	Mission
04/19	STA	NSO	National Accounts	Mission
04/19	STA	MOF	Government finance statistics	Mission
03/19	MCM	RBM	Local currency bond market	Mission
02/19	FAD	MOF	TSA/IFMIS	Mission
02/19	ICD	RBM	Forecasting and Policy Analysis System	Mission
12/18	FAD	MOF	Revenue administration	Mission
12/18	STA	MOF	Government finance statistics	Mission
12/18	FAD	MOF	Building effective taxpayer registers	Workshop
11/18	STA	NSO	National Accounts	Mission
10/18	FAD	MOF	PFM	Mission
10/18	FAD	MOF	Revenue administration	Mission
10/18	ICD	RBM	Policy analysis and forecasting	Mission
10/18	MCM	RBM	Insurance Supervision and Regulation	Mission
09/18	FAD	MOF	Revenue administration	Workshop
08/18	FAD	MOF	Macro-fiscal forecasting	Mission
08/18	FAD	MOF	PFM/ IFMIS	Mission
06/18	STA	MOF	Government finance statistics	Workshop
06/18	MCM	MOF/RBM	Developing Local Securities Market	Mission
06/18	FIN/LEG	RBM	Central Bank law	Mission
06/18	FAD	MOF	PFM/Budget Execution and Controls	Mission
06/18	FAD	MOF	Strengthening oversight of SOEs	Mission
05/18	STA	NSO	National accounts	Mission
04/18	FAD	MOF	Public Investment Management	Mission
03/18	STA	NSO	National Accounts	Mission
03/18	STA	RBM	Monetary and financial statistics	Mission
03/18	STA	MOF	Government finance statistics	Mission
03/18	FIN/LEG	RBM	Safeguards Assessment Mission	Mission
03/18	FAD	MOF	PFM/ Fiscal risk	Mission
03/18	FAD	MOF	Revenue Administration	Mission
03/18	ICD	RBM	Policy analysis and forecasting	Mission
03/18	STA	RBM	Monetary and financial statistics	Mission
02/18	FAD	MOF	PFM / Financial controls	Mission
02/18	STA	RBM	Monetary and financial statistics	Mission
02/18	FAD	MOF	Customs administration	Mission
01/18	STA	NSO	External sector statistics	Mission
01/18	STA	NSO	Price statistics	Mission
12/17	FAD	NSO	National accounts	Mission

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
12/17	FAD	MOF	Budgeting	Mission
12/17	FAD	MOF	Tax administration	Workshop
11/17	STA	MOF	Government finance statistics	Workshop
11/17	MCM	RBM	Financial sector regulation	Mission
11/17	MCM	RBM	Banking supervision	Mission
11/17	STA	NSO	National account statistics	Mission
11/17	FAD	MOF	Debt management system	Mission
11/17	MCM / WB	RBM / MOF	Debt management strategy	Mission
10/17	STA	MOF	Government Financial Statistics	Mission
09/17	STA	NSO	Price Statistics	Mission
09/17	ICD	RBM	Policy analysis and forecasting	Mission
08/17	FAD	MOF / MOF / NSO	Macroeconomic forecasting	Mission
08/17	ICD	RBM	Policy analysis and forecasting	Mission
08/17	FAD	MOF	Public financial management	Mission
07/17	MCM	RBM	Forex operations and repo market	Mission
05/17	ICD / MCM	RBM	Forecasting / Policy Analysis System	Mission
05/17	FAD	MOF	Customs administration	Mission
05/17	FAD	MOF	Cash management and TSA	Mission
04/17	STA	RBM	Financial soundness indicators	Mission
04/17	FAD	MOF	Compliance risk analysis	Mission
04/17	FAD	MOF	Cash management	Mission
03/17	MCM	RBM	Financial market infrastructure	Workshop
01/17	MCM	RBM	Bank supervisory framework	Mission
01/17	ICD / MCM	RBM	Monetary policy framework	Mission
11/16	FAD	MOF	Taxpayer register	Mission
10/16	FAD	MOF	Risk management in customs	Mission
10/16	ICD / MCM	RBM	Forecasting / Policy Analysis System	Training
09/16	STA	RBM	General Data Dissemination System	Mission
09/16	FAD	MOF	PFM / Financial controls	Mission
08/16	STA	NSO	Consumer price Framework	Mission
07/16	ICD	MOF	Government financial statistics	Training
06/16	STA	NSO	National accounts statistics	Mission
06/16	LEG	RBM	Bank resolution	Workshop
05/16	MCM/ICD	RBM	Monetary policy framework	Mission
04/16	FAD	MOF	PFM	Mission
04/16	MCM	RBM	Basel framework	Mission
04/16	STA	NSO	National accounts statistics	Mission
03/16	MCM	RBM	IT risk	Mission
02/16	LEG	RBM	Safeguard assessment	Mission
02/16	MCM	RBM	Foreign exchange interventions	Mission
01/16	LEG	RBM	AML/CFT supervision	Mission
01/16	FAD	MOF	Tax reform	Mission

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
11/15	MCM	RBM	Interbank money market	Mission
11/15	FAD	MOF	Fiscal reporting	Mission
10/15	MCM	RBM	Repo market and forex swaps	Workshop
10/15	STA	NSO	National accounts statistics	Mission
09/15	FAD	MOF	Pension reform proposals	Mission
09/15	FAD	MOF	Expenditure control, bank reconciliation, and fiscal reporting	Mission
07/15	FAD	MOF	Cash planning and management	Mission
06/15	STA	NSO	Price Statistics	Mission
05/15	FAD	RBM	TADAT Pilot Assessment	Mission
04/15	FAD	MOF	Implementing priority PFM reforms II	Mission
04/15	STA	NSO	National Accounts Statistics	Mission
03/15	LEG	RBM	Helping draft Banking law amendments	Mission
03/15	STA	MOF	Government Finance Statistics	Mission
02/15	STA	NSO	Balance of Payments Statistics	Mission
02/15	STA	NSO	National Accounts Statistics Harmonization	Workshop
02/15	MCM	RBM	Advice on the Implementation of ICAAP/SREP supervisory framework.	Mission
01/15	FAD	MOF	Action plan for implementing priority PFM reforms	Mission

JOINT MANAGERIAL ACTION PLAN

(As of September 19, 2019)

Title	Products	Provisional Timing of Missions	Expected Delivery Date
	A. Mutual Information on Relevant Work Programs		
World Bank work program in the next 12 months	**Analytical and Advisory Activities:**		
	1. Malawi Service Delivery Indicators	Oct 28 – Nov 1, 2019 Nov 25 – 29, 2019	December 2019
	2. Malawi National Electrification Program		October 2019
	3. Impact Evaluation of Emergency Response and Post-Crash Care in Malawi and Tanzania		December 2020
	4. Malawi Mainstreaming Governance and Citizen Engagement		January 2021
	5. Mobilizing Long-Term Finance for Infrastructure	Oct 28 – Nov 1, 2019	December 2019
	6. Malawi MAPS Follow Up		September 2019
	7. Malawi Public Expenditure Review (PER)	Oct 14 – 18, 2019	June 2020
	8. Malawi Economic Monitor 2019-20		June 2020
	9. Malawi: Strengthening National Capacity for a Shock-Responsive Monitoring System		June 2020
	10. Mw-Digital Moonshot and Opportunities in the Digital Economy	Sept 30 – Oct 4, 2019	September 2020
	Lending:		
	1. Mozambique Malawi Regional Interconnector Project	Oct 2 – 9, 2019	September 2019
	2. Platform for National Social Protection Project	Oct 23 – 25, 2019	December 2019
	3. Malawi Resilient Productive Landscapes	Sept 30 – Oct 8, 2019	February 2020
	4. Financial Inclusion and Entrepreneurship Scaling Project	Dec 2 – 6, 2019	February 2020
	5. Governance to Enable Service Delivery	Sept 30 – Oct 10, 2019; Nov 4 – 14, 2019	March 2020
	6. Mpatamanga Hydro Power Project	Oct 2 – 9, 2019	June 2020
	7. Inclusive Access for Rural Transformation		October 2020
	8. Nacala Corridor Trade Project	Oct 21 – Nov 12, 2019	December 2020

Title	Products	Provisional Timing of Missions	Expected Delivery Date
B. Requests for Work Program Inputs			
IMF request to World Bank	1. Updates on WB support to Malawi		Continuous
World Bank request to IMF	1. Regular updates and exchange of views on medium-term macroeconomic and fiscal projections including sharing detailed excel tables on Real, Monetary, Fiscal and External Sectors		Continuous
C. Agreement on Joint Products and Missions			
Joint products in next 12 months	1. Debt Sustainability Analysis (update)		November, 2019

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK

(As of September 2019)

The African Development Bank (AfDB) operations in Malawi date back to 1969. The AfDB Group Malawi Country Office was opened in 2007. As of September 20, 2019, the AfDB had provided significant and diversified support to Malawi, with cumulative commitments worth UA 967 million (about US$1.4 billion) to finance 113 operations, including thirteen studies and two lines of credit.

The AfDB' s Malawi Country Strategy Paper (CSP) covering the period 2018-2022 is fully aligned with the third Malawi Growth and Development Strategy (MGDS III, 2017-22) and the AfDB's corporate priorities in the Long-Term Strategy (LTS, 2013–22) and High 5 priorities.

The current CSP 2018-2022, aims to support the foundations of private sector led growth by investing in infrastructure and promoting diversification and transformation agenda. In this regard, the CSP covers two pillars. Pillar I: *Investing in infrastructure development through energy and transport; and* Pillar II: *Investing in economic transformation by strengthening agriculture value addition and developing water infrastructure*.

The strategic objective of pillar 1 is to improve competitiveness and efficiency of private and public sector, by extending infrastructure, limiting bottlenecks, and reducing investment constraints that increase business transaction costs. The outcomes to this pillar include improved connectivity to local and regional markets, reduced transport cost, increased private sector investment in energy and transport. Similarly, the strategic objective of pillar 2 is to boost economic diversification and build resilience by reducing cost of market entry, underpinning the creation of firms and jobs that contribute to the broadening the tax base and enhancing macro-stability. The outcomes for pillar 2 include increased productivity and production, increased market development and diversification, empowered local communities and improved health and wellness.

Given the rapidly growing population, it is critical that the economy starts creating more economic opportunities that would generate increased revenues for the government to efficiently and effectively provide required social services and public goods while ensuring a dynamic and growing private sector.

Crosscutting themes are mainstreamed into the CSP and are an integral part of lending and non-lending operations. Environment and climate change, skills and training especially amongst the youth, and economic and financial governance will be central cross-cutting areas in operations selected for support.

Since the CSP approval in October 2018, the AfDB has approved USD 113 million *for* 6 operations in the water, agriculture, and roads sectors in line with the CSP priorities. About 91% of the approved resources were secured from the African Development Fund; while the remaining balance came from Nigerian Trust Fund, Global Environmental Facility and Special Relief Fund. The recently approved projects includes: (i) Nkhata Bay Town Water Supply and Sanitation Project

(USD 15 million) in October 2018; Shire Valley Transformation Programme (USD 35 million) in December 2018; (iii) Additional Financing to Sustainable Rural Water and Sanitation Infrastructure Project (USD 2.5million) in May 2019; (iv) Post Cyclone IDAI Emergency Recovery for Malawi (USD 22.5 million) in June 2019; and (v) the Multinational Nacala (Nsipe-Liwonde Rehabilitation) Road Project (USD 37 million) in June 2019. In April 2019, the AfDB has also approved an Emergency Relief Assistance to the tune of USD 1.5 million (USD 1 million to Mozambique and USD 250,000 each to Malawi and Zimbabwe). The grant resources aimed to contribute to Government efforts in meeting the urgent and immediate needs of the households affected by Cyclone IDAI.

Through a strong partnership with the EU, the AfDB has managed to secure 18 million Euros (grant) on 25th February 2019 to co-finance the Multinational Nacala Road Corridor Development Project Phase V. In support of the Nkhata Bay Town Water Supply and Sanitation Project, the AfDB is administering OPEC Fund for International Development (OFID) USD 12 million loan.

The other planned project in the year is the Sustainable Fisheries and Aquaculture Development and Watershed Management Project (USD 13 million) planned to be approved in early October.

These interventions aim at strengthening economic transformation by enhancing agriculture value chains, increasing mechanization, increasing access to finance, improving market linkages and supporting crop diversification. These will underpin new income opportunities for emerging commercial farmers while strengthening linkages to small-scale farmers with increased focus on women and youth. Small industry development will be supported through agro-processing and light industrialization that will contribute to expand the economy and create jobs. The interventions in the water sector are expected to increase capacity of water reservoirs, small dams harvesting schemes, and improve access to potable water to free up time in rural areas especially for women: to allow them focus on other social economic activities. The interventions will support water resource management in key water basins such as Songwe River and Lake Malawi that impact on other sectors, such as energy, agriculture, tourism and fisheries.

In the recent past, the AfDB has also provided Malawi with quick disbursing budget support. Following Government's re-engagement with the IMF and the approval of the US$157 million Extended Credit Facility (ECF) arrangement in July 2012, the AfDB approved an ADF Grant for Crisis Response Budget Support operation, for US$40 million. The AfDB designed the Restoration of Fiscal Stability and Social Protection (RFSSP) program whose objective was to contribute to restoring fiscal stability and enhancing public finance management, as well as support social protection measures to mitigate the adverse social impact of the devaluation of the kwacha and the increases in fuel and electricity prices. To support this agenda, the RFSSP had two components to strengthen: PFM transparency and accountability, and social protection systems.

In 2015, the African Development Fund Board approved a grant of US$30 million for the Protection of Basic Services Program (PBS). This ring-fenced Sector Budget Support was designed to protect critical expenditures in health and education, and improve accountability following suspension of general budget support. The grant was disbursed in one tranche in July 2015. The Food Crisis Response Budgetary Support followed the PBS operation in 2016. The AfDB will continue to coordinate closely with the IMF in the design of its future budget support operations to ensure its programs are underpinned by sound macro-economic policies.

The AfDB has been working with development partners in strengthening Malawi's public finance management (PFM) systems. In support to the implementation of PFM reforms and in strengthening internal control systems following 'cashgate', the AfDB approved two PFM Institutional Support Projects (US$7 million), one of which closed in June in 2018 and the other expected to close in May 2019. Among others, the PFM support is focusing on tax administration reforms (upgrading of the Automated System for Customs Data—ASYCUDA, putting in place a Tax Appeals Tribunal legislative framework, review of the Customs and Excise Act, etc.); public procurement reforms; and strengthening financial management systems, including reviewing the PFM Act, Treasury Instructions, Treasury Funds Management Guidelines, undertaking an audit of Treasury Funds, and strengthening the Integrated Financial Management Information System (IFMIS) oversight, among others.

In terms of private sector support, the AfDB supported a number of private sector projects directly and indirectly through regional operations and private equity (PE) funds. The AfDB approved, in 2017, a USD 300 million long-term senior loan to finance the Nacala Rail and Port Project, which is a regional project. The loan included an allocation of USD 18.1536 million to Central African Railways Company Limited (CEAR) of Malawi. The project will provide Malawi with a more efficient access to a sea port and will therefore lead to a reduction in transportation costs for import and export trade. To complement the Nacala Rail and Port Project and the Nacala Roads Projects and in order to support inclusive growth along the Nacala Development Corridor in Malawi, the AfDB approved a USD 1 million Nacala Rail and Port Value Additional TA Project. The TA project will help local SMEs and farmers take advantage of the road and rail infrastructures by improving on the efficiency and competitiveness of their businesses. The AfDB also approved, in 2016, a soft commodity finance facility of USD 20 million (a regional project) to Meridan Consolidated Investment Limited. The funds approved will be used to purchase soft commodities (i.e. maize, groundnuts, pigeon peas, soya, sesame and beans) directly from small-scale farmers in Malawi, Mozambique and Zimbabwe. Meridan Consolidated Investment Limited is originally a Malawian company that has expanded its operations regionally.

The AfDB has also provided support for non-lending activities, including feasibility studies and analytic work, to inform the design of new operations and policy dialogue. In 2017, the AfDB prepared a feasibility study for Kholombidzo Hydro Power Project, which will provide a foundation for pipeline operations. In the same year, the AfDB financed the feasibility study for establishment of an Agriculture Cooperative AfDB. Based on the findings and recommendations of the feasibility study, the Government of Malawi recently launched the Malawi Agricultural and Industrial Investment Corporation Plc which is a government initiative to establish a development AfDB in the country but being led by the private sector.

In addition, the AfDB is supporting the Private Public Partnership Commission (PPPC) with a grant to build PPP negotiation capacity through a "hot line" arrangement, whereby the PPPC can tap into international legal services to advise on PPP transactions. The AfDB has provided technical assistance to the Malawi Postal Cooperation for the development of the E-Post Strategy and Action Plan. It is to be noted that the AfDB, in recent years, has undertaken a number of analytical studies, including Domestic Resource Mobilization Study for Malawi, and provided TA to the Reserve AfDB of Malawi to strengthen capacity in macro-economic forecasting; prepared a Public Expenditure Review with the World Bank and other development partners; and provided support for undertaking of the Expenditure Tracking Study for Malawi.

Looking forward, the AfDB plans to scale up its lending to the energy sector with a view to address power shortages. The pipeline of energy sector projects includes the Songwe River Basin Development Project, the Malawi-Zambia Power Inter-connector Project, and the Kholombidzo Hydro Power Project. The AfDB continues to engage with the World Bank and other partners for co-financing arrangements of its pipeline operations. In view of this, the AfDB is taking the lead in mobilizing donor resources and private finance for the Songwe Hydro Power Project, a multinational project with Tanzania. It will also promote private investment in the energy sector, through PPPs and the use of innovative financing instruments, such as Partial Risk Guarantees.

For the year beyond 2019, the AfDB also plans to support the Enhancing Competitiveness & Improving Access to Digital Project and the Multinational North-South Road Corridor Project (Salima – Dwangwa Road).

The AfDB shall in 2020 commence the mid-term review of the Country Strategy Paper (2018-2022), to take stock of achievement of results and aligned with Malawi's new National Development Plan and the Bank's Long Term Strategy, in particular, the "High Fives" priorities, which include "Light up and Power Africa", "Feed Africa", "Industrialize Africa", "Integrate Africa" and "Improve the Quality of Life for the People of Africa".

INTERNATIONAL MONETARY FUND

MALAWI

November 7, 2019

SECOND AND THIRD REVIEWS UNDER THE THREE-YEAR EXTENDED CREDIT FACILITY ARRANGEMENT AND REQUESTS FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA AND AUGMENTATION OF ACCESS—DEBT SUSTAINABILITY ANALYSIS[1]

Approved By
David Robinson and S. Ali Abbas (IMF) and Marcello Estevão (IDA)

Prepared by the staffs of International Monetary Fund and the International Development Association (IDA)

Malawi: Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	*Moderate*
Overall risk of debt distress	*High*
Granularity in the risk rating	*Some space to absorb shocks*
Application of judgement	*No*

Malawi's external debt is assessed to be at a moderate risk of debt distress, but with some space to absorb shocks. Results of the model show that two external debt burden indicators (that is, PV of debt-to-exports ratio and debt service-to-exports ratio) would breach the thresholds determined by Malawi's debt carrying capacity[2] under the exports shock.

[1] The analysis presented in this document is based on the debt sustainability framework for low-income countries approved by the Boards of both the International Monetary Fund and the International Development Association.

[2] Malawi's debt carrying capacity is classified as "weak" according to the composite indicator score determined by the World Bank's Country Policy and Institutional Assessment (CPIA) Index and other key fundamentals including real GDP growth, import coverage of reserves, remittances as percent of GDP, and growth rate of the world economy. The relevant thresholds for external debt under this category are: 30 percent for PV of debt-to-GDP ratio, 140 percent for PV of debt-to-exports ratio, 10 percent for debt service-to-exports ratio, and 14 percent for debt service-to-revenue ratio. The benchmark on total public debt (sum of public and publicly guaranteed external debt and public domestic debt) is 35 percent for PV of total debt-to-GDP ratio.

Malawi is assessed to be at high overall risk of debt distress. This mainly reflects increasing amounts of domestic debt contracted at high interest rates during recent years. The present value of total public debt to GDP is projected to decline throughout the program period but would breach the benchmark until 2027.

The projected borrowing path and debt policies remain broadly unchanged since the last DSA.[3] *Budget credibility and fiscal discipline should be strengthened to avoid accumulation of domestic debt at high interest rates. Close attention will be needed on the financing terms of any proposed infrastructure investments given limited headroom for further borrowing. To enhance resilience to shocks, efforts should be stepped up to further diversify the economy, particularly exports, broaden the revenue base, and strengthen public financial management*

PUBLIC DEBT COVERAGE

1. **Public debt used for the DSA is public and publicly guaranteed (PPG) external and public domestic debt, covering debt contracted and guaranteed by the central government and the Reserve Bank of Malawi (RBM).** Due to data limitations, it does not include debt held by state and local governments, other elements in the general government (such as the social security fund and extra budgetary funds), or non-guaranteed state-owned enterprise (SOE) debt. Considering the limited debt coverage, the contingent liability of the general government is assumed to be 2 percent of GDP (whereas, it is assumed to be zero for many countries). However, the authorities are committed to strengthening the oversight and monitoring of SOEs, including conducting pilot audits of the largest SOEs, publishing consolidated annual reports on SOEs, and developing a prototype SOE database over the next few years (staff report Table -11a, ¶19 and MEFP ¶18). These steps will help gradually broaden the public debt coverage. For the current DSA, the stress tests, described below, include an adjustment to reflect the portions of the public sector not captured in the reported debt data (Text Table 1).

[3] IMF Country Report No. 18/336 Annex II.

Text Table 1. External and Public DSAs: Coverage of Public Debt and Design of Contingent Liabilities (Tailored) Stress Tests

	Subsectors of the public sector	Check box
1	Central government	X
2	State and local government	
3	Other elements in the general government	
4	o/w: Social security fund	
5	o/w: Extra budgetary funds (EBFs)	
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	

1	The country's coverage of public debt	The central government, central bank, government-guaranteed debt		
		Default	Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0 percent of GDP	2	Limited debt coverage.
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	2	
4	PPP	35 percent of PPP stock	0.00	
5	Financial market (the default value of 5 percent of GDP is the minimum	5 percent of GDP	5	
	Total (2+3+4+5) (in percent of GDP)		9.0	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

BACKGROUND ON DEBT

2. **Malawi's public and publicly guaranteed (PPG) external debt stood at about US$2.15 billion (31.2 percent of GDP) in 2018**, up from $2.04 billion in 2017 (32.8 percent of GDP). The increase in PPG external debt during 2018 mainly reflects $127 million of new disbursements (with $97 million from multilaterals and $30 million from bilateral creditors) and principal payments of about US$50 million.

3. **Public external debt is held mainly by multilateral creditors** (79 percent of total, Text Table 2). The main provider is the International Development Association (IDA) followed by the African Development Fund (ADF) and the IMF. China and India are the main bilateral creditors.[4] Public external debt at end-2018 was concessional with an average grant element above 35 percent.

4. **New concessional external loans signed in 2019 as of end July ($124.5 million, mainly from multilateral creditors) are financing priority infrastructure projects.** They cover water and sanitation, irrigation, agricultural commercialization, financial advancement for rural markets, and digitalization.

[4] Data on private external debt remains unavailable, but the amounts are not believed to be large.

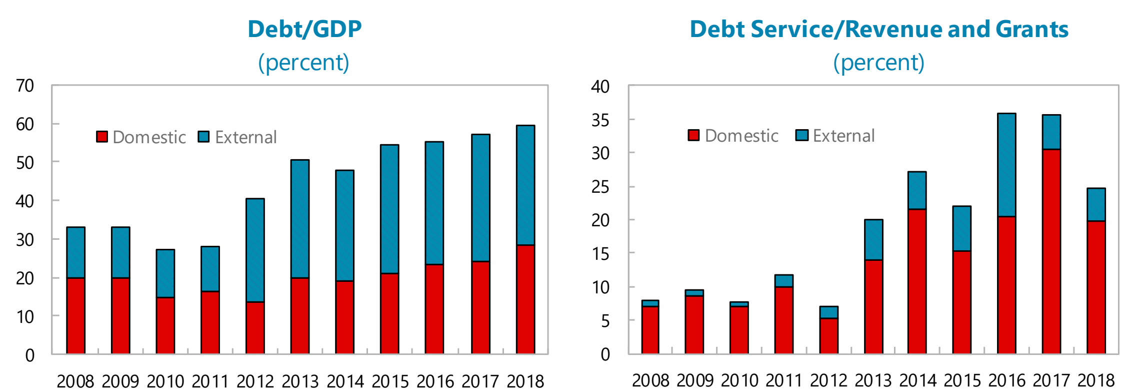
Text Table 2. Composition of Public and Publicly Guaranteed Medium- and Long-Term External Debt

(Million U.S. dollars)

	2015		2016		2017		2018	
	Actual	Share	Actual	Share	Actual	Share	Actual	Share
Multilateral	1,172	73	1,293	75	1,584	78	1,708	79
IDA	590	37	642	37	860	42	919	43
ADF	229	14	248	14	290	14	325	15
IMF	163	10	206	12	224	11	222	10
IFAD	72	4	73	4	77	4	79	4
Other multilateral	119	7	124	7	133	6	163	8
Bilateral	440	27	426	25	437	21	424	20
China	243	15	227	13	236	12	220	10
India	152	9	147	9	142	7	145	7
Others	45	3	52	3	58	3	59	3
Commercial	0.4	0	0	0	0	0	0	0
Guarantees to SOEs	n.a.	n.a.	n.a.	n.a.	20	1	20	1
Total	1,612	100	1,719	100	2,041	100	2,151	100

Sources: Malawian authorities and IMF staff calculations.

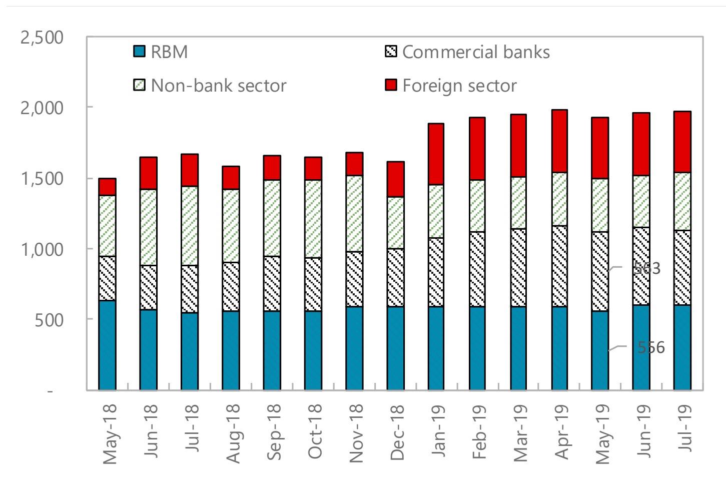
Text Figure 1. Public and Publicly Guaranteed Debt



Sources: Malawian authorities and IMF calculations.

5. **Public domestic debt is held by commercial banks, the non-bank financial sector, and the RBM.** As noted in the previous DSA, the recent spike in public domestic debt reflects a progressive shift of debt from external to domestic borrowing during recent years (Text Table 3, Text Figure 1). Between July 2018 and July 2019, the RBM's share of outstanding treasury bills and notes declined from 33.0 percent to 30.5 percent while commercial banks' share increased from 20.1 percent to 26.9 percent (Text Figure 2).

Text Figure 2. Holdings of Treasury Bills and Notes
(at face value, billions of Kwacha)



Sources: Malawian authorities and IMF staff calculations.

6. **Public domestic debt, 28.4 percent of GDP at end-2018, is expected to edge up to 32 percent in 2019**—7 percentage points higher than envisaged in the previous DSA. The primary deficit (net of budget support and dedicated grants) in FY 2018/19 was
3.4 percent compared to the previously programmed level of 1.1 percent, mainly due to faster than envisaged implementation of rural electrification and domestically-financed development spending planned for FY 2019/20, expenditure overruns related to ensuring safety during elections and post-election protests, and disaster relief after Cyclone Idai. The current DSA continues to incorporate guarantees to SOEs of MK 17 billion (0.4 percent of GDP).

7. **As of July 2019, nonresidents held about MK 428 billion kwacha-denominated Treasury Notes** (28 percent of total or about 7.5 percent of projected 2019 GDP). Due to difficulties in monitoring such debt, the current DSA uses a currency-based definition for domestic/external debt, classifying the kwacha-denominated debt owed to nonresidents as domestic. The terms of these treasury bills/notes held by nonresidents and residents are the same.

Text Table 3. Composition of Gross Domestic Debt
(Percent of GDP)

	2012	2013	2014	2015	2016	2017	2018
Treasury bills at cost value	9.0	9.1	6.9	6.2	5.8	5.6	10.0
Treasury notes	2.7	1.8	5.4	9.6	12.9	15.1	15.8
Local registered stocks (LRS)	0.20	0.07	0.04	0.00	0.02	0.00	0.00
Ways and means advances from RBM	1.7	5.2	3.0	0.9	0.9	1.0	1.4
Promissory notes	0.1	3.6	3.7	4.2	3.7	2.3	0.8
Commercial bank advances	0.100	0.007	0.005	0.019	0.004	0.004	0.001
Gurantees to SOEs	n.a.	n.a.	n.a.	n.a.	n.a.	0.374	0.336
Total (including gurantees to SOEs)	**13.8**	**19.8**	**19.0**	**21.0**	**23.3**	**24.2**	**28.3**

Sources: Malawian authorities; IMF staff estimates.

BACKGROUND ON MACRO FORECASTS

8. **The medium- and long-term macroeconomic framework underlying this DSA is consistent with the scenario presented in the Staff Report for the Second and Third Reviews of the ECF arrangement** (Text Table 4 and Box 1). To compensate for expenditure overruns in FY 2018/19 and rein in the debt buildup, while accommodating for large post-flood recovery and reconstruction needs following Cyclone Idai, the current DSA maintains a domestic primary balance of 0.9 percent of GDP in FY 2019/20- a 2.1 percentage point improvement relative to FY 2018/19. The improvement is achieved mainly through higher tax revenues (e.g., improved revenue collection, impact of expeditiously implemented tax policies), reduced goods and services spending (including the unwinding of spending related to the holding of elections) while prioritizing post-cyclone rehabilitation and aligning capital spending with implementation capacity while prioritizing resilient reconstruction. Efforts to enhance SOE oversight and monitoring will also help generate SOEs' revenue generation capacity, ensure more efficient spending and public service delivery, and reduce potential transfers and eliminate bailouts. It is, however, a 0.4 percentage point loosening relative to the first review under the ECF arrangement, reflecting a 0.2 percent of GDP shortfall in domestic revenues and about 0.3 percent of GDP in increased spending (including 0.2 percent of GDP in for post cyclone rehabilitation,1.5 percent of GDP for reconstruction, and 0.5 percent of GDP for additional security partially offset by 1.9 percent of GDP in spending cuts or reprioritization).

Text Table 4. Macroeconomic Forecast and Assumptions
(Previous and Current DSAs)

Year	Real GDP growth (percent)		Primary deficit (percent of GDP)		Change in public debt (percent of GDP)		Current account (percent of GDP)		FDI (percent of GDP)	
	Previous	Current	Previous	Current	Previous	Current	Previous	Current	Previous	Current
2016	2.3	2.3	2.4	2.4	1.1	0.7	-13.0	-18.5	3.1	2.1
2017	4.0	4.0	3.6	2.1	2.1	2.0	-11.1	-22.3	2.1	2.0
2018	3.2	3.2	0.3	2.1	-0.3	2.5	-9.3	-20.6	2.0	2.3
2019	4.0	4.5	-1.0	2.2	-1.2	2.2	-7.6	-18.4	2.1	2.7
2020	5.0	5.1	-0.2	-0.6	-0.8	-1.8	-7.9	-17.2	2.3	3.0
2021	5.5	5.5	-0.3	-0.1	-1.4	-1.9	-7.7	-16.8	2.4	3.4
2022	6.0	6.0	-0.4	-0.3	-2.0	-4.2	-7.7	-15.7	2.5	3.7
2023	6.5	6.5	-0.6	-0.5	-2.2	-3.8	-7.6	-14.8	2.5	3.8
2024	6.5	6.5	-0.2	0.0	-2.0	-3.0	-7.9	-14.0	2.5	3.9
Avg 2024-38	6.5		0.1		-1.4		-7.1		3.1	
Avg 2025-39		5.6		0.3		-1.2		-13.4		4.3

Sources: Malawian authorities and IMF staff calculations and projections.

Box 1. Baseline Macroeconomic Assumptions

Real GDP growth is projected to rise to 4.5 percent this year, edge up to 5.1 percent next year, and gradually stabilize at 5.5 percent over the long term. These growth prospects are predicated on recent land reforms that will facilitate the use of irrigation infrastructure as well as further significant improvements in irrigation infrastructure and cropping techniques (including diversification away from maize production), enhanced electricity generation, better road and telecommunications networks, and greater access to finance for the private sector. It is also assumed that the quality and capacity of the government's public investment and debt management steadily improves, beginning with the reforms under the current ECF arrangement.

Inflation is projected to moderate below 9 percent by end-2019 (reflecting lower international fuel prices and improved inflation expectations) and continue on a gradual disinflation path to reach 5 percent by 2024. Tight fiscal and monetary policies are expected to continue anchoring inflation expectations.

The exchange rate is projected to remain constant in real effective terms.

Private sector credit growth is expected to continue picking up this year thanks to improved credit demand and gradually strengthen to about 16 percent over the medium term in line with stronger real growth.

The tax revenue to GDP ratio is anticipated to edge up by 0.6 percentage points during FY 2019/20 and gradually rise in the medium to long term, assuming the implementation of a mix of tax policy measures (streamlining various tax incentives, expanding the VAT base and improving SME taxation) and tax administration measures (rollout of the Integrated Tax Administration System and improving tax compliance).

External debt will be mainly contracted with multilateral creditors on concessional terms.

Box 1. Baseline Macroeconomic Assumptions (Concluded)

New disbursements on external loans. The disbursements for FY 2018/19 were broadly in line with expectations. Project capital spending covered by external loans is projected to remain at 3.9 percent of GDP in FY 2019/20 and rise slightly in subsequent fiscal years.

The current account deficit is projected to narrow only gradually, reflecting large and persistent import needs partly offsetting the impact of lower fuel import prices and steady growth of non-traditional exports.[1]

Gross official reserves (at $690 million as of end-July) are expected to increase to about $777 million at year-end, covering 2.9 months of next year's imports. Over the medium term, reserves are projected to gradually rise, covering 4.1 months of imports by 2024.

Net domestic financing. It is assumed that the government's net domestic financing moderates to 4.0 percent in FY 2019/20, following peaks above 6 percent in FY 2017/18 – 19/20. By FY 2023/24, net domestic financing is expected to be contained within 1 percent of GDP.

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[1] Fund staff has adopted the Malawi National Statistics Office's (NSO) trade data based on its improved reliability. Previously, the IMF's reported series was based on staff estimates. Consequently, the IMF's reported current account deficit widened for 2017 from 11.1 to 25.6 percent of GDP (reflecting export shares revised downward by 10.6 percent of GDP and import shares revised upward by 3.8 percent of GDP); and for 2018 from 9.3 to 20.6 percent of GDP (reflecting export shares revised downward by 11.5 percent of GDP and import shares revised up by 4 percent of GDP and services and unrequited transfers revised upward by 4.2 percent of GDP). Errors and omissions were adjusted by offsetting amounts, leaving the overall balance unchanged. Future TA missions on capital and financial accounts' statistics may result in reclassification of this offsetting adjustment.

9. **In Malawi, one of the most important sources of financing the current account deficit has been capital account flows,** consisting of project grants, dedicated grants, and off-budget support, which totaled around 6 percent of GDP over the past 5 years. These flows are expected to average at 5-6 percent of GDP over the medium term. This, combined with price and exchange rate factors, lead to large negative residuals going forward (Table 1).

10. **Over the medium to long term, external financing in the form of project support loans is expected to gradually increase.** There is an upside risk that the pace of this increase may accelerate if the economy's absorption capacity increases faster than expected. The grant element of project loans will remain relatively high over the forecast period, with no access to market financing. In line with a strengthening of Malawi's external position and ability to service external debt, project and dedicated grants are expected to decline to less than one percent over the long term, with no resumption of budget support operations assumed beyond the World Bank disbursement in FY 2019/20 for disaster relief and reconstruction.

11. The realism tools suggest that the baseline macroeconomic assumptions are reasonable (Figure 4).

- *The total fiscal adjustments* (reduction in primary deficit) are projected at 2.3 percent of GDP between 2018 and 2021. It lies in the middle of the top quartile based on the historical distribution of fiscal adjustment among low-income countries. Continued donor support would help stabilize the economy and boost private sector confidence, and reforms under the ECF arrangement would support an improved business environment and attract more FDI. Moreover, reforms to tax policy and administration would increase transparency of business processes, reduce corruption, strengthen compliance, and raise tax revenue. Higher tax revenue will in turn better support much needed high-quality social sector spending, helping achieve the SDGs.

- *The projected growth path* lies above what is implied by assuming only a fiscal impact from the last observed growth rate (which is 3.2 percent in 2018). However, as discussed in the staff report ¶18, the fiscal consolidation in FY 2019/20 is not expected to have a material impact on economic growth due to the composition of the consolidation measures. The baseline medium-term growth forecasts also build in significant improvements in the drivers of growth, which will help lift growth potential to a level significantly higher than its historical average. These improvements include more robust agricultural production which constitutes around 30 percent of GDP (owing to improvement in irrigation infrastructure, cropping techniques and diversification of producing crops), enhanced electricity generation (from new solar and hydro sources and a new interconnection with Zambia), better road and telecommunication networks, improved access to finance, and timely implementation of structural reforms that lower the cost of doing business, improve policies and governance, and reduce vulnerabilities to corruption, boosting private sector involvement and donor confidence. However, there are substantial downside risks. External risks include adverse weather, infestations, worsened terms of trade, while internal risks include intensified governance challenges and weaker-than-expected reform implementation.

- *Private investment rates* are expected to remain broadly unchanged starting in 2020, while *public investment rates* are trending up to 6.8 percent in 2024. For this year, domestically financed development spending has been higher than expected, raising public investment rates. The projected 5-year average *contribution of government capital to real GDP growth* is also expected to remain broadly unchanged from the last DSA, but higher than its historical average partly due to better absorption capacity to implement larger public investments.

COUNTRY CLASSIFICATION AND DETERMINATION OF SCENARIO STRESS TESTS

12. Malawi's debt carrying capacity is classified as remaining weak. The classification of the debt carrying capacity is guided by the composite indicator (CI) score. The CI, in turn, is determined by the World Bank's CPIA and other variables from the macroeconomic framework, such as real GDP growth, import coverage of reserves, remittances as percent of GDP, and growth of the world economy. Malawi's CI based on the current vintage (2018 CPIA and 2019 April WEO) is 2.72, above the threshold value of 2.69, however, considering the lower CI of 2.64 based on the previous vintage, the debt carrying capacity remains "weak".[5] The four external debt burden thresholds and the total public debt benchmark are determined by this classification of the debt carrying capacity (Text Table 5).

Text Table 5. Composite Indicator and Threshold Tables

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	140
GDP	30
Debt service in % of	
Exports	10
Revenue	14

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	35

New framework			
	Cut-off values		
Weak	CI ≤	2.69	
Medium	2.69	≤ CI ≤	3.05
Strong	CI >	3.05	

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	140
GDP	30
Debt service in % of	
Exports	10
Revenue	14

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	35

New framework			
	Cut-off values		
Weak	CI ≤	2.69	
Medium	2.69	< CI ≤	3.05
Strong	CI >	3.05	

[5] An upgrade of the debt carrying capacity from "weak" to "moderate" requires the CI to be above the threshold of 2.69 for at least two consecutive vintages.

13. There are two tailored stress tests:

- One tailored stress test combines contingent liabilities of a one-time debt shock (equivalent to 9 percent of GDP) in 2020, to capture the potential impact of limited public debt coverage (2 percent of GDP, instead of the default level of zero) and contingent liabilities from SOEs (equal to the default level of 2 percent of GDP—the medium SOE external liability identified by a Fund staff survey in 2016) and the need for bank recapitalization (equal to the default level of 5 percent of GDP—the average cost to the government of a financial crisis in a low-income country since 1980). Malawi's experience in recent years, such as the recapitalization of the RBM due to exchange rate devaluation and the Agricultural Development and Marketing Corporation (ADMARC) bailout, has illustrated that the materialization of contingent liabilities can contribute to an unexpected increase in the debt-to-GDP ratio.

- The second tailored stress test is a natural disaster induced one-off shock (of 10 percent of GDP) to external PPG debt-to-GDP ratio in 2020. While Malawi is not on the list of Fund's natural disaster-prone countries,[6] judgment was applied as the country is historically vulnerable to weather-related shocks—Malawi recently suffered from three consecutive weather shocks over two years (drought, floods, and a cyclone)—two of which resulted in a sharp increase in food insecurity, triggering a humanitarian crisis. Weather-related natural disasters are assessed to be the main driver of the unexpected changes in debt (Figure 3).

EXTERNAL DSA

14. Under the baseline scenario, all debt burden indicators remain below their indicative thresholds. The PPG external debt is projected to peak at 29.8 percent of GDP in 2019, with a PV of debt-to-GDP ratio peaking at 19 percent in 2019. The PV of PPG external debt is expected to decline gradually to around 16 percent over the long term. The debt service-to-exports ratio is expected to average around 7 percent in the next six years and gradually decline to about 4 percent over the longer term.

15. Under the historical scenario, external debt is projected to increase. This scenario envisages real GDP growth, the primary balance-to-GDP ratio, the GDP deflator, the non-interest current account, and net FDI flows permanently remain at their historical levels. However, as noted in the previous DSA, the likelihood is low for Malawi to repeat its history by running high and protracted current account deficits in the medium to long term. FDI inflows are expected to pick up steadily as macroeconomic stability is entrenched, and the business environment improves.

[6] This list is based on the IMF Policy Paper "Small states' resilience to natural disaster and climate change—role for the IMF" (December 2016).

16. Under the standard and tailored stress test scenarios, all but two debt burden indicators remain below their indicative thresholds. An export shock (nominal export growth set to its historical average minus one standard deviation) in 2020 and 2021, equivalent to a decline of 8 percent each year, is the most extreme shock for PV debt to GDP, PV debt and debt service to exports ratios. Under this shock both PV debt-to-exports and debt service-to-exports ratios would increase above their indicative thresholds over the medium term (Figure 1, Table 1, and Table 3).

OVERALL RISK OF PUBLIC DEBT DISTRESS

17. Total public debt is projected to rise to 61.8 percent this year, from 59.5 percent in 2018. This increase reflects a 1-percentage-point decrease of PPG external debt and a 3.7 percentage point increase of public domestic debt. Public domestic debt is expected to peak at 32 percent this year, before gradually declining to 21.3 percent by 2024, supported by continuous improvements in primary balances (Figure 3). As the RBM has stopped financing the central government deficit (RBM financing is limited to intra-year liquidity management), all net domestic financing will be met by commercial banks and non-banks. Guided by a multi-year strategy, the RBM will further unwind its holdings of government securities to be absorbed by private sector investors as the domestic debt market continues to develop.

18. Under the baseline, the PV of the total debt-to-GDP ratio is projected to remain continuously above the benchmark throughout 2026. This path is broadly unchanged from that envisaged in the last DSA—where the PV of total debt was expected to decline below 35 percent of GDP by 2026. The larger than previously envisioned domestic primary deficit for FY 2018/19 (-1.2 percent of GDP) is more than offset by corrective measures that are anticipated to produce domestic primary surpluses in the following years (0.9 percent of GDP in FY20/21 and around 2 percent of GDP in each of the next three fiscal years).

19. Under all the standard and tailored stress test scenarios, the PV of the total debt-to-GDP ratio remains above the benchmark through 2023, sometimes even well above it. The natural disaster shock constitutes the most extreme shock which elevates the PV of the total debt-to-GDP ratio to 59 percent and above 40 percent even in 2029. The real GDP growth shock is the most extreme shock for the PV of debt-to-revenue ratio and is expected to raise PV of debt by nearly 256 percent of revenue in the peak year of 2021 (Figure 2, Table 2, and Table 4). The growth shock is the most extreme shock for the debt service-to-revenue ratio: lower growth of 2.5 percent for 2020 and 2021 would raise the debt service to nearly 90 percent in the medium term.

RISK RATING AND VULNERABILITIES

20. Malawi is assessed to have a moderate risk of external debt distress with some space to absorb shocks, but a high overall risk of debt distress due to high public domestic debt (Figure 5). The main risks to the ratings assessment arise from weaker-than-expected policy implementation, limited data coverage, macroeconomic uncertainty (especially from weather shocks), tighter global financial conditions, and a weak global economy which could depress export growth. However, factors such as an adoption of the MTDS (Medium-Term Debt Management Strategy), prospects of stable demand for T-bills/T-notes, and putting in place a domestic revenue mobilization strategy, help mitigate risks keeping the debt outlook sustainable. Recently, the Malawian government developed and published the MTDS with support from WB. It includes cost and risk analysis of alternative borrowing strategies as a guidance to construct the optimal portfolio. Authorities also release a government issuance calendar at the beginning of each financial year to inform market participants and stakeholders. Second, with limited alternative investment opportunities especially with similar liquidity, demand for government bonds is expected to be stable. For many large banks, around 40 percent of their balance sheet is composed of T-bills/T-notes. In addition, the authorities plan to put in place a domestic revenue mobilization strategy that will be incorporated into the FY 2020/21 budget and to undertake a comprehensive review of tax system which are expected to significantly strengthen revenue going forward. All these factors underpin the argument that while the risk of overall debt distress is high, the outlook remains sustainable.

21. Absorption of the shocks that Malawi faces while maintaining macroeconomic stability and debt sustainability will require careful macroeconomic management and difficult policy choices.

- *Increasing fiscal restraint and budget credibility*. Malawi should increase fiscal restraint and budget credibility to contain fiscal deficits and reduce domestic borrowing at high interest rates. Budget credibility requires realistic revenue projections and prioritization of expenditures within the available resource envelope. Moreover, strengthening expenditure prioritization in line with development priorities will be key to achieving higher, more diversified, and resilient growth.

- *Prudent project selection*. Given limited headroom for further borrowing, close attention and prudence should be applied to project identification and the financing terms of any proposed infrastructure investments. The government should focus on projects with high returns that are closely aligned to development priorities and rely on concessional loans that contain borrowing costs. Reining in domestic borrowing, which currently occurs at high interest rates, would also serve this purpose and avoid crowding out of private sector credit expansion.

- *Broadening the revenue base and strengthening public financial management*. Given Malawi's high aid dependency, risks of negative financing shocks in the form of delayed donor support, or lower-than-expected revenue collection remain. Such an environment requires further efforts to maximize the impact of finite domestic resources, including broadening the tax base (e.g., currently under 50 percent of the TINS issues are active tax payers) and strengthening public procurement and public financial management.

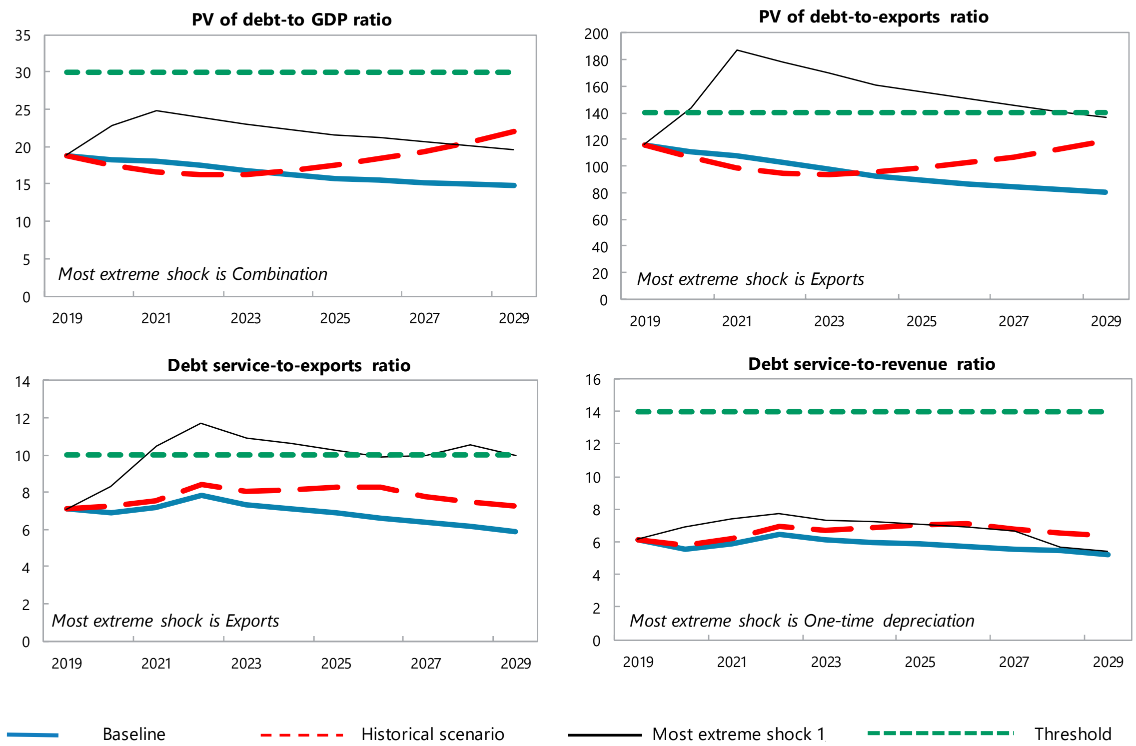
- *Reducing the sovereign-bank nexus*. There is a significant nexus between sovereign debt and the banking system since the RBM and commercial banks have been the main sources of domestic financing for the central government. Such large exposure of bank balance sheets to the sovereign risks a negative feedback loop if fiscal challenges emerge or liquidity conditions tighten.

- *Closely monitoring contingent liabilities.* Contingent liabilities have in general been one of the largest sources of fiscal risk. Malawi's experience in recent years, such as recapitalization of the RBM due to exchange rate devaluation and the ADMARC bailout, has illustrated that the materialization of contingent liabilities can contribute to unexpected increases in the debt-to-GDP ratio, crowding out private credit and jeopardizing debt sustainability. Efforts should be stepped up to estimate, disclose, manage, and contain contingent liabilities, especially those in the financial sector and state-owned enterprises.

AUTHORITIES' VIEWS

22. The authorities agreed with the DSA assessment of the risk of external debt distress remaining "moderate" and the overall risk of debt distress as high. They acknowledged the significant vulnerabilities from growing public domestic debt. Therefore, while the country has a strong need for critical infrastructure projects, the authorities are committed to ensuring that financing of the projects preserves debt sustainability.

Figure 1. Malawi: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2019–2029



Customization of Default Settings	Size	Interactions
Tailored Tests		
Combined CLs	Yes	
Natural Disasters	No	No
Commodity Prices [2/]	n.a.	n.a.
Market Financing	n.a.	n.a.

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.0%	1.0%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	33	33
Avg. grace period	6	6

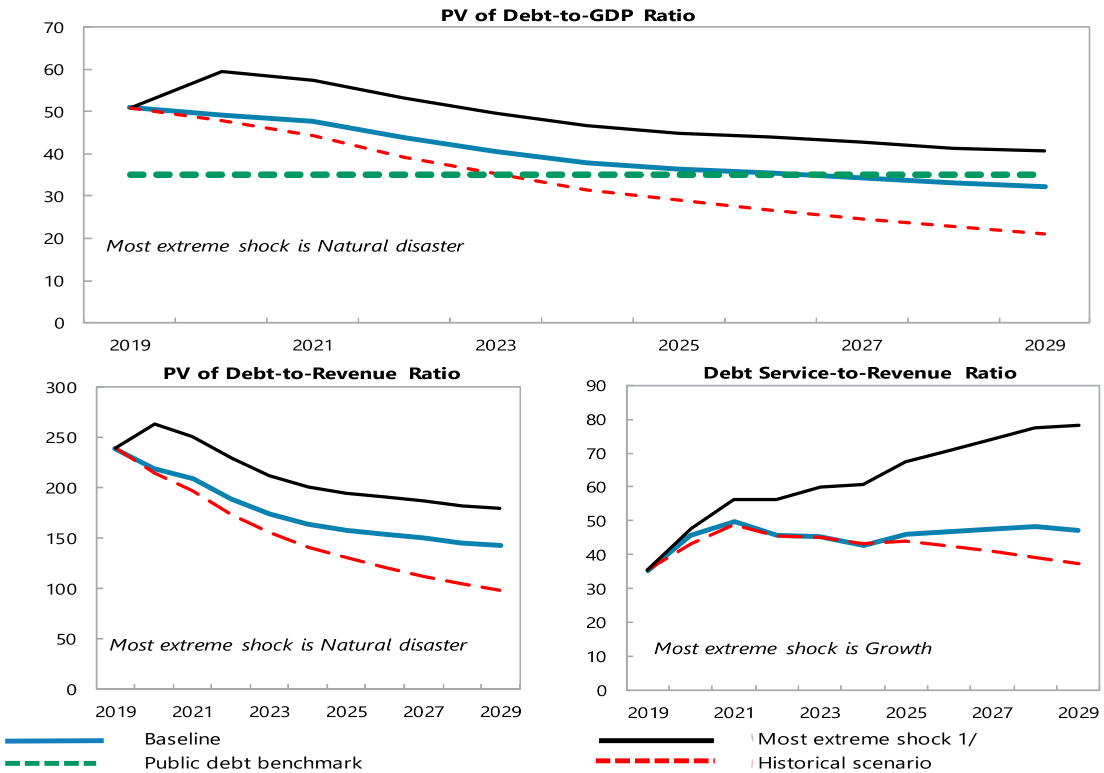
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2029. Stress tests with one-off breaches are also presented (if any), while these one-off breaches are deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF

Figure 2. Malawi: Indicators of Public Debt Under Alternative Scenarios, 2019–2029



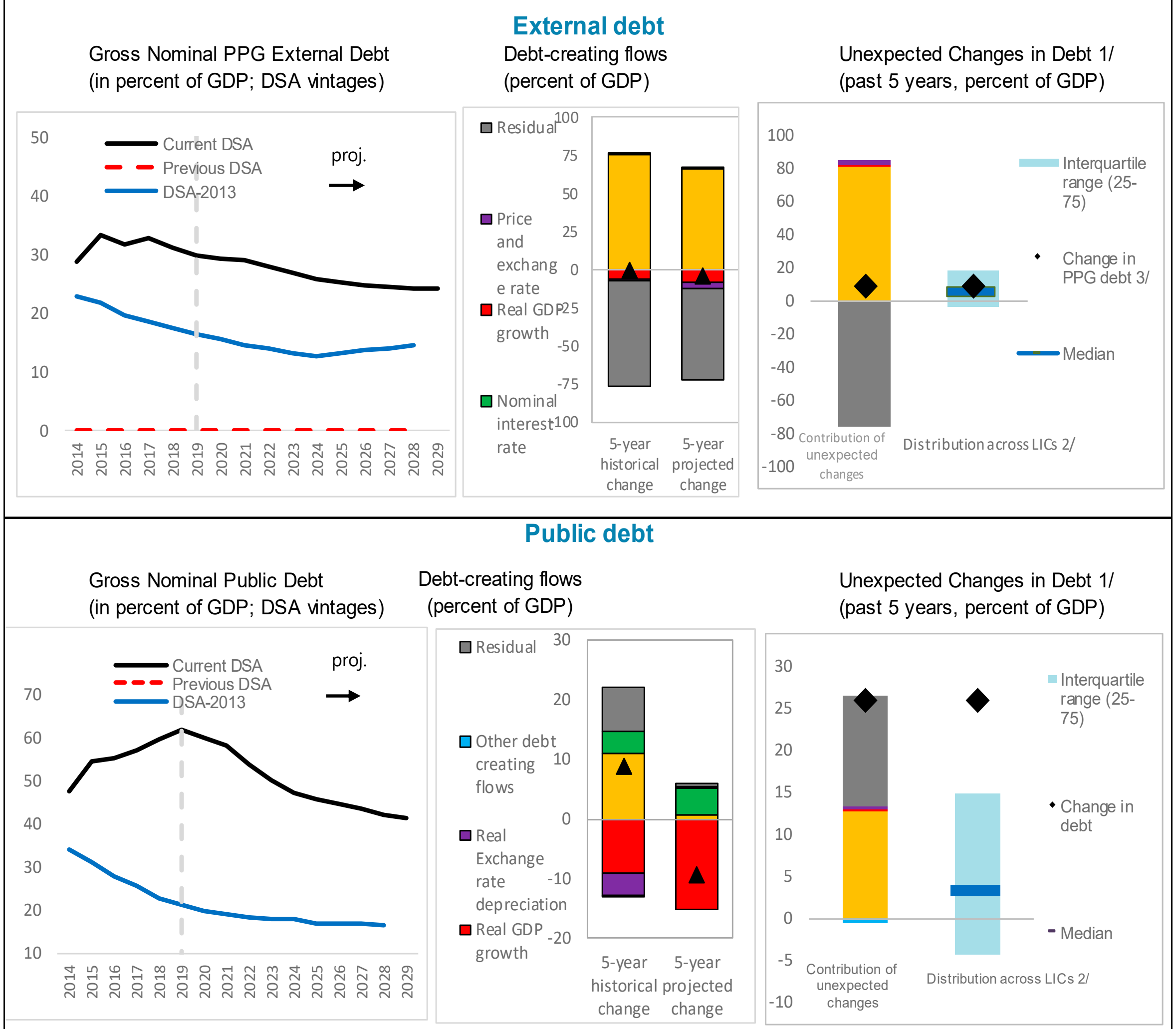
Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	20%	20%
Domestic medium and long-term	24%	24%
Domestic short-term	56%	56%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.0%	1.0%
Avg. maturity (incl. grace period)	33	33
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	7.6%	7.6%
Avg. maturity (incl. grace period)	2	2
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	6%	6.0%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2029. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Malawi: Divers of Debt Dynamics—Baseline Scenario



1/ Difference between anticipated and actual contributions on debt ratios.

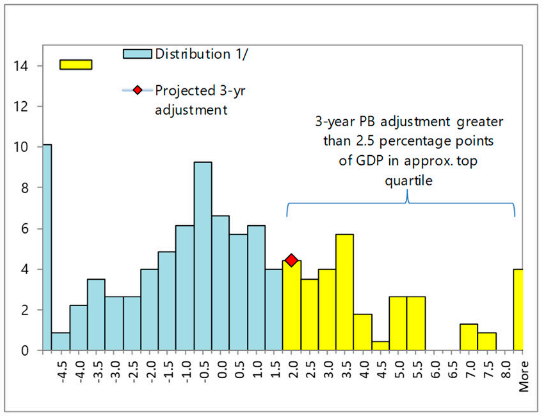
2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

Figure 4. Malawi: Realism Tools

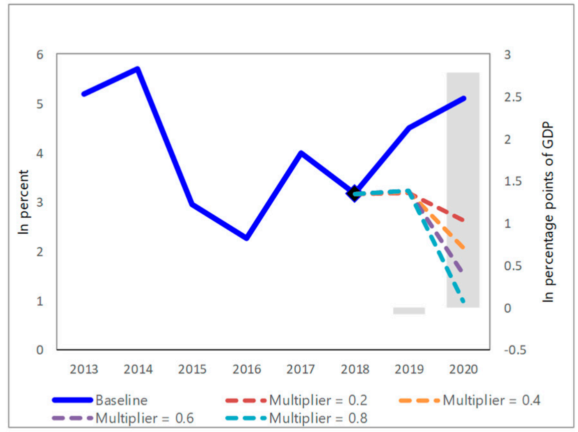
3-Year Adjustment in Primary Balance

(Percentage points of GDP)



1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

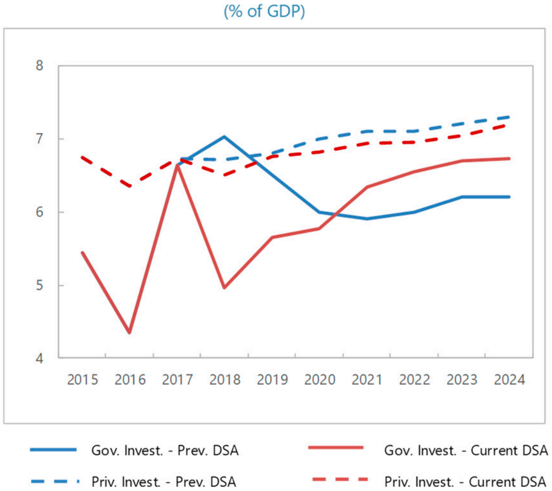
Fiscal Adjustment and Possible Growth Paths 1/



1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates

(% of GDP)



Contribution to Real GDP growth

(percent, 5-year average)

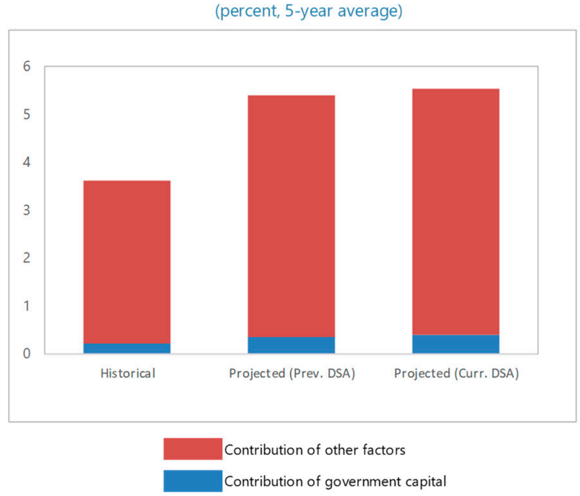
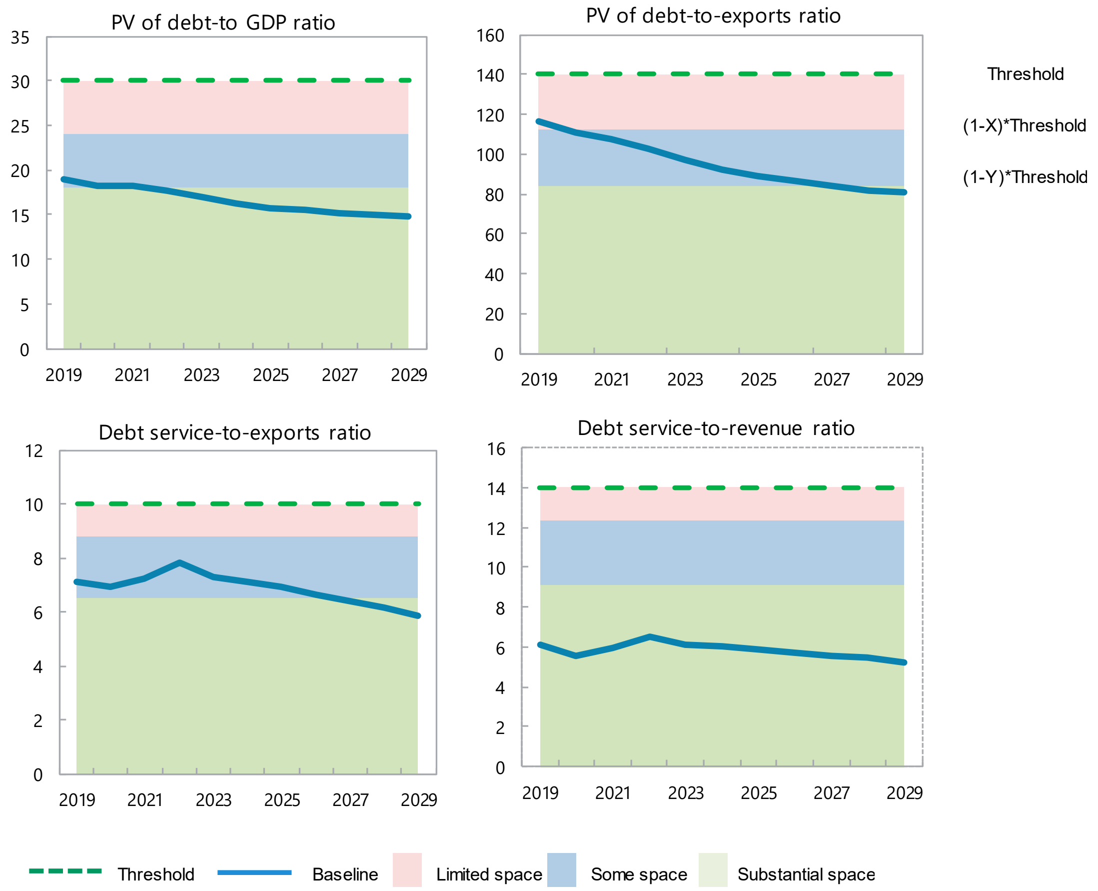


Figure 5. Malawi: Qualification of the Moderate Category, 2019-2029[1/]



Sources: Country authorities; and staff estimates and projections.

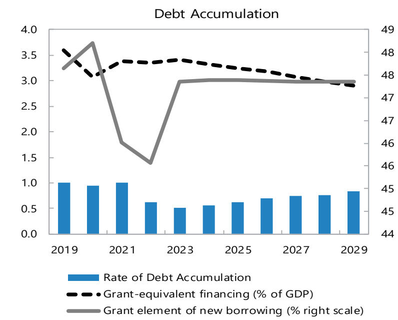
1/ For the PV debt/GDP and PV debt/exports thresholds, x is 20 percent and y is 40 percent. For debt service/Exports and debt service/revenue thresholds, x is 12 percent and y is 35 percent.

Table 1. Malawi: External Debt Sustainability Framework, Baseline Scenario, 2016–2039

(in percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029	2039	Historical	Projections
External debt (nominal) 1/	**35.9**	**36.5**	**34.7**	**33.0**	**32.5**	**32.0**	**30.9**	**29.5**	**28.4**	**26.3**	**27.6**	**28.8**	**29.2**
of which: public and publicly guaranteed (PPG)	**31.8**	**32.8**	**31.2**	**29.8**	**29.5**	**29.1**	**28.0**	**26.8**	**25.8**	**24.2**	**26.1**	**25.3**	**26.6**
Change in external debt	-1.0	0.7	-1.9	-1.7	-0.5	-0.4	-1.2	-1.3	-1.1	-0.2	0.0		
Identified net debt-creating flows	**21.5**	**15.9**	**15.0**	**14.6**	**13.0**	**12.1**	**10.5**	**9.3**	**8.3**	**8.2**	**6.5**	**11.0**	**10.0**
Non-interest current account deficit	**18.1**	**22.0**	**20.2**	**18.1**	**17.0**	**16.6**	**15.4**	**14.6**	**13.7**	**13.5**	**12.1**	**13.0**	**14.9**
Deficit in balance of goods and services	22.9	27.3	26.3	24.5	23.0	22.8	21.5	20.6	19.6	19.1	17.1	**20.4**	**20.8**
Exports	21.5	16.9	16.1	16.2	16.5	16.9	17.2	17.4	17.6	18.5	20.1		
Imports	44.4	44.2	42.4	40.7	39.5	39.7	38.7	37.9	37.2	37.6	37.1		
Net current transfers (negative = inflow)	-4.9	-7.5	-8.1	-8.5	-8.1	-8.2	-8.1	-8.0	-7.8	-7.5	-6.5	**-6.2**	**-7.9**
of which: official	0.0	-0.2	0.0	-0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other current account flows (negative = net inflow)	0.1	2.2	2.1	2.1	2.0	2.0	2.0	2.0	2.0	1.9	1.6	**-1.2**	**2.0**
Net FDI (negative = inflow)	**-3.1**	**-2.1**	**-2.0**	**-2.3**	**-2.7**	**-3.0**	**-3.4**	**-3.7**	**-3.8**	**-4.2**	**-4.5**	**-1.7**	**-3.6**
Endogenous debt dynamics 2/	**6.4**	**-4.0**	**-3.2**	**-1.1**	**-1.3**	**-1.4**	**-1.6**	**-1.6**	**-1.5**	**-1.1**	**-1.1**		
Contribution from nominal interest rate	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.3		
Contribution from real GDP growth	-1.0	-1.3	-1.0	-1.4	-1.6	-1.7	-1.8	-1.9	-1.8	-1.4	-1.4		
Contribution from price and exchange rate changes	7.1	-3.0	-2.5	...	...	...	...	...	...	...	...		
Residual 3/	**-22.5**	**-15.3**	**-16.9**	**-16.3**	**-13.5**	**-12.5**	**-11.7**	**-10.7**	**-9.5**	**-8.4**	**-6.4**	**-9.2**	**-10.7**
of which: exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	**...**	**...**	**19.9**	**18.9**	**18.2**	**18.2**	**17.6**	**16.9**	**16.3**	**14.8**	**15.9**		
PV of PPG external debt-to-exports ratio	**...**	**...**	**123.3**	**116.3**	**110.8**	**107.7**	**102.5**	**97.2**	**92.3**	**80.4**	**79.4**		
PPG debt service-to-exports ratio	**17.4**	**9.3**	**6.4**	**7.1**	**6.9**	**7.2**	**7.8**	**7.3**	**7.1**	**5.8**	**4.4**		
PPG debt service-to-revenue ratio	**20.2**	**8.0**	**5.1**	**6.1**	**5.5**	**5.9**	**6.5**	**6.1**	**6.0**	**5.2**	**5.4**		
Gross external financing need (Billion of U.S. dollars)	1.0	1.3	1.4	1.3	1.3	1.3	1.3	1.3	1.2	1.6	2.5		
Key macroeconomic assumptions													
Real GDP growth (in percent)	2.3	4.0	3.2	4.5	5.1	5.5	6.0	6.5	6.5	5.5	5.5	**4.5**	**5.7**
GDP deflator in US dollar terms (change in percent)	-16.1	9.1	7.4	5.9	3.3	0.5	0.7	0.8	0.7	1.1	1.5	**-1.0**	**1.5**
Effective interest rate (percent) 4/	0.7	0.9	0.9	0.8	0.8	0.8	0.8	0.9	0.9	1.0	1.0	**0.8**	**0.9**
Growth of exports of G&S (US dollar terms, in percent)	-7.1	-10.7	5.6	11.4	10.2	8.6	8.7	8.6	8.7	7.6	8.5	**3.8**	**8.6**
Growth of imports of G&S (US dollar terms, in percent)	-4.3	13.0	6.2	6.2	5.2	6.6	4.1	5.2	5.1	6.8	7.6	**3.8**	**6.1**
Grant element of new public sector borrowing (in percent)	...	...	...	47.7	48.2	46.0	45.6	47.4	47.4	47.4	47.3	**...**	**47.2**
Government revenues (excluding grants, in percent of GDP)	18.5	19.5	20.2	18.8	20.5	20.5	20.7	20.7	20.8	20.8	16.5	**18.3**	**20.5**
Aid flows (in Billion of US dollars) 5/	0.3	0.4	0.2	0.3	0.3	0.3	0.4	0.4	0.4	0.5	0.7		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	3.6	3.1	3.4	3.4	3.4	3.3	2.9	1.8	**...**	**3.2**
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	75.6	72.9	72.1	75.8	78.6	77.1	71.4	59.2	**...**	**74.4**
Nominal GDP (Billion of US dollars)	5.5	6.2	6.9	7.6	8.3	8.8	9.4	10.1	10.8	14.9	29.4		
Nominal dollar GDP growth	-14.2	13.4	10.8	10.6	8.6	6.0	6.7	7.4	7.2	6.7	7.0	**3.6**	**7.3**
Memorandum items:													
PV of external debt 7/	...	...	23.3	22.1	21.3	21.1	20.4	19.6	18.8	17.0	17.4		
In percent of exports	...	...	144.6	135.9	129.1	125.1	118.9	112.7	107.0	92.0	86.5		
Total external debt service-to-exports ratio	17.4	9.3	8.8	9.2	8.8	9.0	9.5	8.8	8.5	6.8	4.9		
PV of PPG external debt (in Billion of US dollars)			1.4	1.4	1.5	1.6	1.7	1.7	1.8	2.2	4.7		
(PVt-PVt-1)/GDPt-1 (in percent)				1.0	0.9	1.0	0.6	0.5	0.6	0.8	1.2		
Non-interest current account deficit that stabilizes debt ratio	19.2	21.3	22.1	19.8	17.5	17.0	16.6	15.9	14.8	13.8	12.1		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**Yes**



Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
4/ Current-year interest payments divided by previous period debt stock.
5/ Defined as grants, concessional loans, and debt relief.
6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).
7/ Assumes that PV of private sector debt is equivalent to its face value.
8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

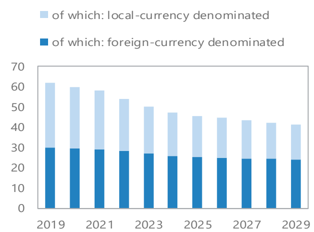
Table 2. Malawi: Public Sector Debt Sustainability Framework, Baseline Scenario, 2016–2039

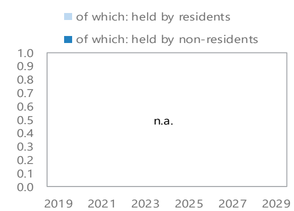
(in percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029	2039	Historical	Projections
Public sector debt 1/	55.1	57.1	59.5	61.8	60.0	58.1	53.9	50.1	47.2	41.4	29.2	**45.3**	**49.8**
of which: external debt	31.8	32.8	31.2	29.8	29.5	29.1	28.0	26.8	25.8	24.2	26.1	**25.3**	**26.6**
Change in public sector debt	0.7	2.0	2.5	2.2	-1.8	-1.9	-4.2	-3.8	-3.0	-0.7	-0.6		
Identified debt-creating flows	-1.2	0.3	0.4	2.0	-2.1	-2.3	-3.9	-3.4	-2.6	-0.5	-0.7	**0.5**	**-1.5**
Primary deficit	2.4	3.5	2.1	2.2	-0.6	-0.1	-0.3	-0.5	0.0	0.8	0.8	**1.5**	**0.2**
Revenue and grants	21.1	22.7	21.5	21.3	22.5	22.8	23.2	23.3	23.2	22.6	17.2	**22.9**	**22.8**
of which: grants	2.6	3.3	1.3	2.5	2.0	2.3	2.5	2.6	2.4	1.9	0.7		
Primary (noninterest) expenditure	23.5	26.3	23.6	23.5	21.9	22.6	22.9	22.8	23.2	23.4	18.0	**24.4**	**23.0**
Automatic debt dynamics	-3.3	-3.2	-1.7	-0.2	-1.5	-2.2	-3.7	-2.9	-2.7	-1.3	-1.5		
Contribution from interest rate/growth differential	-0.8	-0.8	-0.2	0.6	-1.9	-2.5	-3.9	-3.2	-2.9	-1.5	-1.6		
of which: contribution from average real interest rate	0.4	1.3	1.6	3.1	1.1	0.7	-0.6	0.1	0.1	0.7	-0.1		
of which: contribution from real GDP growth	-1.2	-2.1	-1.8	-2.6	-3.0	-3.1	-3.3	-3.3	-3.1	-2.2	-1.6		
Contribution from real exchange rate depreciation	-2.6	-2.4	-1.5	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	**0.0**	**0.0**
Privatization receipts (negative)	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	1.9	1.7	2.0	-0.5	0.7	0.7	0.0	-0.1	-0.1	0.0	0.2	**2.2**	**0.1**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	48.2	51.0	49.4	47.6	43.8	40.5	37.9	32.3	19.4		
PV of public debt-to-revenue and grants ratio	...	...	223.9	239.3	219.5	209.2	189.2	173.8	163.4	142.7	112.8		
Debt service-to-revenue and grants ratio 3/	36.0	35.6	24.7	35.4	45.8	49.8	45.8	45.3	42.7	47.2	16.5		
Gross financing need 4/	5.7	7.6	7.4	9.7	9.7	11.2	10.3	10.0	9.9	11.4	3.6		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	2.3	4.0	3.2	4.5	5.1	5.5	6.0	6.5	6.5	5.5	5.5	**4.5**	**5.7**
Average nominal interest rate on external debt (in percent)	1.1	1.0	1.1	0.9	0.9	0.9	0.9	1.0	1.0	1.1	1.1	**1.0**	**1.0**
Average real interest rate on domestic debt (in percent)	2.4	6.6	8.3	13.1	4.8	3.5	-1.1	1.6	1.7	5.3	4.5	**2.4**	**4.9**
Real exchange rate depreciation (in percent, + indicates depreciation)	-7.9	-8.0	-4.8	...	...	...	...	...	... .	...	...	**5.5**	**...**
Inflation rate (GDP deflator, in percent)	20.5	10.9	7.7	8.0	7.9	6.7	5.8	5.1	4.4	5.1	6.5	**16.0**	**5.6**
Growth of real primary spending (deflated by GDP deflator, in percent)	-1.5	16.2	-7.1	3.9	-2.1	8.9	7.3	6.1	8.5	7.8	-2.3	**3.6**	**5.7**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	1.7	1.5	-0.3	0.0	1.2	1.8	3.9	3.3	3.0	1.5	1.5	**1.0**	**1.9**
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**Yes**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.
1/ Coverage of debt: The central government, central bank, government-guaranteed debt. Definition of external debt is Currency-based.
2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.
3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.
4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period and other debt creating/reducing flows.
5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.
6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Malawi: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2019–2029

	Projections 1/										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
PV of debt-to GDP ratio											
Baseline	18.9	18.2	18.2	17.6	16.9	16.3	15.8	15.5	15.2	15.0	14.8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	18.9	17.5	16.7	16.2	16.2	16.8	17.5	18.4	19.4	20.6	22.0
B. Bound Tests											
B1. Real GDP growth	18.9	19.0	19.9	19.2	18.4	17.8	17.2	16.9	16.6	16.4	16.2
B2. Primary balance	18.9	18.7	19.2	19.0	18.6	18.3	18.0	17.9	17.8	17.6	17.5
B3. Exports	18.9	19.9	22.7	22.0	21.1	20.4	19.8	19.4	19.0	18.5	18.1
B4. Other flows 3/	18.9	21.0	23.9	23.2	22.3	21.5	20.9	20.5	20.0	19.4	18.9
B5. One-time 30 percent nominal depreciation	18.9	22.9	18.7	18.1	17.3	16.6	16.1	15.8	15.5	15.5	15.6
B6. Combination of B1-B5	18.9	22.8	24.8	24.0	23.1	22.3	21.7	21.2	20.7	20.1	19.7
C. Tailored Tests											
C1. Combined contingent liabilities	18.9	19.2	19.7	19.6	19.2	18.9	18.7	18.5	18.4	18.3	18.3
C2. Natural disaster	18.9	19.6	20.2	20.2	19.9	19.7	19.6	19.6	19.6	19.6	19.7
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	116.3	110.8	107.7	102.5	97.2	92.3	89.0	86.2	83.9	81.9	80.4
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	116.3	106.4	98.8	94.2	93.3	95.5	98.8	102.3	107.1	112.7	119.2
B. Bound Tests											
B1. Real GDP growth	116.3	110.8	107.7	102.5	97.2	92.3	89.0	86.2	83.9	81.9	80.4
B2. Primary balance	116.3	113.3	113.7	110.8	107.3	103.9	101.7	99.8	98.0	96.2	94.8
B3. Exports	116.3	**143.6**	**187.2**	**178.3**	**169.4**	**161.2**	**155.5**	**150.6**	**145.8**	**140.8**	136.6
B4. Other flows 3/	116.3	127.5	**141.6**	135.0	128.3	122.1	117.8	114.1	110.2	106.0	102.5
B5. One-time 30 percent nominal depreciation	116.3	110.8	88.1	83.7	79.2	75.1	72.3	70.2	68.3	67.6	67.3
B6. Combination of B1-B5	116.3	**147.4**	134.5	**160.4**	**152.4**	**145.0**	139.9	135.5	130.6	126.0	122.2
C. Tailored Tests											
C1. Combined contingent liabilities	116.3	116.6	116.6	114.0	110.7	107.3	105.2	103.3	101.6	100.1	98.9
C2. Natural disaster	116.3	121.1	121.7	119.8	116.9	114.1	112.5	111.2	110.1	109.2	108.5
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	7.1	6.9	7.2	7.8	7.3	7.1	6.9	6.6	6.4	6.2	5.8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	7.1	7.2	7.5	8.4	8.0	8.1	8.2	8.2	7.7	7.4	7.2
B. Bound Tests											
B1. Real GDP growth	7.1	6.9	7.2	7.8	7.3	7.1	6.9	6.6	6.4	6.2	5.8
B2. Primary balance	7.1	6.9	7.2	7.9	7.4	7.3	7.1	6.8	6.7	6.6	6.4
B3. Exports	7.1	8.3	**10.4**	**11.7**	**10.9**	**10.6**	**10.3**	9.9	**10.0**	**10.6**	9.9
B4. Other flows 3/	7.1	6.9	7.5	8.4	7.9	7.6	7.4	7.1	7.5	7.9	7.5
B5. One-time 30 percent nominal depreciation	7.1	6.9	7.2	7.5	7.0	6.8	6.6	6.4	6.1	5.1	4.9
B6. Combination of B1-B5	7.1	7.8	9.5	**10.4**	9.7	9.4	9.1	8.7	9.4	9.4	8.9
C. Tailored Tests											
C1. Combined contingent liabilities	7.1	6.9	7.3	8.0	7.5	7.3	7.2	6.9	6.7	6.5	6.1
C2. Natural disaster	7.1	7.1	7.6	8.3	7.8	7.6	7.4	7.2	7.0	6.8	6.4
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	6.1	5.5	5.9	6.5	6.1	6.0	5.9	5.7	5.6	5.4	5.2
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	6.1	5.8	6.2	6.9	6.7	6.9	7.0	7.1	6.8	6.6	6.4
B. Bound Tests											
B1. Real GDP growth	6.1	5.8	6.5	7.1	6.7	6.6	6.4	6.3	6.1	5.9	5.7
B2. Primary balance	6.1	5.5	6.0	6.6	6.2	6.2	6.1	5.9	5.8	5.8	5.7
B3. Exports	6.1	5.6	6.2	7.0	6.6	6.5	6.3	6.1	6.3	6.7	6.3
B4. Other flows 3/	6.1	5.5	6.2	7.0	6.6	6.5	6.3	6.1	6.5	7.0	6.6
B5. One-time 30 percent nominal depreciation	6.1	7.0	7.4	7.8	7.3	7.2	7.1	6.9	6.7	5.7	5.4
B6. Combination of B1-B5	6.1	5.9	6.8	7.5	7.1	6.9	6.8	6.6	7.2	7.3	6.9
C. Tailored Tests											
C1. Combined contingent liabilities	6.1	5.5	6.0	6.6	6.3	6.2	6.1	6.0	5.8	5.7	5.4
C2. Natural disaster	6.1	5.5	6.0	6.6	6.3	6.2	6.2	6.0	5.9	5.8	5.5
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	14	14	14	14	14	14	14	14	14	14	14

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. Malawi: Sensitivity Analysis for Key Indicators of Public Debt, 2019–2029

	Projections 1/										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
PV of Debt-to-GDP Ratio											
Baseline	**51.0**	**49.4**	**47.6**	**43.8**	**40.5**	**37.9**	**36.5**	**35.5**	34.4	33.1	32.3
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2(	**51**	**48**	**44**	**39**	**35**	32	29	27	25	23	21
B. Bound Tests											
B1. Real GDP growth	**51**	**52**	**54**	**52**	**50**	**48**	**48**	**48**	**48**	**48**	**48**
B2. Primary balance	**51**	**53**	**54**	**50**	**46**	**43**	**41**	**40**	**39**	**37**	**37**
B3. Exports	**51**	**51**	**52**	**48**	**44**	**42**	**40**	**39**	**38**	**36**	**35**
B4. Other flows 3/	**51**	**52**	**53**	**50**	**46**	**43**	**42**	**41**	**39**	**38**	**36**
B5. One-time 30 percent nominal depreciation	**51**	**50**	**47**	**43**	**39**	**35**	33	31	29	27	25
B6. Combination of B1-B5	**51**	**51**	**50**	**43**	**40**	**37**	**36**	35	34	33	32
C. Tailored Tests											
C1. Combined contingent liabilities	**51**	**57**	**55**	**51**	**47**	**44**	**42**	**41**	**40**	**38**	**37**
C2. Natural disaster	**51**	**59**	**57**	**53**	**50**	**47**	**45**	**44**	**43**	**41**	**41**
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
PV of Debt-to-Revenue Ratio											
Baseline	239.3	219.5	209.2	189.2	173.8	163.4	158.1	154.3	150.7	145.4	142.7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2(	239	215	197	173	156	141	130	121	113	105	98
B. Bound Tests											
B1. Real GDP growth	239	231	237	221	211	205	206	207	209	208	211
B2. Primary balance	239	235	237	215	198	186	180	175	171	165	161
B3. Exports	239	226	228	207	191	180	174	170	166	160	156
B4. Other flows 3/	239	232	235	214	197	186	181	177	172	165	161
B5. One-time 30 percent nominal depreciation	239	226	208	186	168	154	144	136	128	119	113
B6. Combination of B1-B5	239	228	219	187	172	161	156	152	150	145	143
C. Tailored Tests											
C1. Combined contingent liabilities	239	256	243	220	202	191	184	179	175	169	165
C2. Natural disaster	239	264	251	229	212	201	195	191	187	182	179
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Debt Service-to-Revenue Ratio											
Baseline	35.4	45.8	49.8	45.8	45.3	42.7	46.0	46.6	47.5	48.2	47.2
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2(	35	43	49	46	45	43	44	43	41	39	37
B. Bound Tests											
B1. Real GDP growth	35	48	56	56	60	61	67	71	74	77	78
B2. Primary balance	35	46	60	64	61	56	58	57	56	56	54
B3. Exports	35	46	50	46	46	43	46	47	48	49	48
B4. Other flows 3/	35	46	50	46	46	43	46	47	48	50	49
B5. One-time 30 percent nominal depreciation	35	43	48	41	43	41	44	45	45	46	44
B6. Combination of B1-B5	35	45	50	46	45	42	46	46	48	49	49
C. Tailored Tests											
C1. Combined contingent liabilities	35	46	73	68	63	58	59	58	58	57	55
C2. Natural disaster	35	46	77	72	68	63	64	63	63	63	61
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.
3/ Includes official and private transfers and FDI.

Statement by Mr. Mahlinza, Executive Director and
Mr. Sitima-wina, Senior Advisor on Malawi
November 22, 2018

Introduction

1. Our authorities appreciate the candid dialogue during the recent program review mission. They broadly concur with the staff appraisal and key policy conclusions.

2. Malawi has continued to make progress in the implementation of the third Growth and Development Strategy (MGDS III) which aims to boost productivity, enhance competitiveness, and build resilience through growth-enhancing investments and economic diversification, supported by the Extended Credit Facility (ECF) arrangement. This has helped restore macroeconomic stability as reflected by the decline in inflation, stability in the exchange rate and the steady pick-up in growth.

3. Implementation of the MDGS has, however, been challenged by the increased frequency of weather-related shocks over the past few years. In March 2019, the southern part of Malawi was hit by Tropical Cyclone Idai causing significant loss of lives and property and damaging vital infrastructure. In response, the authorities increased spending on goods and services to meet immediate post cyclone disaster relief and rehabilitation expenses, projected to cost around $370 million.

4. Against this background, the authorities request augmentation of access under the ECF arrangement to finance imports for post cyclone reconstruction and place the economy back on a firm recovery path. They also request Executive Directors' support towards the completion of the second and third reviews under the ECF arrangement and some waivers for the non-observance of performance criteria.

Performance under the ECF Arrangement

5. All quantitative performance criteria (QPC) for end-December 2018 and end-June 2019 were met except one on the primary fiscal balance. Indicative targets (ITs) on new domestic arrears and on social spending were met for both end-December and end-June. In addition, most structural benchmarks (SBs) in the financial sector and public financial management were met.

6. The QPC on the primary fiscal balance for end-December 2018 was missed by 1.5 percent of GDP due to front-loading of planned spending for the year. The same QPC was missed by 2.5 percent of GDP at end-June 2019, due to revenue shortfalls and expenditure overruns necessitated by unbudgeted support to post-cyclone disaster relief and rehabilitation; spending to ensure safety during and after elections; payment of arrears arising from court rulings; and transfers to universities to accommodate salary increases following staff strikes. To correct these slippages, the authorities have tightened spending relative to the FY 2018/19 outcome, returning to levels envisaged during the first review under the ECF arrangement. Based on the foregoing, our authorities request waivers for non-observance of the two QPCs.

Recent Economic Developments and Macroeconomic Outlook

7. The Malawi economy is expected to grow at 4.5 percent in 2019, up from 3.2 percent in 2018. This growth is supported by an agricultural rebound, increased electricity generation and post-cyclone reconstruction. Over the medium-term, prospects remain positive with growth projected to accelerate to 6-7 percent, supported by robust agricultural production driven by improved irrigation infrastructure, crop diversification, increased electricity generation, greater access to finance and an improved business climate. However, adverse weather conditions exacerbated by climate change could weigh on growth.

8. Headline inflation declined from 9.9 percent at end-2018 to 9.2 percent in September 2019. It is expected to average 9.1 percent during the year. However, food prices remain elevated due to disruptions in supply chains caused by the cyclone and grain hoarding by some suppliers. Over the medium term, inflation is expected to remain in single digit territory and gradually converge to 5 percent aided by the continued implementation of tight fiscal and monetary policies.

9. On the external sector, the impact of Cyclone Idai on some agricultural exports was somewhat offset by the strengthening of drought-resistant export commodities such as cotton, sugar, pulses and edible nuts. Consequently, the current account deficit is anticipated to narrow from 20.6 percent in 2018 to 18.4 percent of GDP in 2019. Over the medium term, improvements in competitiveness and export diversification are expected to contribute to a steady narrowing of the current account deficit to around 15 percent of GDP, with foreign reserves rising above 4 months of prospective imports.

Fiscal Policy and Public Financial Management Reforms

10. The authorities reiterate their commitment to the implementation of prudent fiscal policies to keep public debt on a downward path while safeguarding social spending and critical growth enhancing expenditures. To avoid fiscal slippages, all spending commitments will be carefully monitored and undertaken as revenues materialize.

11. To enhance domestic revenue mobilization, broad based tax reforms will be implemented complemented by stepped up efforts to enforce tax compliance. A domestic revenue mobilization strategy aimed at delivering an efficient, transparent and fair tax system will be ready for implementation with the FY2020/21 budget. Meanwhile, the FY 2019/20 budget incorporates new tax measures which are currently being implemented including, a presumptive tax on commercial passenger vehicles; a carbon tax on motor vehicles; excises on plastic products; and import surcharge on select goods (e.g., alcohol, cigarettes). Further, the Malawi Revenue Authority (MRA) has enhanced the use of the ASYCUDA World system to improve the collection of trade taxes. An Integrated Tax Administration System (ITAS) to enhance overall tax administration will also be rolled out. In addition, the authorities have raised user fees and charges and enhanced their collection. Going forward, the user fees and charges will be periodically reviewed to maintain their real values and adjusted towards marginal costs. Furthermore, dividend remittances by state-owned enterprises (SOEs) will be reinforced through the implementation of the revised dividend policy.

12. In the medium term, the authorities will continue to rationalize expenditures and enforce controls to prevent the re-emergence of domestic payment arrears and ensure overall debt sustainability. For FY 2019/20, expenditure cuts have been implemented, with savings deployed to support cyclone victims and meet rehabilitation costs. At the same time, domestically financed capital projects have been reoriented to boost disaster resilience. Furthermore, wage and pension increases have been aligned with inflation developments while new hiring has been confined to essential staff. To enhance the oversight and reporting of all SOEs and mitigate contingent fiscal risks, revised regulations, policies and monitoring guidelines for SOEs have been issued. Further, the authorities completed the audit of the public sector investment program (PSIP) database to inform investment decisions and enhance efficiency and effectiveness in public investment management and procurement.

13. The authorities have made considerable progress in public financial management reforms including in cash management, commitment controls, regular publication of reports by Ministries, Departments and Agencies (MDAs) and enhancing debt management and monitoring capacity. Going forward, the authorities will expand the coverage of IFMIS to enhance controls and improve fiscal reporting. This will further boost confidence in the budget system and reduce vulnerabilities to corruption. On debt, a comprehensive medium-term debt strategy has been developed and will be updated regularly.

Monetary, Exchange Rate and Financial Sector Policies

14. Monetary policy will continue to focus on containing inflation within single digits. Over the medium-term, the Reserve Bank of Malawi (RBM) plans to complete the transition to an interest rate-based operational framework and adopt inflation targeting. To this end, they are expanding capacity in developing high frequency data, liquidity forecasting, and the forecasting and policy analysis system (FPAS) modeling. To further strengthen the monetary transmission mechanism, the RBM, in consultation with the market players, recently modified the reference rate for base lending rates of commercial banks from the Lombard rate to a weighted average of four rates. The authorities will continue to monitor developments around implementation of the new reference rate and review it as and when necessary.

15. The authorities remain fully committed to a flexible exchange rate regime. In this regard, interventions have been made solely for the accumulation of foreign reserves and smoothening volatility in the FX market. To achieve greater exchange rate flexibility, crucial for absorbing shocks and supporting economic diversification, the RBM is working on deepening the interbank FX market. This will be guided by a well-sequenced action plan which will be informed by a comprehensive study to determine obstacles to FX market development.

16. Safeguarding financial sector stability and strengthening resilience remains a key priority for the authorities. To this end, they continue to enhance supervision and the regulatory framework. Further, the level of non-performing loans (NPLs) have declined markedly from 15.7 percent at end-2017 to 4.8 percent in June 2019, reflecting loan recovery and overall growth in bank lending. With all banks fully compliant with IFRS9 standards, the level of provisioning has substantially increased. To reduce the time required to recover collateral associated with NPLs, the RBM has encouraged banks to enhance their loan recovery efforts, improve analysis of collateral quality and enhance the collateral registry.

Structural Reforms

17. The authorities consider the implementation of comprehensive structural reforms as important to attaining higher and more inclusive growth. Accordingly, they have made notable progress in public financial management reforms, reduced vulnerabilities to corruption and improved transparency. To enhance inclusive growth and address inequality, the authorities are stepping up efforts to promote financial inclusion and boost access and affordability of credit.

18. Building on the National Disaster Recovery Framework and the 2017 Strategic Program for Climate Resilience, the authorities are transitioning from a disaster reactive system to a preventive system. In this respect, a Disaster Risk Financing (DRF) strategy to anticipate, prepare and better respond to disasters was recently approved by Cabinet. Currently, a broad resilience strategy which will include risk-transfer instruments and minimize the impact of disasters on the fiscal budget is being finalized. In addition, the authorities will continue to focus on more resilient infrastructure (enhanced electricity generation and irrigation) and crop diversification to strengthen the country's resilience to weather shocks. They remain committed to implementing the automatic fuel pricing mechanism which enables full cost recovery by fuel importers and eliminates the need for a government subsidy. Further, they will continue with reforms to improve the business environment, including easing procedures to start a business and obtain construction permits, strengthening contract enforcement and enhancing insolvency processes.

Conclusion

19. Our authorities reiterate their commitment to entrenching macroeconomic stability and enhancing governance to achieve higher, more inclusive and sustainable growth. In pursuit of these objectives, they will continue to implement an appropriate policy combination of prudent fiscal and monetary policies, accompanied by growth enhancing structural reforms. They also wish to express their appreciation to the international community including, the World Bank and the African Development Bank, for their assistance in providing immediate disaster relief in response to Cyclone Idai and would welcome further support to meet the significant reconstruction needs that remain. They continue to value Fund engagement and look forward to Executive Directors' support in completing the second and third reviews under the ECF.