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# Malawi: First Review Under the Extended Credit Facility Arrangement, Request for Waiver of Performance Criterion, and Modification of Performance Criteria—Staff Report; Informational Annex; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Malawi.

In the context of the First Review Under the Extended Credit Facility Arrangement, Request for Waiver of Performance Criterion, and Modification of Performance Criteria, the following documents have been released and are included in this package:

- The staff report for the First Review Under the Extended Credit Facility Arrangement, Request for Waiver of Performance Criterion, and Modification of Performance Criteria, prepared by a staff team of the IMF, following discussions that ended on November 15, 2012, with the officials of Malawi on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on December 5, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A press release, summarizing the views of the Executive Board as expressed during its December 19, 2012 discussion of the staff report that completed the review.
- 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.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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**Washington, D.C.**

INTERNATIONAL MONETARY FUND

MALAWI

# First Review Under the Extended Credit Facility Arrangement, Request for Waiver of Performance Criterion, and Modification of Performance Criteria

Prepared by the African Department
(In consultation with other departments)

Approved by David Owen and Dhaneshwar Ghura

December 5, 2012

**ECF arrangement:** On July 23, 2012, the Executive Board approved a new three-year arrangement for Malawi under the Extended Credit Facility (ECF) in the amount of SDR 104.1 million (150 percent of quota). Quarterly reviews are scheduled for the first year and semi-annual reviews thereafter. SDR 13.02 million (18.75 percent of quota) was disbursed upon the approval of the arrangement. Another SDR 13.02 million is scheduled to be disbursed upon completion of the first review.

**Mission:** Discussions were held in Lilongwe and Blantyre during October 30–November 15, 2012. The mission was led by Mr. T. Tsikata (AFR), and included Mr. O. Adedeji, M. Ghazanchyan, Ms. J. Peng (all AFR), Mr. M. Raissi (SPR) and Ms. R. Randall (Resident Representative). The mission met President Joyce Banda, Minister of Finance Dr. Ken Lipenga, Governor of the Reserve Bank of Malawi (RBM) Mr. Charles Chuka, Secretary to the Treasury Mr. Randson Mwadiwa, other senior government and RBM officials, and representatives of the business community, banks, civil society organizations, trade unions and Malawi's development partners. Ms. H. Teferra (OED) participated in the discussions and the mission was assisted by Mr. S. Banda (Economist in the office of the IMF Resident Representative).

**First ECF review:** Most of the quantitative targets and all structural benchmarks for the first review were met. However, the end-September 2012 performance criterion on the level of the RBM's net domestic assets (NDA) was missed on account of the central bank's extension of liquidity support to the banking system, including through an uncollateralized facility for banks that run out of eligible securities for borrowing through the regular discount window. The RBM closed the uncollateralized lending window on November 30 and has placed distressed banks are under heightened scrutiny to ensure that they are on a path to meeting prudential liquidity requirements. The RBM also conducted open market operations to withdraw liquidity as part of its effort to stabilize the exchange rate. Staff supports the authorities' requests for a waiver in respect of the nonobservance of the RBM NDA performance criterion and for modification of performance criteria for the second and third reviews (test dates of end-December 2012 and end-March 2013, respectively). The modifications are needed to reflect: a worse external environment than envisaged when the program was designed, a tightening of policies by the authorities, and additional donor support. Staff recommends completion of the first review.

**Safeguards assessment:** The update assessment reiterates concern over RBM's lack of operational autonomy and recommends amendments to the RBM Act to remedy the situation. It also calls for enhanced oversight over foreign reserves management.

**Outreach:** The Fund co-organized (with the Ministry of Finance and the RBM), a very well received conference on the topic "Toward More Inclusive Growth" in Lilongwe during November 2–3. The conference, which was opened by President Banda, brought together a wide range of stakeholders and experts to discuss policies and strategies to speed up the recovery and make output and export growth more broad based and more inclusive of the poor.

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## EXECUTIVE SUMMARY

**Drought conditions in parts of the country have dampened the near-term outlook for growth, contributed to a spike in inflation and rendered nearly 2 million people food insecure.** Output contraction in agriculture is the main factor behind a downward revision in real GDP growth in 2012 from 4.3 percent earlier in the year to 1.9 percent. A marked rise in domestically produced food prices, the May devaluation and continuing depreciation of the exchange rate—partly reflecting lower than expected tobacco sales—are the principal factors behind a surge in inflation from 12.4 percent in April to 30.6 percent in October.

**Performance under the program was satisfactory.** Most quantitative targets and all structural benchmarks for the first review were met. However, the end-September 2012 performance criterion on the RBM's net domestic assets and the indicative target on reserve money were missed on account of RBM accommodation of liquidity needs of banks. The indicative target on social spending was also not met, because of delays in procuring fertilizers for the farm input subsidy program. The RBM has reduced its lending to banks and is exercising greater oversight of distressed banks to ensure that they are on a path to meeting prudential regulations.

**Policy discussions focused on measures to stabilize the exchange rate and contain inflation.** Given the low level of international reserves, staff and the authorities agreed on measures to tighten monetary policy and the fiscal stance. Shutting down uncollateralized lending by RBM and conducting open market operations to withdraw liquidity and slow down growth in the monetary aggregates will take some pressure off the exchange rate. Fiscal policy will also play a role by saving a portion (equivalent to ½ percent of GDP) of additional external resources being provided by Malawi's development partners. This will allow the RBM to begin building up international reserves from current precariously low levels.

**A wide range of structural reforms is under way.** On the budget side, key reforms aim to: (i) enhance revenue administration to make up for revenue losses arising from implementation of Malawi's obligations under regional treaties (SADC and COMESA); and (ii) strengthen public financial management to prevent the accumulation of arrears and improve cash management. The RBM has intensified its surveillance over the financial system with a view to detecting at an early stage emerging threats to financial stability. The government and the RBM are considering amendments to the RBM Act to strengthen the RBM's operational independence. The authorities are also committed to improving the business environment and investment climate by removing regulatory hurdles to doing business as well as addressing infrastructure bottlenecks (e.g., related to electricity and water supply).

**The authorities' commitment to reforms remains strong.** In particular, they reiterated their commitment to a flexible exchange rate regime and to the automatic price adjustment mechanism for petroleum products.

**Staff recommends completion of the first review, based on performance thus far and on the authorities' policy commitments.**

# I. Sustaining Reforms in the Face of Adjustment Pains

1. **The authorities have implemented strong adjustment measures to address Malawi's substantial external and internal imbalances.** On assumption of the presidency, following the death of her predecessor in April 2012, President Joyce Banda authorized the implementation of a set of bold measures to tackle the country's foreign exchange problems. Concurrently, the Reserve Bank of Malawi (RBM) tightened monetary policy by raising its policy interest rate. Measures implemented by the authorities in May included:

- A devaluation that increased the price of foreign exchange by nearly 50 percent, and adoption of a floating exchange rate regime.
- Removal of restrictions on foreign exchange transactions by banks and foreign exchange bureaus.
- Relaxation of surrender requirements on export proceeds, allowing them to flow to commercial banks, instead of mainly to the Reserve Bank of Malawi (RBM).
- Increases in retail prices of petroleum products and adoption of an automatic adjustment mechanism to keep prices in line with import costs.

2. **The adjustment measures attracted increased pledges of aid from Malawi's development partners and paved the way for approval of the new three-year ECF arrangement in July.** The previous administration's non-adherence to commitments to adopt a flexible exchange rate regime and liberalize the current account led to the interruption and eventual cancellation of an ECF arrangement approved in 2010. The new ECF-supported program is designed to help the authorities achieve macroeconomic stability, boost real GDP growth, and scale up social protection programs to mitigate the adverse impact of adjustment measures on the poor.[1] Structural reforms under the program focus on strengthening domestic revenue mobilization and public financial management, enhancing the operational independence of the RBM, deepening the financial sector, and improving the investment climate.

3. **Manifestations of acute foreign exchange shortage have abated but there is growing public disaffection with austerity measures, continuing depreciation of the exchange rate and rising inflation.** Government spending in the first quarter of FY2012/13 was restrained, reflecting delays in rolling out social protection programs. The parallel market for foreign exchange has virtually disappeared, but the price of foreign exchange has increased by about another 30 percent since the May devaluation, reflecting lower-than-expected tobacco and sugar proceeds and higher foreign exchange requirements to clear the

[1] About 70 percent of the spending on social protection programs is financed by Malawi's development partners, including the World Bank and the African Development Bank.

backlog of private sector external arrears.[2] The supply of petroleum products has improved considerably, albeit at rising prices in line with movements in import costs. The price of maize (the staple food) has shot up in recent months due to a decline in output arising from drought conditions in parts of the country. It is estimated that about 2 million people (about 12 percent of the total population) face food deficits in the period before the next harvest in March/April 2013 (MEFP ¶30).

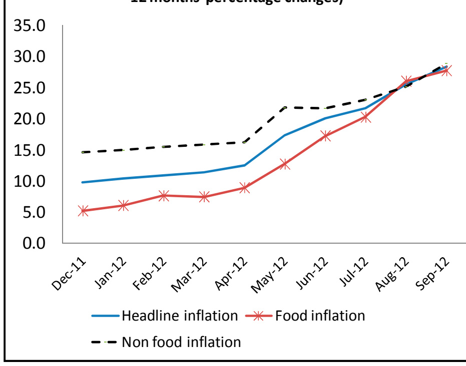
4. **The government has launched the Malawi Economic Recovery Plan (ERP),** to sharpen priorities within the extensive set of programs and projects in the second Malawi Growth and Development Strategy (MGDS II). The ERP lays out action plans over the short- and medium-term to make rapid progress toward poverty reduction through economic growth and wealth creation. It identifies commercial agriculture, tourism, energy, mining, transport infrastructure, and information and communications technology as key sectors and activities that can lead growth and achieve quick development results.

## II. RECENT ECONOMIC DEVELOPMENTS

5. **A marked slowdown in growth is now expected in 2012, driven largely by contractions in agricultural and manufacturing output (Table 1 and Figure 1).** Real GDP growth for 2012 has been revised downward from 4.3 percent in the last staff report (same growth rate as in 2011) to 1.9 percent. Poor rainfall in some areas in the south and central parts of the country have resulted in a decline in maize output, while poor price incentives (reflecting the overvalued exchange rate that prevailed until May) contributed to a lower tobacco crop. Manufacturing output is also estimated to have contracted, reflecting pronounced foreign exchange shortages earlier in the year which constrained imported inputs. While the private sector has cleared a substantial amount of its external payments arrears, external lines of credit have been slow to be re-established, as banks and other creditors have adopted a wait-and-see attitude because of concerns about possible policy reversals. Services continue to exhibit strong growth, led by information and communications technology, and construction.

6. **Devaluation, continuing depreciation of the exchange rate, and decline in domestic food production led to a surge in inflation.** On a year-on-year basis, headline inflation rose from 12.4 percent in April to 30.6 percent in October, with both the food and non-food components of the CPI rising sharply (text chart 1, Figure 1).

Text Chart 1. Malawi: Inflation
(December 2011-September 2012, 12 months percentage changes)




[2] The RBM estimates that about US$500 million worth of arrears have been cleared since May, with RBM foreign exchange sales accounting for about US$200 million.

7. **The mission welcomed resumption (in November) of implementation of the automatic price adjustment mechanism for petroleum products.** From May 2012 when the authorities restored the automatic price adjustment mechanism (APM) through September, prices of these products were adjusted on a monthly basis. The Malawi Energy Regulatory Authority announced price increases in early October only to withdraw them within a day, citing technical problems with the announced prices. The November adjustments reflected developments in world prices and the exchange rate since September.

8. **The overall fiscal balance in the first quarter of FY2012/13 was stronger than programmed, after a weaker-than-expected outturn for FY2011/12.** The fiscal deficit (including grants) for FY2011/12 is reported at 8.5 percent of GDP, compared to 7 percent of GDP projected during the May/June mission (Tables 2a and 2b). A shortfall in grants (by about 1.1 percent of GDP) and increased domestic interest payments were the main factors behind the deviation, and the higher deficit was financed by increased domestic borrowing. The first quarter of FY2012/13 registered a larger surplus than programmed (Table 2c), reflecting lower spending on subsidies due to delays in initiating the procurement of fertilizers for the Farm Input Subsidy Program (FISP) as the government sought to revamp the procurement system to make it more efficient.[3]

9. **Liquidity conditions in the banking system tightened significantly soon after the May devaluation.** Several banks resorted to the RBM discount window to meet their liquidity needs In order to provide relief to the hardest hit banks which continued to have difficulty meeting liquidity requirements, the RBM introduced a temporary window for providing short-term uncollateralized loans to the banks (MEFP ¶23). Most banks appear to have adjusted their balance sheets to the new conditions, and a number have become providers of liquidity to other banks in a more active interbank market. Actions taken by banks include deposit mobilization, curtailment of new loans, and injection of capital (MEFP ¶17). In response to the increases in the RBM's policy rate (from 13 percent to 16 percent in April and to 21 percent in July), banks increased both their lending and deposit rates. The spread between deposit and lending rates does not appear to have changed much (Figure 3a).

10. **The restrained fiscal stance in the first quarter of FY2012/13 has contributed to a slowdown in the growth of money.** Year-on-year growth in reserve money slowed from a peak of 80 percent in July 2012 to 20 percent in September, with RBM lending to banks now the principal source of growth in reserve money (Table 3a). Broad money growth has fallen from the 30–35 percent range in the first half of 2012 to 20 percent in September, with lending to the private sector as the principal source of growth (Table 3b).

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[3] Teething problems with a new accounting system at the RBM resulted in a large discrepancy (equivalent to 2 percent of GDP) between above-the-line fiscal data compiled by the Ministry of Finance and below-the-line financing data compiled by the RBM (Table 2c). Delay in recording government revenues collected in FY2011/12 Q4 in the government's account at the RBM accounted for about half of the discrepancy. This led to higher government borrowing (overdraft) in that quarter than needed. Government repaid part of its outstanding borrowing from the RBM following reconciliation of the fiscal and monetary accounts.

11. **Low production of Malawi's main export, tobacco, translated into significantly lower sales volumes on the auction floors in 2012 compared to 2011.**[4] The volume of sales fell to one third of the level in 2011 and only half of what was projected at the beginning of the season, while the value of sales fell by 40 percent. Thus, the supply of foreign exchange to the local market has been much less than expected. Higher unit prices paid to farmers helped to moderate the negative impact on sales of significantly lower output (see Text table below). Sugar exports also declined as a result of drought in central and southern parts of the country. The current account deficit as a ratio of GDP is projected to narrow from about 6 percent in 2011 to about 3½ percent in 2012, reflecting significantly higher official transfers (Tables 4a and 4b, and Figure 4). The import coverage of international reserves has improved slightly, reflecting increased donor assistance to Malawi.

**Tobacco Auction Sales: 2010–12**

| | 2010 | 2011 | 2012 |
|---|---|---|---|
| Volume (Millions of Kgs) | 220 | 237 | 80 |
| Value (US$ millions) | 416 | 294 | 178 |
| Avg Price (US cents/Kg) | 189 | 124 | 223 |

Source: Tobacco Control Commission.

## III. Policy Discussions

12. **Policy discussions were informed by an updated medium-term macroeconomic framework (Tables 1–4b and Figures 1–4).** A summary of revisions to key macroeconomic indicators is presented in Text Table below. The main revisions include significantly lower real GDP growth in 2012, higher inflation in 2012 and the first half of 2013, and higher grants or official transfers (based on updated information from Malawi's development partners) which allows for both higher social spending and lower domestic borrowing (the fiscal anchor of the program). At the same time, availability of higher external loans allows for a wider deficit than under the original program. External debt service remains low at less than 5 percent of exports for the foreseeable future.

[4] Trading on the auction floors usually opens in early April and closes in September. The sales are an important source of foreign currency for the foreign exchange market in Malawi but are not directly linked to exports during the current year. Large movements in inventories influence exports in any particular year.

**Text Table 1. Malawi: Selected Indicators**

| | Est. | Program | | | | Revised Program | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 | 2012 | 2013 | 2014 | 2015 |
| Real GDP growth | 4.3 | 4.3 | 5.7 | 6.1 | 6.5 | 1.9 | 5.5 | 6.1 | 6.5 |
| CPI inflation (eop) | 9.8 | 22.9 | 12.0 | 7.3 | 6.5 | 31.7 | 10.1 | 5.8 | 5.4 |
| CPI inflation (average) | 7.6 | 18.4 | 16.1 | 7.5 | 6.1 | 20.8 | 18.0 | 7.2 | 5.7 |
| Fiscal indicators (% of GDP, fiscal year basis) 1/ | | | | | | | | | |
| Government revenue (% of GDP) | 24.5 | 21.5 | 22.8 | 23.3 | 23.6 | 22.1 | 23.3 | 24.1 | 24.5 |
| Grants | 7.6 | 5.5 | 10.4 | 8.4 | 7.9 | 4.4 | 14.5 | 12.8 | 11.3 |
| Expenditure and net lending | 35.0 | 34.0 | 34.3 | 32.8 | 32.5 | 35.0 | 39.7 | 38.9 | 37.5 |
| Overall balance including grants | -2.9 | -7.0 | -1.1 | -1.1 | -0.9 | -8.5 | -1.9 | -1.9 | -1.6 |
| Domestic financing | 1.7 | 5.6 | 0.0 | 0.0 | 0.0 | 6.6 | -1.3 | 0.0 | 0.0 |
| External indicators (% of GDP, unless otherwise indicated) | | | | | | | | | |
| Current account balance including official transfers | -5.9 | -4.3 | -1.7 | -1.8 | -1.6 | -3.6 | -1.6 | -1.9 | -2.3 |
| Current account balance excluding official transfers | -12.3 | -15.7 | -12.7 | -12.1 | -11.2 | -18.3 | -16.0 | -16.2 | -15.5 |
| Overall balance | -1.8 | -0.5 | 3.2 | 2.9 | 3.2 | -0.1 | 3.7 | 3.3 | 3.2 |
| Gross international reserves | | | | | | | | | |
| In US$ millions | 190.2 | 204.5 | 405.7 | 564.9 | 728.6 | 214.7 | 403.3 | 547.1 | 677.7 |
| In month of imports | 1.0 | 1.0 | 2.0 | 2.6 | 3.1 | 1.1 | 1.9 | 2.4 | 2.8 |

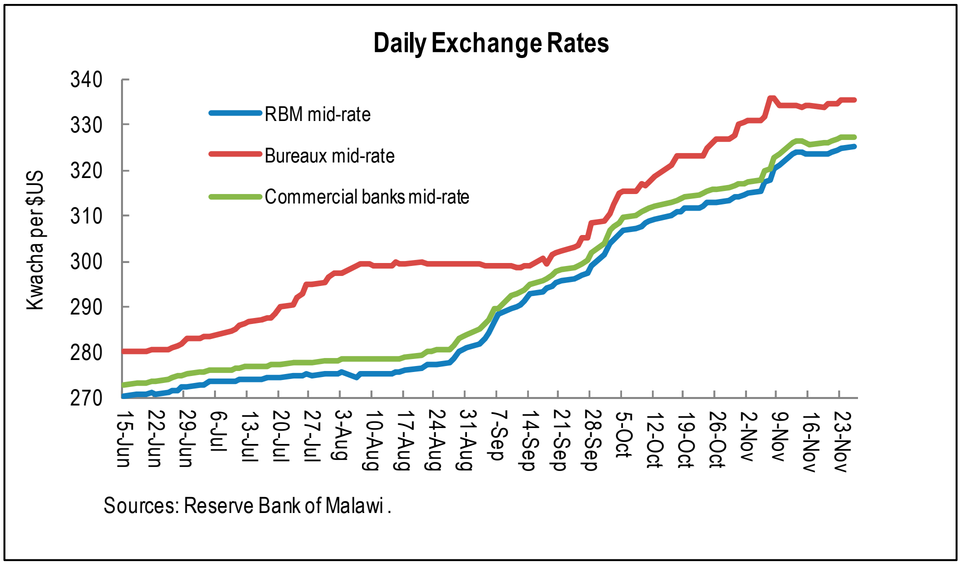
Source: IMF staff estimates and projections.

1/ For example, 2011 refers to FY2010/11 (spanning July 1, 2010 through June 30, 2011).

## A. Exchange Rate Policy

13. **The authorities reiterated their commitment to a flexible exchange rate regime (MEFP ¶20)**. They intend to continue to allow the official exchange rate to reflect market fundamentals so as to enhance Malawi's external competitiveness. The RBM calculates the official exchange rate at the beginning of each business day as a weighted average of rates established by commercial banks the previous day. Foreign exchange bureaus are free to set their own rates.[5] Transactions in the bureaus represent a relatively small part of the foreign exchange market, and tend to be mainly cash transactions.

[5] The authorities have agreed to a review by Fund staff to determine whether the exchange system complies with Malawi's obligations under Article VIII of the Fund's Articles of Agreement. Staff is in the process of reviewing recent reforms to make an assessment of Malawi's exchange system.




14. **An updated assessment of the real exchange rate indicates that the Kwacha is broadly in equilibrium (Appendix II).** The official exchange rate was relatively stable for three months after the devaluation but has depreciated sharply since August. By mid November, the price of foreign exchange had increased by an additional 30 percent after the May devaluation.

15. **The authorities and staff agreed that stabilizing the exchange rate is critical for avoiding a depreciation-inflation-depreciation spiral, and for retaining broad support for a flexible exchange rate regime.** The authorities recognize that, with very low international reserves, fixing the exchange rate carries a high risk of a return to an overvalued rate and dismal prospects for recovery and growth. It was agreed that under the country's current circumstances (low international reserves and onset of the lean season for private foreign exchange inflows) a tightening of both monetary and fiscal policies is required.

## B. Monetary Policy and Financial Sector Issues

16. **The authorities undertook to tighten monetary policy as part of the effort to stabilize the exchange rate and contain inflation.** Staff noted that the RBM's lending to banks had been the principal source of expansion in reserve money in the third quarter of calendar year 2012 and that this contributed to the pressure on the exchange rate. The authorities agreed on the need to tighten monetary policy and took steps to do so in the fourth quarter. To this end, as a prior action for this review, the RBM closed its uncollateralized lending window on November 30. It also conducted open market operations to absorb liquidity. Going forward, to ensure that cost considerations do not prevent the RBM from conducting effective monetary operations, it was agreed that the use of treasury bills for monetary operations will be formalized in a Memorandum of Understanding (MOU) between the RBM and the Ministry of Finance by end-December 2012 (MEFP ¶21). The MOU will indicate clearly that the Ministry of Finance will be responsible for meeting the interest costs of treasury bills used for monetary operations. The authorities expressed concern over the

likely impact of tighter monetary policy on the pace of the recovery and sought the assistance of staff to mobilize additional external resources to support the ongoing adjustment efforts.

17. **The RBM is undertaking a review of the RBM Act with a view to recommending amendments to strengthen its operational independence.** A key amendment will limit the outstanding amount of the government's total borrowing of all kinds from the RBM (end-June 2013 structural benchmark).

18. **The RBM is increasing its oversight over distressed banks.** A few banks have persisted in relying heavily on borrowing from the RBM or the interbank market to meet liquid reserve requirements. The RBM will enforce its prudential regulations, and if warranted, require the banks to submit time-bound restructuring plans. Restructuring is likely to include securitization of some assets, curtailing the levels of lending and putting on hold expansion plans (MEFP ¶24).

19. **Financial stability indicators suggest that the banking sector in Malawi remains sound, notwithstanding the challenges being faced by some banks**. Non-performing loans are at low levels—their share as a ratio of total loans was 6. 4 percent as at end-September 2012. However, the deterioration in the macroeconomic environment in the last two years and the slow pace of recovery have elevated the risks to banks' portfolios. The RBM has intensified its monitoring and surveillance of the financial system with a view to detecting at an early stage emerging threats to financial stability.

## C. Fiscal Policy

20. **The FY2012/13 budget is under stress from higher inflation and continuing depreciation of the exchange rate.** In order to meet the increased need for resources to deliver reasonable levels of public services, the government appealed to Malawi's development partners to provide additional assistance over and above pledges reflected in the approved budget. A number of donors have responded positively with additional resources equivalent to about US$64 million in grants. This will allow the government to increase expenditure in several critical areas, including social spending and goods and services to maintain basic functions of the government. **A restrained fiscal stance is needed to help stabilize the exchange rate and build international reserves.** Increased project loans allow the authorities to finance a larger overall fiscal deficit, while increased external grants allow them to both increase social spending and also reduce domestic borrowing (the fiscal anchor of the program). The authorities agreed to a net government repayment equivalent to 1.3 percent of GDP for FY2012/13 (Tables 2a and 2b), compared to the programmed target of zero net domestic financing. The revised net repayment amount includes 0.8 percent of GDP in repayment already made by using carry-over revenues from last fiscal year to retire unbudgeted borrowing in the last quarter of FY2011/12 (see footnote 3). Thus, the extent of tightening based on developments in FY2012/13 is 0.5 percent of GDP. Proposed revisions to the FY2012/13 budget reflect an expanded resource envelope (reflecting additional grants and concessional loans), and increased allocations to FISP, interest payments and externally

financed development expenditure. Higher grants provided by donors will allow both higher social spending and reduced domestic financing to help stabilize the exchange rate.

| Malawi: Grants (2010/11-2014/15) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | FY2010/11 | FY2011/12 | FY2012/13 | | FY2013/14 | | FY2014/15 | |
| | Act. | Act. | Prog. | Rev. Prog. | Prog. | Rev. Prog. | Prog. | Rev. Prog. |
| | In millions of US dollars | | | | | | | |
| Total grants | 579.0 | 394.1 | 597.6 | 661.9 | 525.4 | 604.9 | 531.3 | 587.1 |
| Budget support | 100.2 | 1.5 | 208.1 | 234.2 | 147.1 | 196.8 | 157.7 | 183.1 |
| Dedicated | 255.1 | 173.3 | 185.0 | 197.7 | 176.2 | 185.1 | 170.0 | 179.2 |
| Project | 125.2 | 103.3 | 87.2 | 112.2 | 100.0 | 120.0 | 100.0 | 120.0 |
| Source: IMF staff estimates | | | | | | | | |

21. **The authorities are continuing their efforts to enhance domestic revenue mobilization.** Emphasis is being placed on further improving enforcement mechanisms through increased audits and use of modern information and communication technology (ICT) systems to improve revenue collection. Revenues are expected to improve through the adoption and use of electronic fiscal devices in the enforcement of VAT and the use of computerized cargo scanners on imports. A recent IMF mission provided advice on automating and managing taxpayer compliance to support a full self-assessment system, and on developing and implementing best practice performance indicators for tax and customs administration.

22. **The government is committed to strengthening the public financial management systems**. In order to strengthen the commitment control and avoid the accumulation of arrears (structural benchmark, Table 9), the commitment module in IFMIS is now being piloted and a press statement will be issued to the general public on procurement rules (MEFP ¶32). The authorities are also reviewing the functional requirements of IFMIS with a view to allowing financial transactions to be processed with very little manual intervention. Government is also making progress on improving the cash management system, including improved co-ordination with the RBM.

23. **Staff discussed with the government the issue of converting verified arrears into government securities**. These arrears (estimated at about MK72 billion in June 2012) were incurred over the last three years by government ministries and departments and parastatals (on behalf of government) to suppliers of goods and services and contractors engaged in government construction projects. Most of the arrears have now been verified and certified by National Audit Office (structural benchmark, Table 9). As a way of settling these amounts, government has issued promissory notes to banks whose customers were affected and also directly to some service providers/contractors (MEFP ¶34). The notes cover four years from FY 2013/14 to 2016/17. This transaction is being incorporated into the medium term fiscal framework.

### D. Business Climate and International Competitiveness

24. Malawi ranks low globally and behind its neighbours in indicators of the business environment. For example it ranks 129th out of 144 countries in the 2012/13 Global Competitiveness Indices of the World Economic Forum, and 155th out of 183 countries in the 2013 World Bank Doing Business Report. According to the Business Climate Survey conducted annually by the Malawi Confederation of Chambers of Commerce and Industry the top five challenges to doing business in Malawi are: (i) electricity; (ii) transport infrastructure; (iii) exchange rate policy (i.e., misalignment); (iv) economic and regulatory policy uncertainty; and (v) cost of finance. The private sector also highlights inadequate educated and skilled workforce as a major obstacle. The government is committed to removing obstacles to doing business in Malawi and enhancing its international competitiveness, including by removing regulatory hurdles to starting a business, obtaining permits, registering property and trading across borders (MEFP ¶35–37).

## IV. PROGRAM ISSUES

25. **Performance under the program has been satisfactory.** Most of the quantitative targets and all structural benchmarks for the first review (end-September 2012) were met. The performance criteria on net international reserves, government net domestic borrowing and those related to external borrowing were all observed (Table 8a). However, the end-September 2012 performance criterion on the RBM's NDA and the indicative target on reserve money were not observed on account of RBM lending to banks to help them meet liquidity requirements after the devaluation. Delay in the procurement of fertilizers for the Farm Input Subsidy program (FISP) was the main reason why the authorities did not meet the indicative target on social spending (MEFP ¶14). Increased social spending in the second quarter of the fiscal year (October–December) is expected to make up for the shortfall in the first quarter. With respect to structural benchmarks (Table 9), the Malawi Revenue Authority (MRA) began publishing its monthly revenue collections in newspapers in July, the RBM posted the financial stability report for March 2012 on its website, and the Ministry of Finance established quarterly spending ceilings for the first and second quarters (MEFP ¶15).

26. **The authorities have implemented corrective measures that provide a basis for their request for a waiver for nonobservance of the performance criterion on the RBM NDA.** They have shut down uncollateralized lending to banks and conducted open market operations to absorb liquidity from the banking system. The RBM is undertaking an in depth assessment of distressed banks with a view to ensuring that they are on a path to meeting prudential requirements.

27. **The authorities are requesting modifications to performance criteria for end-December 2012 and end-March 2013 (Table 8b).** The modifications on the NDA of the RBM, central government net domestic borrowing, and net international reserves are needed to take account of: (i) disbursement of new emergency budget support (UK); (ii) the bringing forward of a large disbursement of already pledged budget support (EU); and (iii) a

½ percent of GDP tightening of the fiscal stance in FY2012/13. The indicative targets for June 2013 have also been revised to reflect the updated macroeconomic framework. Performance criteria for end-September 2013 are proposed.

28. **An update safeguards assessment for the Reserve Bank of Malawi is substantially complete.** The RBM continues to publish financial statements that are prepared and audited in accordance with international standards. However, the assessment reiterates a key safeguards concern—the lack of operational autonomy— and recommends that already envisaged amendments to the RBM Act to limit lending to government be expanded to strengthen RBM autonomy more broadly. Other recommendations focus on enhancing oversight of foreign reserves management and improvements to data compilation procedures. The latter includes measures to strengthen transparency of contingent liabilities arising from letters of credit that can have implications for program data. The RBM is committed to implementing the assessment's recommendations. The recommendations of the assessment do not require action in the context of the first review and will be closely monitored going forward.

29. **Risks from global spillovers.** Downside risks to the program include potential spillovers from the global economy, including stagnation of euro area and world growth, a substantial fall in non-oil commodity prices, and a reduction in aid flows. Slower world growth would adversely affect demand for Malawi's exports (mainly tobacco), but the overall impact on Malawi's growth is expected to be low. A substantial fall in tobacco prices would adversely affect export proceeds, the income of farmers and dampen growth. Given the size of tobacco in the economy (15 percent of GDP), the expected impact would be moderate. The risk of lower aid flows is low. Most of the major donors have indicated to staff that they would be prepared to scale up their support to Malawi if the government continues to implement appropriate economic policies and there is no deterioration in human rights and political governance. However, with the EU as one of the major donors, it is conceivable that over the medium term aid to Malawi might decline because of shrinking aid budgets in Europe.

30. **Other risks.** Adverse weather conditions and slippages in the implementation of economic reforms in the run up to the 2014 general elections also pose risks to the program. Adverse weather conditions pose a significant risk because of the continued reliance on rain-fed agriculture. Lower agricultural output would have a significant effect on overall GDP growth given the size of agriculture in GDP (30 percent). Slippages in policy implementation and structural reforms could lead to another cut in aid flows. Under the program, reductions in general budget support grants have to be offset by expenditure cuts (mainly in goods and services). It is important to avoid fiscal and monetary laxity in the run-up to the elections in 2014, in order to build credibility for Malawi's commitment to the implementation of prudent policies. Furthermore, failure to improve Malawi's relatively poor track record in implementing structural reforms would dampen the country's prospects for long-term growth and reducing vulnerability to shocks.

## V. Staff Appraisal

31. **Given a more difficult external environment than envisaged when the program was formulated, the authorities deserve credit for keeping the program broadly on track.** In particular, they exercised fiscal discipline in not diverting available resources to lower priority spending. With respect to the targets under the program which were missed, the authorities have taken steps to speed up spending on social protection programs (including on FISP) and the RBM has taken measures to contain its NDA, including by shutting down the temporary uncollateralized lending window it established to help distressed banks meet their liquidity needs.

32. **The authorities' commitment to reforms remains strong and they deserve increased external support.** Staff welcomes the authorities' commitment to maintain the flexible exchange rate regime and automatic price adjustment mechanism for petroleum products. Fixing the exchange rate will quickly lead to overvaluation and associated problems that Malawi experienced over the last 2–3 years. The government cannot afford to subsidize petroleum products which are consumed disproportionately by the better off. Staff supports the authorities request for additional external financing to help them weather unanticipated shocks to agricultural output and to help them build international reserves from current precariously low levels. Staff welcomes the positive response by a few development partners to provide additional resources or advance disbursement of pledged amounts to tide the country over during the lean period of foreign exchange earnings (November–March).

33. **Given the low level of international reserves, a tightening of monetary and fiscal policies is needed to stabilize the exchange rate and contain inflation.** In order to avoid a depreciation-inflation spiral, the authorities should give over-riding priority to stabilizing the exchange rate by tightening monetary policy and exercising fiscal restraint, including temporarily saving a portion of additional grants they receive in order to contain aggregate demand.

34. **The RBM should enforce banking system prudential regulations more forcefully.** Most banks have adjusted their balance sheets after the devaluation and initial liquidity squeeze. A few banks that over extended themselves when the system was awash with liquidity are having a difficult time meeting liquid reserve requirements. Staff urges the RBM to speed up its assessment of the conditions of these banks and to move forward quickly with overseeing restructuring plans that put them back on sound financial footing.

35. **Staff recommends completion of the first review, based on satisfactory performance and policy commitments by the authorities.** Staff supports the requests for a waiver of non-observance of the end-September 2012 performance criterion on the RBM's NDA, for the modifications to performance criteria for December 2012 and March 2013, and for the establishment of new performance criteria for end-September 2013.

**Table 1. Malawi: Selected Economic Indicators, 2009–15**

| | |
|---|---|
| **Population (millions)** | **16.2** |
| **Per capita GDP ($US)** | **285** |
| **Poverty rate (%)** | **52** |

| | 2009 Act. | 2010 Act. | 2011 Prel. | 2012 Prog. | 2012 Prog. Nov. | 2013 Prog. . | 2013 Prog. Nov. | 2014 Proj. | 2015 Proj. |
|---|---|---|---|---|---|---|---|---|---|
| **National accounts and prices** (percent change, unless otherwise indicated) | | | | | | | | | |
| GDP at constant market prices | 9.0 | 6.5 | 4.3 | 4.3 | 1.9 | 5.7 | 5.5 | 6.1 | 6.5 |
| Nominal GDP (billions of kwacha) [1] | 710.2 | 812.4 | 879.8 | 1,068.1 | 1,062.1 | 1,289.0 | 1,298.6 | 1,473.8 | 1,659.2 |
| GDP deflator | 8.4 | 7.4 | 3.8 | 16.4 | 18.5 | 14.2 | 15.9 | 7.0 | 5.7 |
| Consumer prices (end of period) | 7.6 | 6.3 | 9.8 | 22.9 | 31.7 | 12.0 | 10.1 | 5.8 | 5.4 |
| Consumer prices (annual average) | 8.4 | 7.4 | 7.6 | 18.4 | 20.8 | 16.1 | 18.0 | 7.2 | 5.7 |
| **Investment and savings** (percent of GDP) | | | | | | | | | |
| National savings | 20.7 | 24.7 | 9.4 | 12.0 | 13.8 | 19.0 | 19.9 | 20.4 | 20.1 |
| Net factor income | -1.2 | -2.0 | -2.1 | -3.0 | -3.2 | -3.2 | -3.9 | -4.0 | -3.9 |
| Net official transfers | 9.4 | 15.7 | 6.4 | 11.5 | 14.8 | 11.1 | 14.4 | 14.3 | 13.2 |
| Net private transfers | 5.1 | 4.7 | 4.6 | 5.6 | 6.2 | 5.8 | 7.3 | 7.1 | 7.0 |
| Domestic savings | 7.5 | 6.3 | 0.6 | -2.2 | -3.9 | 5.3 | 2.1 | 3.0 | 3.8 |
| Government | -7.1 | -0.8 | -7.6 | -6.9 | -9.8 | -3.9 | -7.7 | -4.6 | -5.1 |
| Private | 14.6 | 7.0 | 8.1 | 4.7 | 5.9 | 9.2 | 9.8 | 7.6 | 8.9 |
| National investment | 25.6 | 26.0 | 15.3 | 16.2 | 17.4 | 20.7 | 21.4 | 22.4 | 22.4 |
| Government | 6.5 | 9.6 | 6.7 | 7.5 | 8.7 | 7.0 | 8.1 | 8.5 | 7.9 |
| Private | 19.1 | 16.4 | 8.6 | 8.7 | 8.7 | 13.7 | 13.4 | 13.9 | 14.4 |
| Saving-investment balance [2] | -4.8 | -1.3 | -5.9 | -4.3 | -3.6 | -1.7 | -1.6 | -1.9 | -2.3 |
| Government | -5.0 | 1.5 | -9.6 | -5.3 | -6.4 | -2.0 | -4.1 | -1.4 | -2.2 |
| Private | 0.1 | -2.8 | 3.7 | 1.0 | 2.9 | 0.3 | 2.5 | -0.6 | 0.0 |
| **Central government** (percent of GDP on a fiscal year basis) [3] | | | | | | | | | |
| Revenue | 32.1 | 33.8 | 32.1 | 27.0 | 26.5 | 33.2 | 37.8 | 36.9 | 35.8 |
| Tax and nontax revenue | 20.5 | 23.5 | 24.5 | 21.5 | 22.1 | 22.8 | 23.3 | 24.1 | 24.5 |
| Grants | 11.6 | 10.3 | 7.6 | 5.5 | 4.4 | 10.4 | 14.5 | 12.8 | 11.3 |
| Expenditure and net lending | 37.8 | 33.8 | 35.0 | 34.0 | 35.0 | 34.3 | 39.7 | 38.9 | 37.5 |
| Overall balance (excluding grants) | -17.3 | -10.3 | -10.5 | -12.5 | -13.0 | -11.6 | -16.5 | -14.7 | -12.9 |
| Overall balance | -5.7 | 0.1 | -2.9 | -7.0 | -8.5 | -1.1 | -1.9 | -1.9 | -1.6 |
| Foreign financing | 2.0 | 0.9 | 1.3 | 1.6 | 1.6 | 1.1 | 2.4 | 1.9 | 1.6 |
| Domestic financing | 3.7 | -0.9 | 1.7 | 5.6 | 6.6 | 0.0 | -1.3 | 0.0 | 0.0 |
| Privatization | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Discrepancy | -0.1 | -0.1 | -0.1 | -0.2 | 0.3 | 0.0 | 0.8 | 0.1 | 0.0 |
| **Money and credit** (change in percent of broad money at the beginning of the period, unless otherwise indicated) | | | | | | | | | |
| Money and quasi money | 23.9 | 33.9 | 35.7 | 18.2 | 17.1 | 24.5 | 26.5 | 16.9 | 20.5 |
| Net foreign assets | -15.5 | 13.3 | -7.9 | -1.2 | -0.6 | 11.3 | 13.9 | 11.3 | 10.8 |
| Net domestic assets | 39.5 | 20.6 | 43.6 | 19.5 | 17.7 | 13.2 | 12.7 | 5.6 | 9.7 |
| Credit to the government | 19.4 | -9.2 | 19.7 | 11.0 | 2.3 | 2.9 | 6.3 | -1.0 | 2.0 |
| Credit to the rest of the economy (percent change) | 36.5 | 47.6 | 30.1 | 17.5 | 19.7 | 16.7 | 9.7 | 10.8 | 13.4 |
| **External sector** (US$ millions, unless otherwise indicated) | | | | | | | | | |
| Exports (goods and services) | 1,050.2 | 1,360.4 | 1,408.7 | 1,386.1 | 1,357.5 | 1,604.1 | 1,603.6 | 1,725.5 | 1,861.3 |
| Imports (goods and services) | 1,961.1 | 2,425.4 | 2,236.2 | 2,257.6 | 2,259.6 | 2,349.2 | 2,329.6 | 2,516.7 | 2,689.2 |
| Usable gross official reserves | 140.5 | 279.6 | 190.2 | 204.5 | 214.7 | 405.7 | 403.3 | 547.1 | 677.7 |
| (months of imports) | 0.7 | 1.5 | 1.0 | 1.0 | 1.1 | 2.0 | 1.9 | 2.4 | 2.8 |
| (percent of reserve money) | 40.7 | 73.4 | 42.5 | 52.8 | 75.0 | 91.3 | 117.3 | 140.3 | 140.7 |
| Current account (percent of GDP) | -4.8 | -1.3 | -5.9 | -4.3 | -3.6 | -1.7 | -1.6 | -1.9 | -2.3 |
| Current account, excl. official transfers (percent of GDP) | -14.2 | -17.0 | -12.3 | -15.7 | -18.3 | -12.7 | -16.0 | -16.2 | -15.5 |
| Real effective exchange rate (percent change) | 9.5 | -6.0 | -3.3 | … | … | … | … | … | … |
| Overall balance (percent of GDP) | -2.0 | 2.2 | -1.8 | -0.5 | -0.1 | 3.2 | 3.7 | 3.3 | 3.2 |
| Terms of trade (percent change) | 7.7 | 3.0 | -17.2 | 20.5 | -3.3 | 1.1 | 1.5 | 3.3 | 2.2 |
| **Debt stock and service** (percent of GDP, unless otherwise indicated) | | | | | | | | | |
| External debt (public sector) | 15.9 | 16.0 | 16.2 | 20.3 | 22.7 | 20.6 | 26.6 | 24.9 | 23.1 |
| NPV of debt (percent of exports) | 57.1 | 44.6 | 48.1 | 52.2 | 53.3 | 46.1 | 46.1 | 42.1 | 38.0 |
| External debt service (percent of exports) | 1.3 | 1.3 | 1.6 | 2.4 | 2.4 | 2.5 | 2.5 | 3.8 | 3.8 |
| External debt service (percent of revenue excl. grants) | 1.4 | 1.5 | 1.7 | 3.6 | 3.9 | 4.0 | 5.1 | 7.1 | 7.0 |
| 91-day treasury bill rate (end of period) | 10.5 | 6.2 | 6.8 | … | … | … | … | … | … |

Sources: Malawian authorities and IMF staff estimates.

[1] Reflects substantial upward revisions to the historical national accounts data received in March 2011.

[2] The government savings—investment balance is calculated adding foreign grants to government savings above.
The private savings—investment balance is calculated adding the items in the balance of payments, net of foreign grants, to private savings above.

[3] For example, 2009 refers to fiscal year 2008/09, which is from July 1, 2008, to June 30, 2009.

# Table 2a. Malawi: Central Government Operations, 2009/10–2014/15

## (Billions of kwacha)

| | 2009/10 | 2010/11 | 2011/12 | | 2012/13 | | 2013/14 | 2014/15 |
|---|---|---|---|---|---|---|---|---|
| | Actual | Actual | Prog. | Prel. | Prog. | Rev. Prog. Nov. | Proj. | Proj. |
| Revenue | 257 | 272 | 260 | 257 | 394 | 446 | 512 | 561 |
| Tax and nontax revenue | 179 | 208 | 208 | 214 | 270 | 275 | 335 | 384 |
| Tax revenue | 142 | 176 | 181 | 188 | 236 | 242 | 295 | 340 |
| Taxes on income and profits | 66 | 81 | 90 | 90 | 111 | 114 | 134 | 152 |
| Taxes on goods and services | 64 | 79 | 80 | 84 | 102 | 106 | 133 | 155 |
| Taxes on international trade | 15 | 17 | 18 | 18 | 31 | 30 | 38 | 42 |
| Other | -4 | -2 | -6 | -3 | -7 | -7 | -9 | -10 |
| Nontax revenue | 37 | 32 | 27 | 26 | 34 | 33 | 39 | 44 |
| Grants | 78 | 64 | 53 | 43 | 124 | 171 | 178 | 177 |
| Budget support | 34 | 15 | 0 | 0 | 54 | 73 | 70 | 67 |
| Project | 26 | 19 | 17 | 18 | 23 | 35 | 42 | 44 |
| Dedicated grants | 19 | 31 | 35 | 25 | 48 | 64 | 65 | 66 |
| *Of which:* | | | 0 | | | | | |
| DFID/EU (maize, fertilizer and seed) | 4 | 3 | 7 | 9 | 9 | 16 | 9 | 7 |
| National AIDS Commission | 7 | 10 | 9 | 4 | 12 | 13 | 16 | 16 |
| Health Sector–Wide Approach (SWAp) | 8 | 11 | 10 | 4 | 8 | 12 | 14 | 14 |
| Education Sector–Wide Approach (SWAp) | | | | | | 19 | 21 | 22 |
| Road Sector Support | | | | | | 4 | 5 | 6 |
| Expenditure and net lending | 257 | 296 | 328 | 340 | 408 | 469 | 539 | 587 |
| Current expenditure | 196 | 230 | 251 | 262 | 332 | 370 | 416 | 456 |
| Wages and salaries | 45 | 58 | 70 | 70 | 87 | 92 | 108 | 122 |
| Interest payments | 21 | 23 | 20 | 24 | 29 | 33 | 32 | 28 |
| Domestic | 21 | 22 | 19 | 22 | 25 | 29 | 27 | 23 |
| Foreign | 1 | 1 | 2 | 2 | 4 | 4 | 5 | 5 |
| Goods and services | 84 | 95 | 103 | 95 | 122 | 138 | 160 | 177 |
| Generic goods and services | 44 | 41 | 60 | 53 | 54 | 61 | 72 | 77 |
| Census | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Roads | 8 | 8 | 6 | 7 | 11 | 10 | 11 | 12 |
| Health SWAp | 20 | 19 | 16 | 16 | 20 | 23 | 28 | 31 |
| Education SWAp | 0 | 10 | 11 | 9 | 18 | 20 | 26 | 30 |
| National/local elections | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Statutory expenditures | 2 | 3 | 4 | 4 | 5 | 5 | 6 | 7 |
| National AIDS Commission | 8 | 12 | 5 | 5 | 13 | 13 | 16 | 18 |
| Maize purchases | 2 | 2 | 1 | 1 | 1 | 5 | 1 | 1 |
| Subsidies and other current transfers | 45 | 54 | 58 | 59 | 84 | 98 | 103 | 117 |
| Pension and gratuities | 6 | 12 | 12 | 10 | 19 | 16 | 18 | 21 |
| Transfers to road and revenue authorities | 4 | 5 | 4 | 5 | 7 | 8 | 0 | 0 |
| Transfers to public entities | 13 | 15 | 17 | 17 | 17 | 19 | 23 | 26 |
| Fertilizer and seed subsidy | 22 | 22 | 25 | 26 | 41 | 55 | 62 | 71 |
| Arrears adjustment | 0 | 0 | 0 | 15 | 10 | 10 | 13 | 12 |
| Development expenditure | 60 | 65 | 77 | 78 | 76 | 99 | 123 | 131 |
| Part I (foreign financed) | 34 | 32 | 35 | 35 | 39 | 63 | 78 | 81 |
| Part II (domestically financed) | 26 | 33 | 42 | 42 | 38 | 36 | 45 | 50 |
| Net lending | 1 | 1 | 0 | 0 | | 0 | 0 | 0 |
| Overall balance (including grants) | 0 | -24 | -68 | -83 | -13 | -23 | -27 | -26 |
| Discrepancy [1] | 0 | -1 | -2 | 0 | 0 | 10 | 0 | 0 |
| Overall balance (including grants and discrepancy) | 0 | -25 | -70 | -83 | -13 | -13 | -27 | -26 |
| Total financing (net) | 0 | 25 | 70 | 83 | 13 | 13 | 27 | 26 |
| Foreign financing (net) | 7 | 11 | 16 | 16 | 13 | 28 | 26 | 25 |
| Borrowing | 8 | 13 | 18 | 18 | 19 | 34 | 35 | 37 |
| Program | 0 | 0 | 0 | 1 | 3 | 5 | 0 | 0 |
| Project | 8 | 13 | 18 | 17 | 16 | 29 | 35 | 37 |
| Other concessional | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Amortization | -2 | -2 | -3 | -3 | -6 | -6 | -9 | -11 |
| Domestic financing (net) | -7 | 14 | 54 | 65 | 0 | -15 | 0 | 0 |
| Privatization | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| *Memorandum items:* | | | | | | | | |
| Overall balance (excluding grants) | -78 | -89 | -121 | -123 | -138 | -194 | -204 | -203 |
| Nominal GDP | 761 | 846 | 964 | 971 | 1,188 | 1,180 | 1,386 | 1,567 |
| Net domestic debt | 110 | 138 | 192 | 188 | 224 | 170 | 170 | 170 |
| Net domestic debt in precent of GDP | 14 | 16 | 20 | 20 | 19 | 14 | 11 | 10 |

Sources: Malawi Ministry of Finance and IMF staff estimates.

[1] The large discrepancy in 2012/13 is due to a carry-over of about 24 bln MKW from 2011/2012, of which about 14 bln MKW was later repaid, leaving a balance of about 10 bln MKW.

## Table 2b. Malawi: Central Government Operations, 2009/10–2014/15

(Percent of GDP)

| | 2009/10 | 2010/11 | 2011/12 | | 2012/13 | | 2013/14 | 2014/15 |
|---|---|---|---|---|---|---|---|---|
| | Actual | Actual | Prog. | Prel. | Prog. | Rev. Prog. Nov. | Proj. | Proj. |
| Revenue | 33.8 | 32.1 | 27.0 | 26.5 | 33.2 | 37.8 | 36.9 | 35.8 |
| Tax and nontax revenue | 23.5 | 24.5 | 21.5 | 22.1 | 22.8 | 23.3 | 24.1 | 24.5 |
| Tax revenue | 18.6 | 20.8 | 18.8 | 19.4 | 19.9 | 20.5 | 21.3 | 21.7 |
| Taxes on income and profits | 8.7 | 9.6 | 9.3 | 9.2 | 9.3 | 9.6 | 9.6 | 9.7 |
| Taxes on goods and services | 8.5 | 9.4 | 8.3 | 8.6 | 8.6 | 8.9 | 9.6 | 9.9 |
| Taxes on international trade | 2.0 | 2.1 | 1.8 | 1.8 | 2.6 | 2.5 | 2.7 | 2.7 |
| Other | -0.5 | -0.3 | -0.7 | -0.3 | -0.6 | -0.6 | -0.6 | -0.6 |
| Nontax revenue | 4.9 | 3.8 | 2.8 | 2.7 | 2.9 | 2.8 | 2.8 | 2.8 |
| Grants | 10.3 | 7.6 | 5.5 | 4.4 | 10.4 | 14.5 | 12.8 | 11.3 |
| Budget support | 4.5 | 1.8 | 0.0 | 0.0 | 4.5 | 6.1 | 5.0 | 4.3 |
| Project | 3.4 | 2.2 | 1.8 | 1.9 | 1.9 | 2.9 | 3.1 | 2.8 |
| Dedicated grants | 2.4 | 3.6 | 3.6 | 2.5 | 4.0 | 5.4 | 4.7 | 4.2 |
| *Of which:* | | | | | | | | |
| DFID/EU (maize, fertilizer and seed) | 0.5 | 0.3 | 0.7 | 0.9 | 0.7 | 1.4 | 0.7 | 0.4 |
| National AIDS Commission | 0.9 | 1.1 | 0.9 | 0.4 | 1.0 | 1.1 | 1.1 | 1.0 |
| Health Sector–Wide Approach (SWAp) | 1.1 | 1.3 | 1.1 | 0.4 | 0.7 | 1.0 | 1.0 | 0.9 |
| Education Sector–Wide Approach (SWAp) | | | | | | 1.6 | 1.5 | 1.4 |
| Road Sector Support | | | | | | 0.4 | 0.4 | 0.4 |
| Expenditure and net lending | 33.8 | 35.0 | 34.0 | 35.0 | 34.3 | 39.7 | 38.9 | 37.5 |
| Current expenditure | 25.7 | 27.2 | 26.0 | 27.0 | 27.9 | 31.4 | 30.0 | 29.1 |
| Wages and salaries | 5.9 | 6.9 | 7.2 | 7.2 | 7.3 | 7.8 | 7.8 | 7.8 |
| Interest payments | 2.8 | 2.7 | 2.1 | 2.4 | 2.4 | 2.8 | 2.3 | 1.8 |
| Domestic | 2.7 | 2.6 | 1.9 | 2.2 | 2.1 | 2.5 | 2.0 | 1.5 |
| Foreign | 0.1 | 0.1 | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 | 0.3 |
| Goods and services | 11.0 | 11.2 | 10.7 | 9.8 | 10.3 | 11.7 | 11.6 | 11.3 |
| Generic goods and services | 5.8 | 4.8 | 6.3 | 5.5 | 4.6 | 5.2 | 5.2 | 4.9 |
| Census | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Roads | 1.0 | 0.9 | 0.7 | 0.7 | 0.9 | 0.8 | 0.8 | 0.8 |
| Health SWAp | 2.6 | 2.2 | 1.6 | 1.7 | 1.7 | 2.0 | 2.0 | 2.0 |
| Education SWAp | 0.0 | 1.2 | 1.1 | 0.9 | 1.5 | 1.7 | 1.9 | 1.9 |
| National/local elections | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Statutory expenditures | 0.2 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 |
| National AIDS Commission | 1.0 | 1.5 | 0.5 | 0.5 | 1.1 | 1.1 | 1.2 | 1.2 |
| Maize purchases | 0.3 | 0.2 | 0.1 | 0.1 | 0.1 | 0.4 | 0.1 | 0.1 |
| Subsidies and other current transfers | 6.0 | 6.4 | 6.0 | 6.1 | 7.0 | 8.3 | 7.5 | 7.5 |
| Pension and gratuities | 0.8 | 1.4 | 1.2 | 1.1 | 1.6 | 1.3 | 1.3 | 1.3 |
| Transfers to road and revenue authorities | 0.6 | 0.6 | 0.5 | 0.6 | 0.6 | 0.7 | 0.0 | 0.0 |
| Transfers to public entities | 1.7 | 1.7 | 1.7 | 1.8 | 1.4 | 1.6 | 1.6 | 1.6 |
| Fertilizer and seed subsidy | 2.9 | 2.6 | 2.6 | 2.7 | 3.4 | 4.7 | 4.5 | 4.5 |
| Development expenditure | 7.9 | 7.7 | 8.0 | 8.0 | 6.4 | 8.4 | 8.8 | 8.4 |
| Part I (foreign financed) | 4.5 | 3.7 | 3.7 | 3.6 | 3.2 | 5.4 | 5.6 | 5.2 |
| Part II (domestically financed) | 3.4 | 3.9 | 4.4 | 4.4 | 3.2 | 3.0 | 3.2 | 3.2 |
| Net lending | 0.2 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Overall balance (including grants) | 0.1 | -2.9 | -7.0 | -8.5 | -1.1 | -1.9 | -1.9 | -1.6 |
| Discrepancy[1] | -0.1 | -0.1 | 0.0 | 0.0 | 0.0 | 0.8 | 0.0 | 0.0 |
| Overall balance (including grants and discrepancy) | 0.0 | -2.9 | 7.0 | -8.5 | -1.1 | -1.1 | -1.9 | -1.6 |
| Total financing (net) | -0.1 | 2.9 | 7.0 | 8.5 | 1.1 | 1.1 | 1.9 | 1.6 |
| Foreign financing (net) | 0.9 | 1.3 | 1.6 | 1.6 | 1.1 | 2.4 | 1.9 | 1.6 |
| Borrowing | 1.1 | 1.5 | 1.9 | 1.9 | 1.6 | 2.9 | 2.6 | 2.3 |
| Program | 0.0 | 0.0 | 0.0 | 0.1 | 0.3 | 0.4 | 0.0 | 0.0 |
| Project | 1.1 | 1.5 | 1.9 | 1.8 | 1.3 | 2.4 | 2.6 | 2.3 |
| Other concessional | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Amortization | -0.2 | -0.2 | -0.3 | -0.3 | -0.5 | -0.5 | -0.7 | -0.7 |
| Domestic financing (net) | -0.9 | 1.7 | 5.6 | 6.6 | 0.0 | -1.3 | 0.0 | 0.0 |
| Privatization | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| *Memorandum items:* | | | | | | | | |
| Overall balance (excluding grants) | -10.3 | -10.5 | -12.5 | -12.7 | -11.6 | -16.5 | -14.7 | -12.9 |
| Nominal GDP | 761 | 846 | 964 | 971 | 1,188 | 1,180 | 1,386 | 1,567 |
| Net domestic debt | 110 | 138 | 192 | 188.0 | 224 | 170 | 170 | 170 |
| Net domestic debt, percent of GDP | 14 | 16 | 20 | 20 | 19 | 14 | 12 | 11 |

Sources: Malawi Ministry of Finance and IMF staff estimates.

[1] The large discrepancy in 2012/13 is due to a carry-over of about 24 bln MKW from 2011/2012, of which about 14 bln MKW was later repaid, leaving a balance of about 10 bln MKW.

**Table 2c. Malawi: Central Government Operations, 2012/2013**
(Millions of kwacha)

| | Q1 Act. | Q1 prog. | Q2 Proj. | Q3 Proj. | Q4 Proj. | Annual |
|---|---|---|---|---|---|---|
| Revenue | 123 | 122 | 120 | 89 | 115 | 446 |
| Tax and nontax revenue | 64 | 73 | 69 | 64 | 77 | 275 |
| Tax revenue | 58 | 63 | 61 | 55 | 68 | 242 |
| Taxes on income and profits | 26 | 24 | 27 | 27 | 34 | 114 |
| Taxes on goods and services | 15 | 28 | 15 | 15 | 17 | 61 |
| Taxes on international trade | 14 | 13 | 13 | 14 | 16 | 57 |
| Other | 1 | -2 | 1 | 1 | 1 | 4 |
| Nontax revenue | 6 | 11 | 8 | 9 | 9 | 33 |
| Grants | 59 | 48 | 51 | 24 | 37 | 171 |
| Budget support | 24 | 22 | 26 | 2 | 20 | 73 |
| Project | 15 | 6 | 6 | 6 | 7 | 35 |
| Dedicated grants | 19 | 21 | 19 | 16 | 11 | 64 |
| *Of which:* | | | | | | |
| DFID/EU (maize, fertilizer and seed) | 2 | 2 | 8 | 3 | 3 | 16 |
| National AIDS Commission | 1 | 5 | 4 | 4 | 4 | 13 |
| Health Sector–Wide Approach (SWAp) | 8 | 5 | 0 | 3 | 0 | 12 |
| Expenditure and net lending | 107 | 115 | 142 | 116 | 104 | 469 |
| Current expenditure | 78 | 90 | 117 | 92 | 83 | 370 |
| Wages and salaries | 21 | 20 | 24 | 24 | 24 | 92 |
| Interest payments | 8 | 9 | 8 | 9 | 8 | 33 |
| Domestic | 7 | 9 | 8 | 8 | 6 | 29 |
| Foreign | 1 | 1 | 1 | 1 | 1 | 4 |
| Goods and services | 32 | 33 | 35 | 34 | 37 | 138 |
| Generic goods and services | 16 | 10 | 14 | 14 | 17 | 61 |
| Census | 0 | 0 | 0 | 0 | 0 | 0 |
| Roads | 2 | 4 | 3 | 3 | 3 | 10 |
| Health SWAp | 5 | 9 | 6 | 5 | 7 | 23 |
| Education SWAp | 4 | 4 | 5 | 5 | 6 | 20 |
| National / local elections | 0 | 0 | 0 | 0 | 0 | 0 |
| Statutory expenditures | 1 | 1 | 1 | 1 | 1 | 5 |
| National AIDS Commission | 2 | 3 | 6 | 2 | 3 | 13 |
| Maize purchases | 1 | 1 | 0 | 4 | 0 | 5 |
| Subsidies and other current transfers | 12 | 25 | 46 | 25 | 15 | 98 |
| Pension and gratuities | 4 | 5 | 4 | 4 | 4 | 16 |
| Transfers to road and revenue authorities | 2 | 2 | 2 | 2 | 2 | 8 |
| Transfers to public entities | 5 | 4 | 6 | 5 | 3 | 19 |
| Fertilizer and seed subsidy | 0 | 13 | 35 | 15 | 5 | 55 |
| Development expenditure | 29 | 25 | 26 | 24 | 21 | 99 |
| Part I (foreign financed) | 18 | 9 | 15 | 15 | 16 | 63 |
| Part II (domestically financed) | 12 | 15 | 11 | 8 | 5 | 36 |
| Net lending | | | | | | |
| Overall balance (including grants) | 15 | 7 | -22 | -27 | 11 | -23 |
| Discrepancy | 24 | 0 | -10 | -4 | 0 | 10 |
| Overall balance (including grants and discrepancy) | 39 | 7 | -32 | -31 | 11 | -13 |
| Total financing (net) | -39 | -7 | 32 | 31 | -11 | 13 |
| Foreign financing (net) | 2 | 5 | 9 | 9 | 9 | 28 |
| Borrowing | 2 | 6 | 10 | 11 | 11 | 34 |
| Program | 0 | 2 | 2 | 2 | 2 | 5 |
| Project | 2 | 4 | 9 | 9 | 9 | 29 |
| Other concessional | 0 | 0 | 0 | 0 | 0 | 0 |
| Amortization | 0 | -1 | -2 | -2 | -2 | -6 |
| Domestic financing (net) | -41 | -12 | 23 | 22 | -19 | -15 |
| Privatization | | | | | | |

Sources: Malawi Ministry of Finance and IMF staff estimates.

## Table 3a. Malawi: Monetary Authorities' Survey, 2009–15

(Billions of Kwacha, unless otherwise indicated)

| | 2009 | 2010 | 2011 | 2012 | | | | | | | 2013 | | | | | | | | 2014 | 2015 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Q1 | Q2 | Q3 | Q4 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | | |
| | Act. | Act. | Act. | Act. | | Prog. | | Act. | Act. | Rev. Prog. | | Prog. | | | | Rev. Prog. | | | Proj. | |
| Reserve money | 50 | 57 | 73 | 89 | 76 | 88 | 98 | 101 | 96 | 97 | 99 | 106 | 114 | 119 | 99 | 108 | 112 | 122 | 143 | 182 |
| Currency outside banks | 27 | 31 | 42 | 37 | … | … | … | … | … | … | … | … | … | … | … | … | … | … | … | … |
| Cash in vault | 6 | 9 | 11 | 9 | … | … | … | … | … | … | … | … | … | … | … | … | … | … | … | … |
| Commercial bank deposits with RBM | 17 | 18 | 20 | 43 | … | … | … | … | … | … | … | … | … | … | … | … | … | … | … | … |
| Net foreign assets (NFA) [1] | -9 | 8 | -9 | -18 | -37 | -21 | -20 | -43 | -25 | -23 | -7 | 5 | 12 | 20 | -35 | -7 | 19 | 26 | 76 | 132 |
| Foreign assets [2] | 24 | 46 | 32 | 24 | 26 | 47 | 52 | 23 | 54 | 74 | 70 | 86 | 97 | 109 | 68 | 103 | 130 | 144 | 202 | 257 |
| Foreign liabilities | -34 | -37 | -40 | -41 | -63 | -68 | -73 | -66 | -80 | -96 | -77 | -81 | -85 | -89 | -103 | -111 | -111 | -118 | -119 | -126 |
| Net domestic assets | 60 | 49 | 82 | 107 | 113 | 109 | 118 | 144 | 121 | 119 | 106 | 101 | 101 | 99 | 134 | 115 | 92 | 96 | 67 | 50 |
| Credit to government (net) 3 | 86 | 73 | 103 | 125 | 126 | 118 | 139 | 136 | 92 | 109 | 135 | 126 | 143 | 148 | 125 | 111 | 107 | 127 | 123 | 132 |
| Credit to statutory bodies (net) | 1 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Credit to domestic banks | 0 | 0 | 0 | 3 | 3 | 3 | 3 | 20 | 12 | 4 | 3 | 3 | 3 | 3 | 4 | 4 | 4 | 4 | 4 | 4 |
| Other items (net)[3] | -27 | -24 | -21 | -20 | -16 | -12 | -24 | -12 | 16 | 7 | -31 | -28 | -44 | -51 | 6 | 0 | -19 | -35 | -60 | -86 |
| *Memorandum items:* | | | | | | | | | | | | | | | | | | | | |
| Money multiplier | 3.4 | 4.0 | 4.3 | 3.5 | 4.2 | 3.8 | 3.8 | 3.5 | 3.7 | 3.8 | 3.9 | 3.8 | 3.7 | 3.9 | 3.8 | 3.8 | 3.8 | 3.8 | 3.8 | 3.6 |
| 91-day treasury bill rate | 10.5 | 6.2 | 6.8 | 7.1 | … | … | … | 15.6 | … | … | … | … | … | … | … | … | … | … | … | … |
| NFA (US$ millions) | -65 | 54 | -54 | -107 | -148 | -82 | -80 | -158 | -85 | -68 | -27 | 19 | 47 | 74 | -103 | -21 | 55 | 73 | 207 | 349 |
| Foreign assets (US$ millions) | 167 | 302 | 193 | 141 | 103 | 187 | 208 | 86 | 182 | 218 | 277 | 340 | 365 | 409 | 200 | 299 | 372 | 406 | 550 | 681 |
| Foreign liabilities (US$ millions) | -231 | -248 | -247 | -248 | -250 | -269 | -287 | -244 | -267 | -285 | -304 | -321 | -318 | -335 | -303 | -320 | -317 | -334 | -344 | -332 |

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

[1] Including SDR allocation and the entire assets and liabilities of the RBM

[2] Reserve holdings managed by the Crown Agents have not yet been verified by an independent audit agency. These assets amounted to US$3.2 million at end-September, 2012.

[3] Includes recapitalization of RBM with a transfer of treasury bills in the amount of 29.3 billion in January 2008.

## Table 3b. Malawi: Monetary Survey, 2009–15

### (Billions of Kwacha, unless otherwise indicated)

| | | | | 2012 | | | | | | | 2013 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2009 | 2010 | 2011 | Q1 | Q2 | Q3 | Q4 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | 2014 | 2015 |
| | Act. | | | Act. | Prog. | | | Act. | Act. | Rev. Prog. | Prog. | | | | Rev. Prog. | | | | Proj. | |
| Money and quasi-money | 173 | 232 | 314 | 316 | 320 | 332 | 372 | 357 | 350 | 368 | 387 | 402 | 422 | 463 | 379 | 410 | 428 | 466 | 545 | 656 |
| Money | 82 | 125 | 164 | 156 | ... | ... | ... | 160 | 145 | ... | ... | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| Quasi-money | 91 | 107 | 150 | 160 | ... | ... | ... | 135 | 151 | ... | ... | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| *Of which:* foreign currency deposits | 18 | 21 | 26 | 27 | ... | ... | ... | 60 | 56 | ... | ... | ... | ... | ... | ... | ... | ... | ... | ... | ... |
| | | | | | | | | | | | | | | | | | | | | |
| Net foreign assets (NFA) 1/ | -2 | 21 | 3 | -4 | -19 | -3 | -1 | -4 | 10 | 1 | 12 | 24 | 32 | 41 | -11 | 18 | 45 | 52 | 105 | 163 |
| Monetary authorities | -9 | 8 | -9 | -18 | -37 | -21 | -20 | -43 | -25 | -23 | -7 | 5 | 12 | 20 | -35 | -7 | 19 | 26 | 76 | 132 |
| Gross foreign assets | 24 | 46 | 32 | 24 | 26 | 47 | 52 | 23 | 54 | 74 | 70 | 86 | 97 | 109 | 68 | 103 | 130 | 144 | 202 | 257 |
| Foreign liabilities | -34 | -37 | -40 | -41 | -63 | -68 | -73 | -66 | -80 | -96 | -77 | -81 | -85 | -89 | -103 | -111 | -111 | -118 | -126 | -126 |
| Commercial banks (net) | 7 | 13 | 11 | 14 | 18 | 18 | 19 | 39 | 36 | 24 | 19 | 19 | 20 | 21 | 24 | 25 | 25 | 26 | 29 | 30 |
| | | | | | | | | | | | | | | | | | | | | |
| Net domestic assets | 175 | 211 | 312 | 320 | 339 | 335 | 373 | 360 | 340 | 367 | 375 | 379 | 389 | 422 | 390 | 392 | 384 | 414 | 440 | 493 |
| Credit to government (net) | 111 | 95 | 141 | 157 | 159 | 148 | 175 | 169 | 127 | 148 | 169 | 159 | 179 | 186 | 168 | 150 | 146 | 171 | 166 | 177 |
| Credit to statutory bodies (net) | 6 | 5 | 20 | 18 | 18 | 18 | 18 | 17 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 |
| Credit to private sector | 95 | 145 | 175 | 179 | 193 | 200 | 210 | 208 | 209 | 215 | 219 | 234 | 222 | 249 | 217 | 237 | 233 | 237 | 265 | 303 |
| Other items (net) | -37 | -34 | -24 | -34 | -31 | -31 | -31 | -34 | -14 | -13 | -31 | -32 | -31 | -31 | -13 | -13 | -13 | -12 | -9 | -5 |
| | | | | | | | | | | | | | | | | | | | | |
| *Memorandum items:* | | | | | | | | | | | | | | | | | | | | |
| Velocity of money (annualized GDP divided by broad money) | 4.0 | 3.5 | 2.8 | 2.9 | 3.0 | 3.1 | 2.9 | 2.7 | 2.9 | 2.9 | 2.9 | 3.0 | 2.9 | 2.8 | 3.0 | 2.9 | 2.9 | 2.8 | 2.7 | 2.5 |
| Annual growth of broad money (percent) | 23.9 | 33.9 | 35.7 | 34.3 | 20.5 | 13.7 | 18.2 | 34.3 | 19.9 | 17.1 | 22.4 | 25.7 | 26.9 | 24.5 | 19.8 | 14.9 | 22.3 | 26.5 | 16.9 | 20.5 |
| Annual growth of credit to the private sector (percent) | 39.5 | 52.4 | 20.5 | 17.7 | 18.6 | 20.8 | 20.6 | 27.8 | 26.6 | 23.0 | 22.2 | 21.1 | 11.3 | 18.1 | 21.3 | 14.0 | 11.3 | 10.6 | 11.6 | 14.3 |
| NFA of the commercial banks (US$ millions) | 50.7 | 81.6 | 68.5 | 83.3 | 71.4 | 71.4 | 74.5 | 144.0 | 119.7 | 69.8 | 74.5 | 74.5 | 74.5 | 78.8 | 70.8 | 71.7 | 72.7 | 73.7 | 78.1 | 83.2 |
| Gross foreign assets (US$ millions) | 77.9 | 92.0 | 103.9 | 113.6 | 98.2 | 98.2 | 98.2 | 172.3 | 139.9 | 139.9 | 98.2 | 98.2 | 98.2 | 98.2 | 141.8 | 143.7 | 145.7 | 147.6 | 156.5 | 166.8 |
| Foreign liabilities (US$ millions) | -27.2 | -10.5 | -35.4 | -30.3 | -26.8 | -26.8 | -23.7 | -28.2 | -20.2 | -70.1 | -23.7 | -23.7 | -23.7 | -19.5 | -71.0 | -72.0 | -72.9 | -73.9 | -78.4 | -83.5 |

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

[1] Including SDR allocation.

**Table 4a. Malawi: Balance of Payments, 2009–15**

**(US$ millions, unless otherwise indicated)**

| | 2009 Act. | 2010 Act. | 2011 Prel. | 2012 Prog. | 2012 Rev. Prog. | 2013 Prog. | 2013 Rev. Prog. | 2014 Proj. | 2015 Proj. |
|---|---|---|---|---|---|---|---|---|---|
| Current account balance (including grants) | -244.1 | -69.9 | -330.0 | -201.3 | -150.5 | -81.3 | -58.9 | -79.2 | -101.7 |
| Merchandise trade balance | -636.7 | -743.7 | -630.1 | -631.9 | -658.2 | -496.4 | -490.1 | -535.6 | -554.6 |
| Exports | 936.7 | 1,237.7 | 1,262.7 | 1,273.8 | 1,253.7 | 1,485.4 | 1,479.2 | 1,593.5 | 1,720.6 |
| *Of which:* Tobacco | 501.3 | 687.6 | 482.4 | 458.0 | 481.1 | 577.1 | 606.2 | 636.5 | 668.3 |
| Uranium | 8.5 | 113.4 | 120.4 | 164.3 | 154.4 | 180.8 | 169.9 | 186.8 | 205.5 |
| Imports | -1,573.3 | -1,981.3 | -1,892.7 | -1,905.7 | -1,911.9 | -1,981.8 | -1,969.3 | -2,129.1 | -2,275.2 |
| *Of which*: Petroleum | -166.4 | -180.9 | -168.8 | -190.2 | -169.4 | -187.5 | -164.7 | -165.1 | -166.4 |
| Services balance | -333.2 | -429.8 | -312.8 | -379.7 | -378.4 | -402.7 | -383.3 | -417.4 | -445.3 |
| Interest public sector (net) | -4.7 | -3.5 | -5.6 | -8.5 | -9.6 | -11.0 | -12.0 | -13.3 | -13.8 |
| Receipts | 0.4 | 0.1 | 0.4 | 1.7 | 0.8 | 1.7 | 0.7 | 0.7 | 0.7 |
| Payments | -5.1 | -3.6 | -6.0 | -10.2 | -10.4 | -12.7 | -12.7 | -13.9 | -14.5 |
| Other factor payments (net) | -54.2 | -105.0 | -109.7 | -131.5 | -124.8 | -143.0 | -135.5 | -148.5 | -158.1 |
| Nonfactor (net) | -274.3 | -321.4 | -197.5 | -239.6 | -244.0 | -248.8 | -235.8 | -255.7 | -273.3 |
| Receipts | 113.5 | 122.7 | 146.0 | 112.3 | 103.8 | 118.7 | 124.4 | 132.0 | 140.6 |
| Payments | -387.8 | -444.1 | -343.5 | -351.9 | -347.7 | -367.5 | -360.3 | -387.7 | -414.0 |
| Unrequited transfers (net) | 725.8 | 1,103.6 | 612.9 | 810.3 | 886.0 | 817.8 | 814.5 | 873.8 | 898.1 |
| Private (net) | 254.5 | 254.1 | 256.0 | 267.1 | 260.8 | 282.3 | 275.1 | 291.8 | 310.9 |
| Receipts | 267.7 | 267.7 | 270.8 | 282.5 | 275.9 | 298.7 | 291.1 | 308.7 | 328.9 |
| Payments | -13.2 | -13.6 | -14.8 | -15.5 | -15.1 | -16.4 | -15.9 | -16.9 | -18.0 |
| Official (net) | 471.2 | 849.5 | 356.9 | 543.2 | 625.2 | 535.5 | 539.3 | 582.0 | 587.2 |
| Receipts | 472.0 | 850.2 | 357.7 | 544.0 | 625.9 | 536.3 | 540.1 | 582.8 | 588.0 |
| Budget support | 81.6 | 321.7 | 0.0 | 88.1 | 171.5 | 185.3 | 162.6 | 178.0 | 183.1 |
| Project related[1] | 390.4 | 528.6 | 357.6 | 455.9 | 454.4 | 351.0 | 377.5 | 404.8 | 404.9 |
| Payments | -0.8 | -0.7 | -0.8 | -0.8 | -0.8 | -0.8 | -0.8 | -0.8 | -0.8 |
| Financial account balance | 235.0 | 280.3 | 157.4 | 177.8 | 145.7 | 234.8 | 199.3 | 213.2 | 243.7 |
| Medium- and long-term flows (net) | 151.3 | 90.5 | 108.9 | 90.6 | 81.8 | 121.6 | 89.4 | 71.2 | 67.1 |
| Disbursements | 73.4 | 104.4 | 123.3 | 108.5 | 100.3 | 144.8 | 112.7 | 100.0 | 100.0 |
| Budget support | 29.5 | 0.0 | 0.0 | 7.8 | 5.0 | 4.0 | 10.0 | 0.0 | 0.0 |
| Project support | 21.9 | 104.4 | 53.3 | 83.2 | 77.9 | 70.8 | 102.7 | 100.0 | 100.0 |
| Other medium-term loans | 22.0 | 0.0 | 70.0 | 17.4 | 17.4 | 70.0 | 0.0 | 0.0 | 0.0 |
| Amortization | -8.5 | -14.0 | -14.4 | -17.8 | -18.5 | -23.3 | -23.3 | -28.8 | -32.9 |
| SDR allocation | 86.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Foreign direct investment and other inflows | 55.5 | 158.2 | 60.8 | 83.4 | 61.9 | 108.2 | 105.3 | 136.7 | 170.6 |
| Short-term capital | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.8 | 0.8 | 0.8 | 0.9 |
| Commercial banks net foreign assets | 27.5 | 30.9 | -13.0 | 3.1 | 1.3 | 4.3 | 3.8 | 4.5 | 5.1 |
| Errors and omissions | -91.8 | -90.3 | 68.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Overall balance** | -100.9 | 120.1 | -103.7 | -23.4 | -4.8 | 153.4 | 140.4 | 133.9 | 142.0 |
| **Financing** | 100.9 | -120.1 | 106.9 | 23.4 | 4.8 | -153.4 | -140.4 | -133.9 | -142.0 |
| Gross reserves (- increase) | 98.5 | -139.1 | 107.7 | -14.3 | -32.1 | -201.2 | -188.7 | -143.8 | -130.6 |
| Liabilities[2] | 2.2 | 19.1 | -1.2 | 37.8 | 36.9 | 47.7 | 48.3 | 9.9 | -11.5 |
| *Of which:* IMF (net) | -0.4 | 21.2 | -0.1 | 37.6 | 36.6 | 51.7 | 51.9 | 14.4 | -6.8 |
| Purchases/drawings | 0.0 | 21.3 | 0.0 | 40.2 | 40.2 | 60.2 | 60.2 | 40.2 | 20.1 |
| Repurchases/repayments | 0.4 | 0.2 | 0.1 | 2.5 | 3.6 | 8.5 | 8.4 | 25.8 | 26.8 |
| *Memorandum items:* | | | | | | | | | |
| Gross official reserves[3] | 140.5 | 279.6 | 190.2 | 204.5 | 214.7 | 405.7 | 403.3 | 547.1 | 677.7 |
| Months of imports[4] | 0.7 | 1.5 | 1.0 | 1.0 | 1.1 | 2.0 | 1.9 | 2.4 | 2.8 |
| Current account balance (percent of GDP) | | | | | | | | | |
| Excluding official transfers | -14.2 | -17.0 | -12.3 | -15.7 | -18.3 | -12.7 | -16.0 | -16.2 | -15.5 |
| Including official transfers | -4.8 | -1.3 | -5.9 | -4.3 | -3.6 | -1.7 | -1.6 | -1.9 | -2.3 |
| Value of exports of goods and services (percent change) | 0.7 | 29.5 | 3.6 | -1.6 | -3.6 | 15.7 | 18.1 | 7.6 | 7.9 |
| Value of imports of goods and services (percent change) | -6.2 | 23.7 | -7.8 | 1.9 | 1.0 | 4.1 | 3.1 | 8.0 | 6.9 |
| REER (percent change) | 9.5 | -6.0 | -3.3 | … | … | … | … | … | … |
| Overall balance (percent of GDP) | -2.0 | 2.2 | -1.8 | -0.5 | -0.1 | 3.2 | 3.7 | 3.3 | 3.2 |
| Terms of trade (percent change) | 7.7 | 3.0 | -17.2 | 20.5 | -3.3 | 1.1 | 1.5 | 3.3 | 2.2 |
| Nominal GDP (millions of U.S. dollars) | 5,034.1 | 5,396.9 | 5,606.6 | 4,733.9 | 4,236.3 | 4,838.1 | 3,750.6 | 4,082.8 | 4,446.5 |

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

1 Includes estimate for project grants not channeled through the budget.

2 Excluding SDR allocation.

3 Figures for 2009 onward take account of Malawi's SDR allocation (SDR 55.4 million). Gross reserves are measured only from the balance sheet of the central bank and exclude holdings of the government overseas in the crown agent accounts, which was US$ 3.1 million at end-December 2010.

4 Months of prospective imports of goods and nonfactor services.

**Table 4b. Malawi: Balance of Payments, 2009–15**

**(Percent of GDP)**

| | 2009 Act. | 2010 Act. | 2011 Prel. | 2012 Prog. | 2012 Rev. Prog. | 2013 Prog. | 2013 Rev. Prog. | 2014 Proj. | 2015 Proj. |
|---|---|---|---|---|---|---|---|---|---|
| Current account balance (including grants) | -4.8 | -1.3 | -5.9 | -4.3 | -3.6 | -1.7 | -1.6 | -1.9 | -2.3 |
| Merchandise trade balance | -12.6 | -13.8 | -11.2 | -13.3 | -15.5 | -10.3 | -13.1 | -13.1 | -12.5 |
| Exports | 18.6 | 22.9 | 22.5 | 26.9 | 29.6 | 30.7 | 39.4 | 39.0 | 38.7 |
| *Of which:* Tobacco | 10.0 | 12.7 | 8.6 | 9.7 | 11.4 | 11.9 | 16.2 | 15.6 | 15.0 |
| Uranium | 0.2 | 2.1 | 2.1 | 3.5 | 3.6 | 3.7 | 4.5 | 4.6 | 4.6 |
| Imports | -31.3 | -36.7 | -33.8 | -40.3 | -45.1 | -41.0 | -52.5 | -52.1 | -51.2 |
| *Of which*: Petroleum | -3.3 | -3.4 | -3.0 | -4.0 | -4.0 | -3.9 | -4.4 | -4.0 | -3.7 |
| Services balance | -6.6 | -8.0 | -5.6 | -8.0 | -8.9 | -8.3 | -10.2 | -10.2 | -10.0 |
| Interest public sector (net) | -0.1 | -0.1 | -0.1 | -0.2 | -0.2 | -0.2 | -0.3 | -0.3 | -0.3 |
| Receipts | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Payments | -0.1 | -0.1 | -0.1 | -0.2 | -0.2 | -0.3 | -0.3 | -0.3 | -0.3 |
| Other factor payments (net) | -1.1 | -1.9 | -2.0 | -2.8 | -2.9 | -3.0 | -3.6 | -3.6 | -3.6 |
| Nonfactor (net) | -5.4 | -6.0 | -3.5 | -5.1 | -5.8 | -5.1 | -6.3 | -6.3 | -6.1 |
| Receipts | 2.3 | 2.3 | 2.6 | 2.4 | 2.4 | 2.5 | 3.3 | 3.2 | 3.2 |
| Payments | -7.7 | -8.2 | -6.1 | -7.4 | -8.2 | -7.6 | -9.6 | -9.5 | -9.3 |
| Unrequited transfers (net) | 14.4 | 20.4 | 10.9 | 17.1 | 20.9 | 16.9 | 21.7 | 21.4 | 20.2 |
| Private (net) | 5.1 | 4.7 | 4.6 | 5.6 | 6.2 | 5.8 | 7.3 | 7.1 | 7.0 |
| Receipts | 5.3 | 5.0 | 4.8 | 6.0 | 6.5 | 6.2 | 7.8 | 7.6 | 7.4 |
| Payments | -0.3 | -0.3 | -0.3 | -0.3 | -0.4 | -0.3 | -0.4 | -0.4 | -0.4 |
| Official (net) | 9.4 | 15.7 | 6.4 | 11.5 | 14.8 | 11.1 | 14.4 | 14.3 | 13.2 |
| Receipts | 9.4 | 15.8 | 6.4 | 11.5 | 14.8 | 11.1 | 14.4 | 14.3 | 13.2 |
| Budget support | 1.6 | 6.0 | 0.0 | 1.9 | 4.0 | 3.8 | 4.3 | 4.4 | 4.1 |
| Project related[1] | 7.8 | 9.8 | 6.4 | 9.6 | 10.7 | 7.3 | 10.1 | 9.9 | 9.1 |
| Payments | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Financial account balance | 4.7 | 5.2 | 2.8 | 3.8 | 3.4 | 4.9 | 5.3 | 5.2 | 5.5 |
| Medium- and long-term flows (net) | 3.0 | 1.7 | 1.9 | 1.9 | 1.9 | 2.5 | 2.4 | 1.7 | 1.5 |
| Disbursements | 1.5 | 1.9 | 2.2 | 2.3 | 2.4 | 3.0 | 3.0 | 2.4 | 2.2 |
| Budget support | 0.6 | 0.0 | 0.0 | 0.2 | 0.1 | 0.1 | 0.3 | 0.0 | 0.0 |
| Project support | 0.4 | 1.9 | 1.0 | 1.8 | 1.8 | 1.5 | 2.7 | 2.4 | 2.2 |
| Other medium-term loans | 0.4 | 0.0 | 1.2 | 0.4 | 0.4 | 1.4 | 0.0 | 0.0 | 0.0 |
| Amortization | -0.2 | -0.3 | -0.3 | -0.4 | -0.4 | -0.5 | -0.6 | -0.7 | -0.7 |
| SDR allocation | 1.7 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Foreign direct investment and other inflows | 1.1 | 2.9 | 1.1 | 1.8 | 1.5 | 2.2 | 2.8 | 3.3 | 3.8 |
| Short-term capital | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Commercial banks net foreign assets | 0.5 | 0.6 | -0.2 | 0.1 | 0.0 | 0.1 | 0.1 | 0.1 | 0.1 |
| Errors and omissions | -1.8 | -1.7 | 1.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Overall balance** | -2.0 | 2.2 | -1.8 | -0.5 | -0.1 | 3.2 | 3.7 | 3.3 | 3.2 |
| **Financing** | 2.0 | -2.2 | 1.9 | 0.5 | 0.1 | -3.2 | -3.7 | -3.3 | -3.2 |
| Gross reserves (- increase) | 2.0 | -2.6 | 1.9 | -0.3 | -0.8 | -4.2 | -5.0 | -3.5 | -2.9 |
| Liabilities[2] | 0.0 | 0.4 | 0.0 | 0.8 | 0.9 | 1.0 | 1.3 | 0.2 | -0.3 |
| *Of which:* IMF (net) | 0.0 | 0.4 | 0.0 | 0.8 | 0.9 | 1.1 | 1.4 | 0.4 | -0.2 |
| Purchases/drawings | 0.0 | 0.4 | 0.0 | 0.8 | 0.9 | 1.2 | 1.6 | 1.0 | 0.5 |
| Repurchases/repayments | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | 0.2 | 0.2 | 0.6 | 0.6 |
| *Memorandum items:* | | | | | | | | | |
| Gross official reserves[3] | 2.8 | 5.2 | 3.4 | 4.3 | 5.1 | 8.4 | 10.8 | 13.4 | 15.2 |
| Months of imports[4] | 0.7 | 1.5 | 1.0 | 1.0 | 1.1 | 2.0 | 1.9 | 2.4 | 2.8 |
| Current account balance (percent of GDP) | | | | | | | | | |
| Excluding official transfers | -14.2 | -17.0 | -12.3 | -15.7 | -18.3 | -12.7 | -16.0 | -16.2 | -15.5 |
| Including official transfers | -4.8 | -1.3 | -5.9 | -4.3 | -3.6 | -1.7 | -1.6 | -1.9 | -2.3 |
| Value of exports of goods and services (percent change) | 0.7 | 29.5 | 3.6 | -1.6 | -3.6 | 15.7 | 18.1 | 7.6 | 7.9 |
| Value of imports of goods and services (percent change) | -6.2 | 23.7 | -7.8 | 1.9 | 1.0 | 4.1 | 3.1 | 8.0 | 6.9 |
| REER (percent change) | 9.5 | -6.0 | -3.3 | … | … | … | … | … | … |
| Overall balance (percent of GDP) | -2.0 | 2.2 | -1.8 | -0.5 | -0.1 | 3.2 | 3.7 | 3.3 | 3.2 |
| Terms of trade (percent change) | 7.7 | 3.0 | -17.2 | 20.5 | -3.3 | 1.1 | 1.5 | 3.3 | 2.2 |

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

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

[2] Excluding SDR allocation.

[3] Figures for 2009 onward take account of Malawi's SDR allocation (SDR 55.4 million). Gross reserves are measured only from the balance sheet of the central bank and exclude

[4] Months of prospective imports of goods and nonfactor services.

**Table 5. Malawi: External Financing Requirement and Source, 2009–17**

| | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|---|---|---|---|
| Total requirement | -625 | -1072 | -593 | -826 | -814 | -845 | -860 | -871 | -916 |
| Current account, excluding official transfers | -715 | -919 | -687 | -776 | -598 | -661 | -689 | -735 | -793 |
| Debt amortization | -9 | -14 | -14 | -19 | -23 | -29 | -33 | -33 | -33 |
| Gross reserves accumulation (- increase) | 99 | -139 | 108 | -32 | -192 | -155 | -138 | -104 | -91 |
| Total Sources | 625 | 1072 | 593 | 826 | 814 | 845 | 860 | 871 | 916 |
| Expected disbursements (official) | 545 | 954 | 480 | 725 | 656 | 693 | 695 | 689 | 691 |
| Grants | 471 | 850 | 357 | 625 | 539 | 582 | 587 | 589 | 591 |
| Medium- and long-term loans | 73 | 104 | 123 | 100 | 116 | 111 | 107 | 100 | 100 |
| Private sector (net) | -5 | 97 | 113 | 64 | 106 | 137 | 172 | 209 | 249 |
| IMF | 86 | 21 | 0 | 37 | 52 | 14 | -7 | -28 | -24 |
| Drawings | 0 | 21 | 0 | 40 | 60 | 40 | 20 | 0 | 0 |
| Repayments | 0 | 0 | 0 | 4 | 8 | 26 | 27 | 28 | 24 |
| SDR allocation | 86 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Gross international reserves | 141 | 280 | 190 | 215 | 403 | 547 | 678 | 781 | 872 |
| Months of imports | 0.7 | 1.5 | 1.0 | 1.1 | 1.9 | 2.4 | 2.8 | 3.0 | 3.1 |

Source: IMF staff estimates.

**Table 6. Malawi: Proposed Schedule of Disbursements Under ECF Arrangement, 2012–15**

(Amounts are in millions of SDR)

| Amount | % of Quota | Date available | Conditions Necessary for Disbursement | Status |
|---|---|---|---|---|
| 13.02 | 18.75 | July 23, 2012 | Executive Board Approval of Three Year ECF arrangement. | Disbursed |
| 13.02 | 18.75 | December 15, 2012 | Observance of performance criteria for September 30, 2012 and completion of first review. | |
| 13.01 | 18.75 | March 15, 2013 | Observance of performance criteria for December 31, 2012 and completion of second review. | |
| 13.01 | 18.75 | June 15, 2013 | Observance of performance criteria for March 31, 2013 and completion of third review. | |
| 13.01 | 18.75 | December 15, 2013 | Observance of performance criteria for September 30, 2013 and completion of fourth review. | |
| 13.01 | 18.75 | June 15, 2014 | Observance of performance criteria for March 31, 2014 and completion of fifth review. | |
| 13.01 | 18.75 | December 15, 2014 | Observance of performance criteria for September 30, 2014 and completion of sixth review. | |
| 13.01 | 18.75 | June 15, 2015 | Observance of performance criteria for March 31, 2015 and completion of seventh review. | |
| 104.10 | 150.00 | Total for the ECF arrangement | | |

Source: IMF staff estimates.

## Table 7. Malawi: Indicators of Capacity to Repay the Fund, 2012–22 [1]

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Projected Payments based on Existing Drawings: | | | | | | | | | | | |
| (SDR millions) | | | | | | | | | | | |
| Principal | 1.7 | 5.4 | 16.7 | 17.4 | 17.9 | 15.7 | 16.5 | 5.4 | 4.7 | 2.6 | 2.6 |
| Charges and interest | 0.1 | 0.1 | 0.3 | 0.2 | 0.2 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.0 |
| Projected Payments based on Existing and Prospective Drawings: | | | | | | | | | | | |
| (SDR millions) | | | | | | | | | | | |
| Principal | 1.7 | 5.4 | 16.7 | 17.4 | 17.9 | 15.7 | 21.7 | 17.1 | 21.6 | 20.8 | 20.8 |
| Charges and interest | 0.1 | 0.1 | 0.4 | 0.4 | 0.4 | 0.4 | 0.3 | 0.3 | 0.2 | 0.2 | 0.1 |
| Total Payments based on Existing and Prospective Drawings: | | | | | | | | | | | |
| SDR millions | 1.7 | 5.5 | 17.1 | 17.8 | 18.3 | 16.1 | 22.0 | 17.4 | 21.8 | 21.0 | 20.9 |
| US$ Millions | 2.7 | 8.5 | 26.4 | 27.5 | 28.2 | 24.8 | 34.0 | 26.8 | 33.7 | 32.4 | 32.3 |
| Percent of exports of goods and services | 0.2 | 0.5 | 1.5 | 1.5 | 1.4 | 1.1 | 1.5 | 1.1 | 1.2 | 1.1 | 1.0 |
| Percent of debt service | 14.3 | 36.5 | 91.5 | 83.6 | 85.8 | 75.5 | 103.5 | 81.6 | 102.5 | 98.6 | 98.4 |
| Percent of quota | 2.5 | 7.9 | 24.6 | 25.6 | 26.3 | 23.2 | 31.7 | 25.0 | 31.5 | 30.3 | 30.2 |
| Percent of gross official reserves | 1.2 | 2.1 | 4.8 | 4.1 | 3.6 | 2.8 | 3.7 | 2.9 | 3.9 | 3.6 | 3.6 |
| Projected Level of Credit Outstanding based on Existing and Prospective Drawings: | | | | | | | | | | | |
| SDR millions | 117.7 | 151.4 | 160.8 | 156.4 | 138.6 | 122.9 | 101.2 | 84.1 | 62.5 | 41.6 | 20.8 |
| US$ Millions | 181.7 | 233.7 | 248.1 | 241.4 | 213.9 | 189.6 | 156.1 | 129.7 | 96.4 | 64.3 | 32.1 |
| Percent of exports of goods and services | 13.4 | 14.6 | 14.4 | 13.0 | 10.6 | 8.7 | 6.7 | 5.2 | 3.6 | 2.2 | 1.0 |
| Percent of debt service | 980.7 | 1004.1 | 861.4 | 734.8 | 650.9 | 577.1 | 475.2 | 394.9 | 293.4 | 195.6 | 97.8 |
| Percent of quota | 169.7 | 218.2 | 231.6 | 225.4 | 199.7 | 177.0 | 145.7 | 121.1 | 90.0 | 60.0 | 30.0 |
| Percent of gross official reserves | 84.6 | 57.9 | 45.3 | 35.6 | 27.4 | 21.7 | 16.8 | 14.0 | 11.2 | 7.1 | 3.6 |
| *Memorandum items:* | | | | | | | | | | | |
| Exports of goods and services (US$ millions) | 1357.5 | 1603.6 | 1725.5 | 1861.3 | 2008.1 | 2169.4 | 2337.4 | 2516.8 | 2714.6 | 2933.0 | 3173.4 |
| Debt service (US$ millions) | 18.5 | 23.3 | 28.8 | 32.9 | 32.9 | 32.9 | 32.9 | 32.9 | 32.9 | 32.9 | 32.9 |
| Quota (SDR millions) | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 | 69.4 |
| Gross official reserves (millions of U.S. dollars) | 214.7 | 403.3 | 547.1 | 677.7 | 781.4 | 872.1 | 929.4 | 928.3 | 863.4 | 907.0 | 889.6 |
| GDP (US$ millions) | 4236.3 | 3750.6 | 4082.8 | 4446.5 | 4823.4 | 5214.1 | 5718.6 | 6678.1 | 7612.9 | 8612.8 | 9740.7 |

Sources: Malawi authorities; and IMF staff estimates and projections

## Table 8a. Malawi: Quantitative Targets (September 2012)[1]

| | Criteria [2] | End-Mar 2012 Stock Act. | End-June. 2012 Stock Proj. | 2012 Stock Act. | Sept. 2012 Prog. | Sept. 2012 Act. | Status |
|---|---|---|---|---|---|---|---|
| **I. Monetary targets (millions of kwacha)** | | | | | | | |
| 1. Ceiling on net domestic assets of the RBM [3,4, 5, 6] | PC | 116,861 | 114,579 | 142,513 | 109,417 | 117,737 | NM |
| 2. Ceiling on reserve money[3] | IT | 89,168 | 76,178 | 101,398 | 88,210 | 95,657 | NM |
| **II. Fiscal targets (millions of kwacha)** | | | | | | | |
| 3. Ceiling on central government's net domestic borrowing [5,6,7] | PC | 176,588 | 178,847 | 188,853 | -11,988 | -41,220 | M |
| 4. Floor on social spending [8] | IT | | | | 39,034 | 27,959 | NM |
| **III. External sector targets (US$ millions, unless otherwise indicated)** | | | | | | | |
| 5. Floor on net international reserves of the RBM[3, 5, 6,9] | PC | -20 | -63 | -74 | 17 | 17 | M |
| 6. Ceiling on the accumulation of external payments arrears [7,10] | PC | | | | 0 | 0 | M |
| 8. Ceiling on new nonconcessional external debt maturing in more than one year [7,10] | PC | | | | 0 | 0 | M |
| 9. Ceiling on new nonconcessional external debt maturing in one year or less [7,10] | PC | | | | 0 | 0 | M |
| 10. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [10,11] | PC | | | | | | M |
| *Memorandum items:* | | | | | | | |
| Net foreign assets of the RBM (US$ millions) | | -107 | -148 | -158 | -82 | -85 | |
| Budget support (US$ millions) | | | | | 86 | 89 | |
| Budget support (millions of kwacha) | | | | | 21,945 | 23,210 | |
| Debt service payments to the World Bank and African Development Bank (millions of kwacha) | | | | | | | |
| Health SWAp receipts (millions of kwacha) | | | | | 5,248 | 7,732 | |
| Education SWAp receipts (millions of kwacha) | | | | | 8,378 | 7,227 | |
| NAC receipts (millions of kwacha) | | | | | 4,777 | 1,538 | |
| Program exchange rate (kwacha per US$) | | 260 | 260 | 260 | 260 | 260 | |

Sources: Reserve Bank of Malawi; Malawi Ministry of Finance; and IMF staff estimates.

1 Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.
2 "PC" means Performance Criterion, and "IT" means Indicative Target.
3 Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).
4 Target is subject to an adjuster for liquidity reserve requirement.
5 Targets are subject to an adjuster for budget support and debt service payments.
6 Targets are subject to an adjuster for donor-funded social sector expenditures consistent with the TMU.
7 Defined as a cumulative flow.
8 Priority social spending as defined in the TMU and quantified in the authorities' budget.
9 Adjusted for Letters of credit with cash cover as at end-March and end-June.
10 Evaluated on a continuous basis.
11 Other standard PCs include introducing or modfying MCPs, concluding bilateral payments agreements that are inconsistent with Article VIII, and imposing or intensifying import restrictions for balance of payment reasons.

## Table 8b. Malawi: Quantitative Targets (December 2012–September 2013)[1]

| | Criteria [2] | End-Sept. 2012 | End-Dec. 2012 | | End-Mar. 2013 | | Indicative End-Jun. 2013 | | End-Sept. 2013 |
|---|---|---|---|---|---|---|---|---|---|
| | | Act. | Prog. | Rev. Prog. | Prog. | Rev. Prog. | Prog. | Rev. Prog. | Prog. |
| **I. Monetary targets (millions of kwacha)** | | | | | | | | | |
| 1. Ceiling on net domestic assets of the RBM [3,4, 5, 6] | PC | 117,737 | 118,542 | 118,293 | 106,256 | 132,082 | 100,930 | 114,444 | 94,132 |
| 2. Ceiling on reserve money[3] | IT | 95,657 | 97,809 | 96,615 | 99,120 | 99,095 | 105,830 | 107,845 | 111,830 |
| **II. Fiscal targets (millions of kwacha)** | | | | | | | | | |
| 3. Ceiling on central government's net domestic borrowing [5,6,7] | PC | -41,220 | 18,500 | -17,756 | 11,609 | 4,444 | 0 | -15,021 | -5,218 |
| 4. Floor on social spending [8] | IT | 27,959 | 94,044 | 95,156 | 121,798 | 144,922 | 151,899 | 185,511 | |
| **III. External sector targets (US$ millions, unless otherwise indicated)** | | | | | | | | | |
| 5. Floor on net international reserves of the RBM[3, 5, 6] | PC | 17 | 19 | 32 | 71 | -3 | 118 | 79 | 155 |
| 6. Ceiling on the accumulation of external payments arrears [7,9] | PC | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 8. Ceiling on new nonconcessional external debt maturing in more than one year [7,9] | PC | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 9. Ceiling on new nonconcessional external debt maturing in one year or less [7,9] | PC | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 10. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [9,10] | PC | | | | | | | | |
| *Memorandum items:* | | | | | | | | | |
| Net foreign assets of the RBM (US$ millions) | | -85 | -80 | -68 | -27 | -103 | 19 | -21 | 55 |
| Budget support (US$ millions) | | 89 | 86 | 170 | 151 | 176 | 208 | 234 | 49 |
| Budget support (millions of kwacha) | | 23,210 | 21,945 | 49,038 | 38,926 | 54,934 | 53,864 | 73,542 | 15,752 |
| Debt service payments to the World Bank and the African Development Bank (US$ millions) | | 0 | | 2 | | 1 | | 3 | 7 |
| Debt service payments to the World Bank and African Development Bank (millions of kwacha) | | 0 | | 684 | | 420 | | 827 | 2,174 |
| Health SWAp receipts (millions of kwacha) | | 7,732 | 5,364 | 7,876 | 7,771 | 10,778 | 7,771 | 11,173 | 3,224 |
| Education SWAp receipts (millions of kwacha) | | 7,227 | 13,221 | 9,614 | 17,073 | 14,994 | 19,049 | 18,194 | 4,800 |
| NAC receipts (millions of kwacha) | | 1,538 | 7,315 | 5,101 | 10,019 | 8,719 | 12,220 | 12,281 | 3,563 |
| Program exchange rate (kwacha per US$) | | 260 | 260 | 320 | 260 | 320 | 260 | 320 | 320 |

Sources: Reserve Bank of Malawi; Malawi Ministry of Finance; and IMF staff estimates.

1 Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.

2 "PC" means Performance Criterion, and "IT" means Indicative Target.

3 Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).

4 Target is subject to an adjuster for liquidity reserve requirement.

5 Targets are subject to an adjuster for budget support and debt service payments.

6 Targets are subject to an adjuster for donor-funded social sector expenditures consistent with the TMU.

7 Defined as a cumulative flow.

8 Priority social spending as defined in the TMU and quantified in the authorities' budget.

9 Evaluated on a continuous basis.

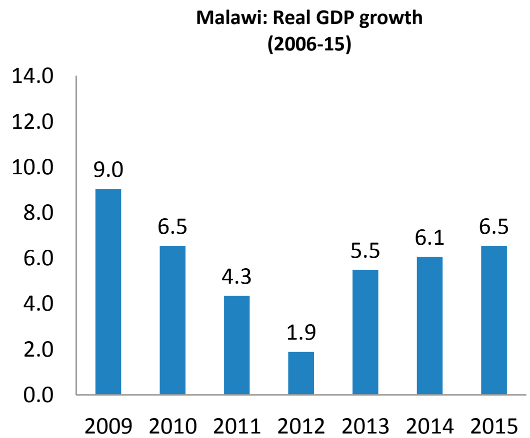
10 Other standard PCs include introducing or modfying MCPs, concluding bilateral payments agreements that are inconsistent with Article VIII, and imposing or intensifying import restrictions for balance of payment reasons.

**Table 9. Malawi: Structural Benchmarks, 2012–13**

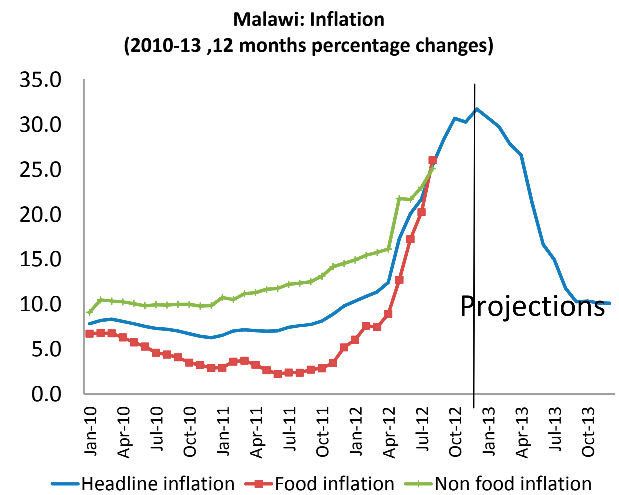
| Measure | Status/Target Date | Macro Rationale | Status |
|---|---|---|---|
| **Prior Actions** | | | |
| ***Approval of the arrangement*** | | | |
| Parliamentary passage of a budget for FY 2012/13 in line with program objectives | | Toward fiscal sustainability | Met |
| ***First review*** | | | |
| Shut down RBM's uncollateralized lending to banks | | | |
| **Structural benchmarks** | | | |
| **Fiscal transparency** | | | |
| Publish monthly revenue collections of the Malawi Revenue Authority in newspapers within two weeks of the end of the month. | 7/31/2012 | Build credibility after recent incidents of inflation of revenue data by the Ministry of Finance. | Met |
| **Public financial management** | | | |
| Provide Ministries, Departments and Agencies with quarterly spending ceilings consistent with quarterly fiscal targets in the program, and enforce ceilings. | Begin in Sept 2012 for FY2012/13 Q2 and quarterly thereafter | Keep spending within available resource envelope. | Met for Q2 |
| Verify existing stock of government domestic arrears and formulate a plan for settling verified claims. | 31-Dec-12 | Ascertain magnitude of government obligations. | |
| Configure the IFMIS Purchase Order (PO) module to support commitment control. | 31-Dec-12 | To restrain creation of arrears. | |
| Progressively extend processes for capturing donor funded project transactions in IFMIS to all projects where bank accounts are controlled by the government of Malawi. | 31-Mar-13 | Fuller accounting for impact of aid flows on the budget. | |
| **Monetary Policy** | | | |
| Amend RBM Act to limit the outstanding amount of RBM's total lending to government. | 30-Jun-13 | Reduce fiscal dominance to enhance effectiveness of monetary policy. | |
| **Financial sector** | | | |
| RBM to publish a financial stability report on a semi-annual basis, with a lag of no more than four months. Start with publication of report for quarter ending March 2012. | Semi-annual, starting in July 2012. | Promote financial stability. | Met |
| Obtain approval and begin implementation of the Financial Sector Development Strategy | 31-Dec-12 | Financial deepening. | |

**Figure 1. Malawi: Real Sector Developments and Prospects , 2006-2015**

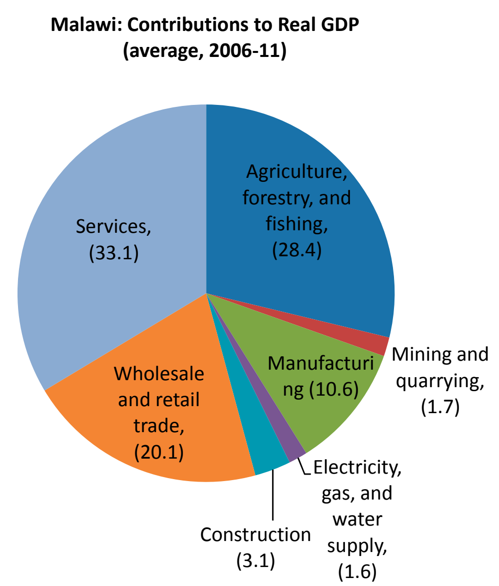
**Rebound in growth is expected in 2013 after the recent steady decline**



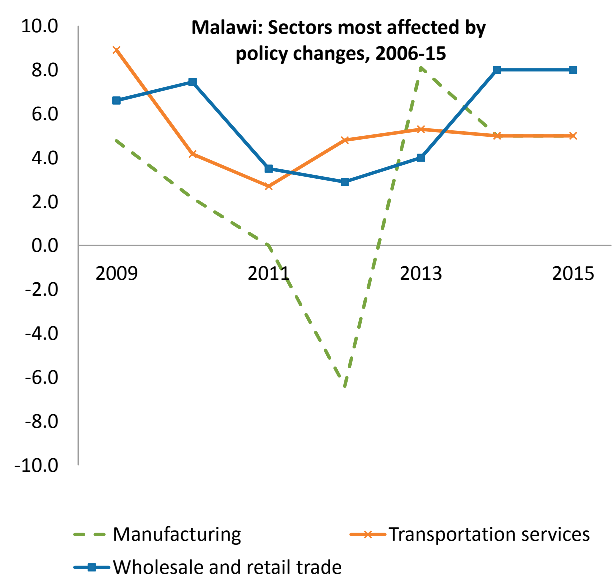

**Spike in inflation reflects the devaluation and rising domestic food prices.**




**Agriculture is the mainstay of the economy**



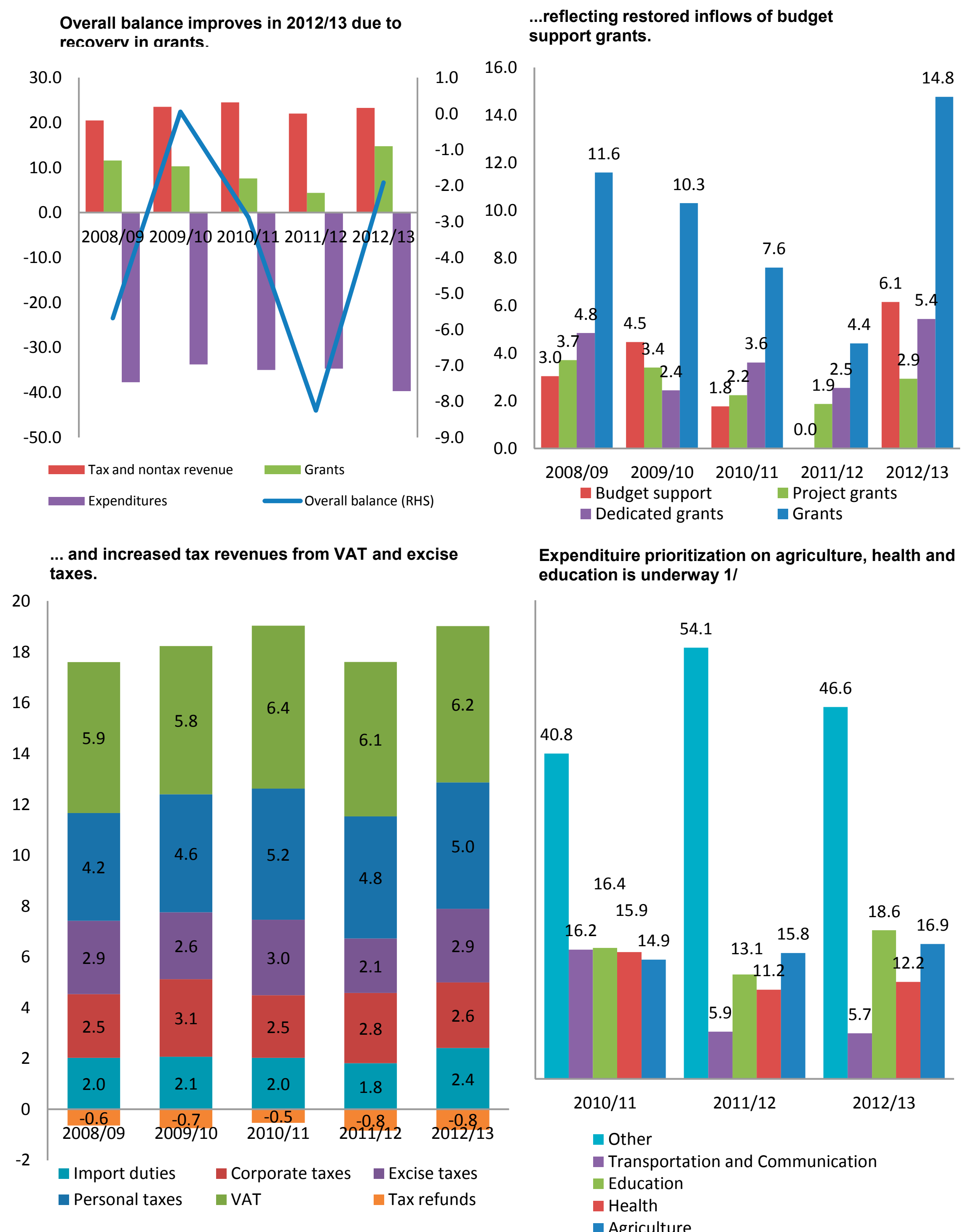

**Manufacturing, trade and transportation services are projected to recover after recent sharp declines.**




Sources: Malawian authorities; and IMF staff estimates.

**Figure 2. Malawi: Fiscal Developments, 2007/08–2012/13**

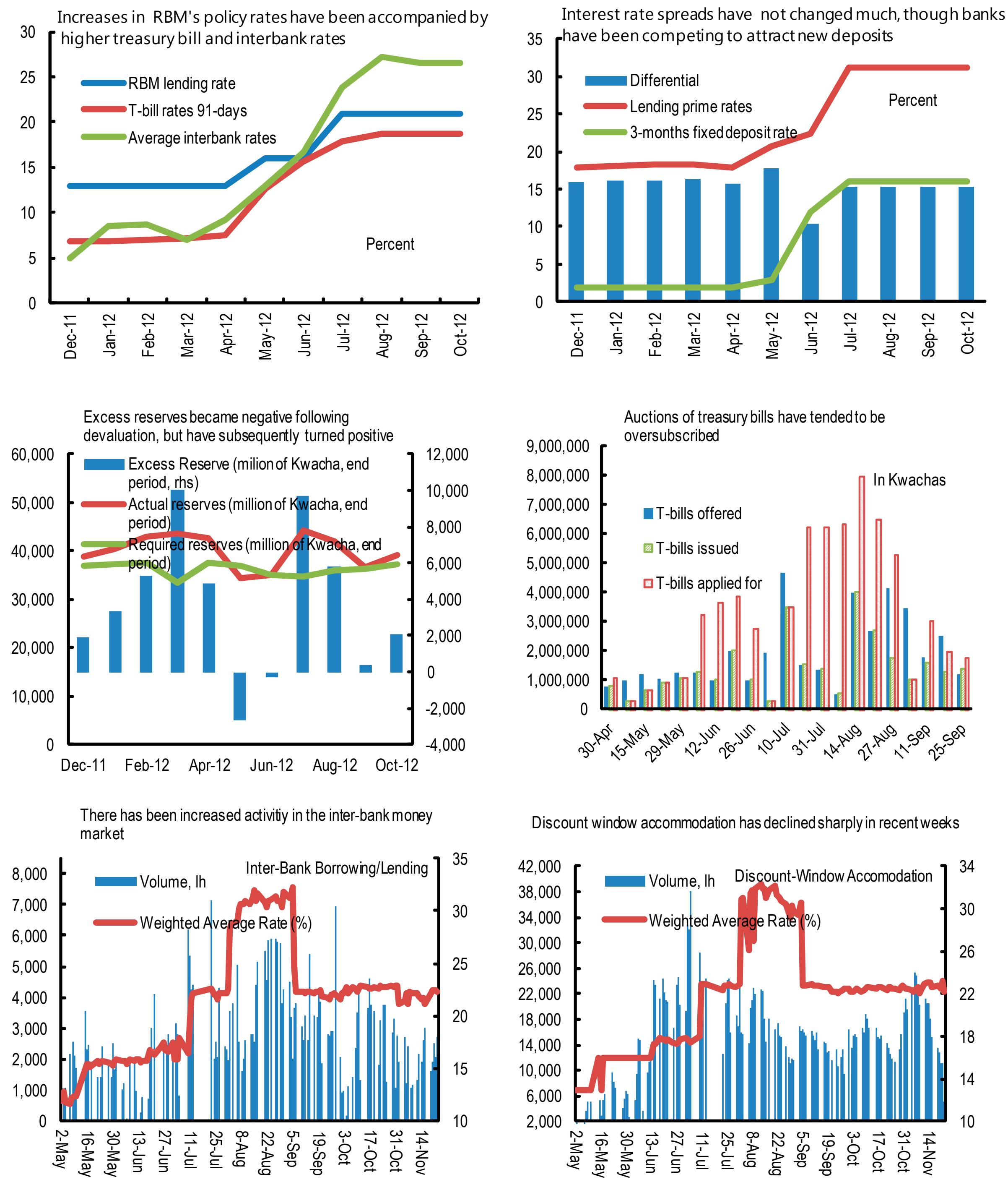
(Percent of GDP)




Sources: Malawian authorities; and IMF staff estimates.

1/ Percent of total expenditures

**Figure 3a. Malawi: Interest Rates and Liquidity Developments**




Source: Malawi authorities and IMF staff calculations.

**Figure 3b. Malawi: Monetary Developments, 2010-15**

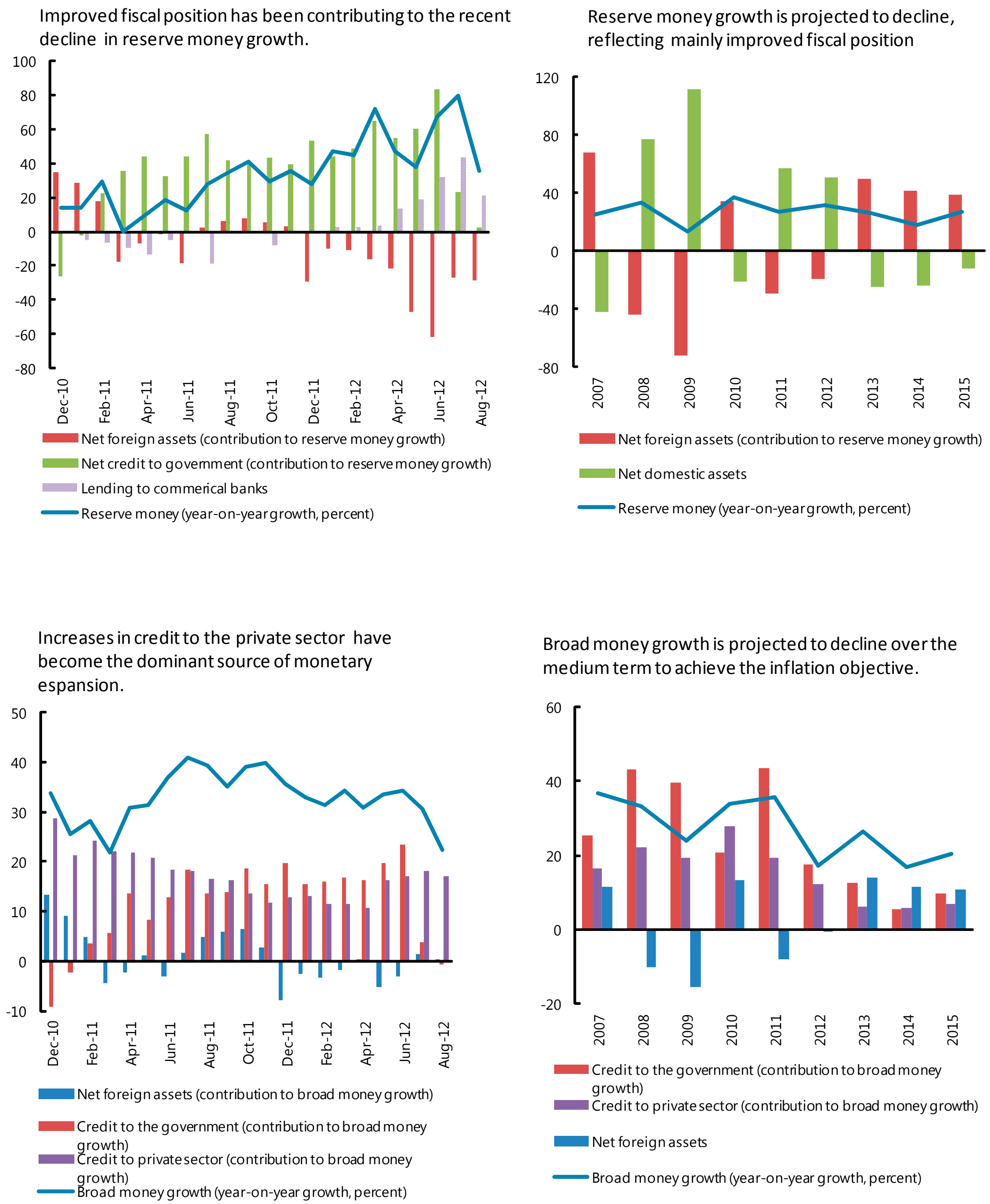
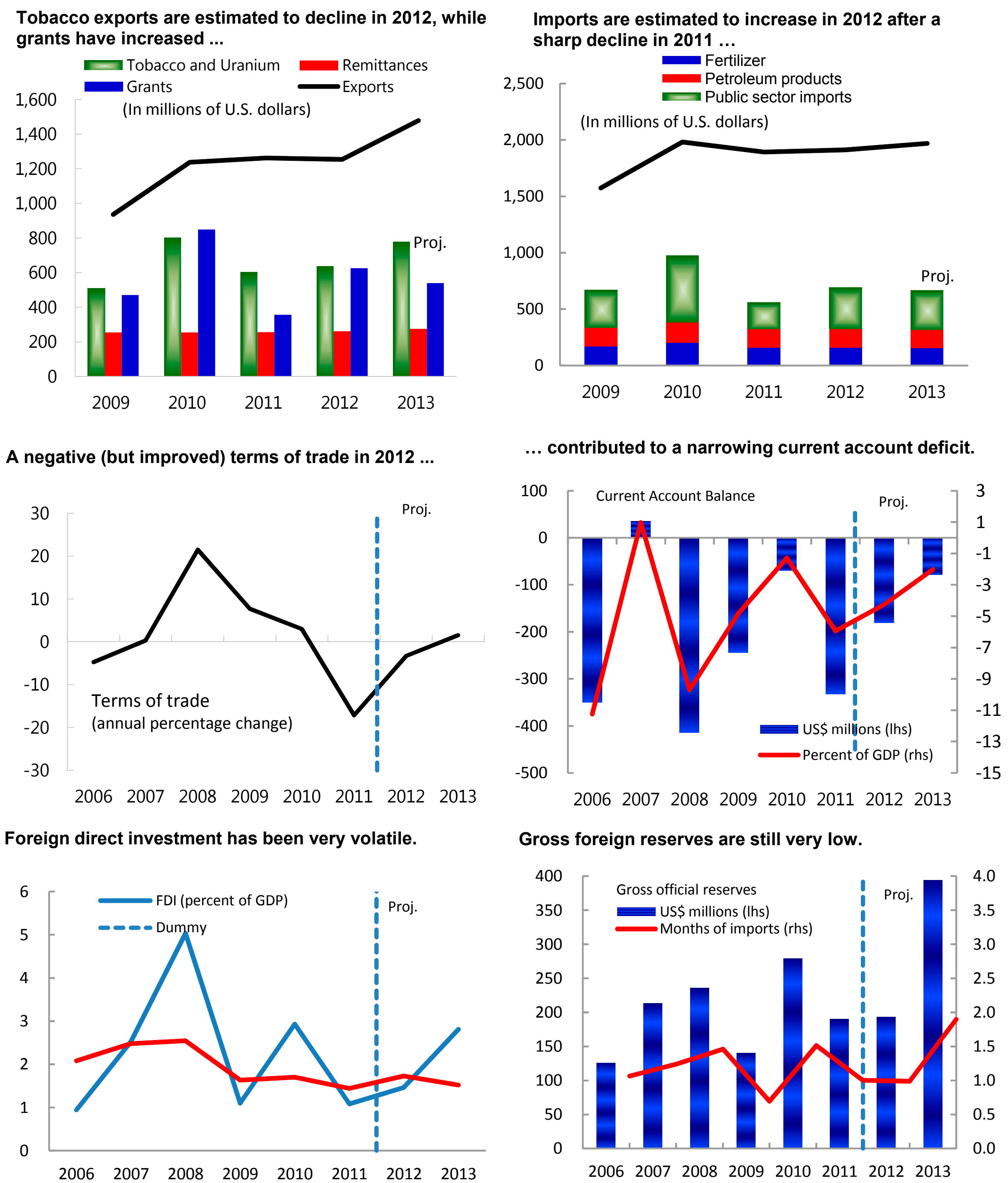


**Figure 4. Malawi: External Sector Developments**




Sources: Malawian authorities; and IMF staff estimates.

## APPENDIX I. LETTER OF INTENT

December 5, 2012

Madam Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431
USA

Dear Madam Lagarde:

On July 23, 2012, the Executive Board of the International Monetary Fund (IMF) approved Malawi's request for a new three year arrangement under the Extended Credit Facility (ECF) in the amount of SDR 104.1 million (150 percent of quota). The arrangement covers Malawi's fiscal years 2012/13 through 2014/15. This letter and the attached Memorandum of Economic and Financial Policies (MEFP) report on recent economic developments, performance under our ECF-supported program, and policies for the rest of FY2012/13 and over the medium term.

The overarching goal of our program remains to reduce poverty in Malawi through sustainable growth and wealth creation. In this connection, the program focuses on achieving and maintaining macroeconomic stability, boosting real GDP growth, and scaling up social-protection programs to mitigate the adverse impact of adjustment measures on the poor. Structural reforms under the program emphasize enhancing domestic revenue mobilization, further improving public financial management, ensuring the operational independence of the Reserve Bank of Malawi (RBM), deepening the financial sector, and improving the investment climate.

The external environment has been more difficult than envisaged at the inception of the program. Lower-than-expected tobacco and sugar proceeds and higher foreign exchange requirements to clear the backlog of private sector external payments arrears put substantial pressure on the exchange rate. Also, the price of maize—the main staple food in the country—has increased considerably in the last few months, as drought conditions in parts of the country impacted negatively on output. It is estimated that nearly 2 million people (about 12 percent of the total population) face food deficits and need assistance in the period before the next harvest (March/April 2013).

Notwithstanding the challenges we faced, most of the quantitative targets for September were met, including those on net international reserves, government's net domestic borrowing, and the contracting of non concessional external borrowing. However, the performance criterion on the level of the RBM's net domestic assets was missed on account of the extension of liquidity support to the banking system in order to avert a payments system crisis. The indicative target on social spending was also not achieved due to delays in the procurement of fertilizers for the farm input subsidy program. All the structural benchmarks scheduled for implementation by end-September were met, and we are on course to meet all those due to be implemented by end-December.

We request a waiver for the nonobservance of the end-September 2012 NDA target, based on corrective measures that we are implementing (MEFP paragraphs 17 and 24). The level of liquidity support to the banks has fallen substantially and the RBM is exercising increased oversight of a few banks that continue to have difficulty meeting prudential liquidity requirements. On the basis of our overall performance, and on the strength of policies set forth in the attached MEFP, we request that the Executive Board of the IMF complete the first review under the ECF arrangement and release the second tranche of SDR 13.02 million (18.75 percent of quota). We also request the modification of the performance criteria for end-December 2012 and end-March 2013, to reflect the updated macroeconomic framework presented in the MEFP, and the establishment of performance criteria for end-September 2013.

We believe that the policies set forth in the MEFP are adequate to achieve the objectives of the program, but we will take any further measures that may become appropriate for this purpose. We will consult with IMF staff on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP, in accordance with the IMF policies on such consultation. Moreover, we will provide the IMF with such information as the IMF requests in connection with the progress in implementing the policies and reaching the objectives of the program.

The Government of Malawi authorizes the IMF to make this letter and the attached MEFP and TMU available to the public, including through the IMF internet website.

Yours sincerely,

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|---|---|
| /s/ | /s/ |
| Dr. Ken Lipenga (MP)<br>Minister of Finance | Mr. Charles Chuka<br>Governor of the Reserve Bank of Malawi |

Attachments:

– Memorandum on Economic and Financial Policies
– Technical Memorandum of Understanding.

## ATTACHMENT I. MALAWI: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICES, 2012/13–2014/15

### I. INTRODUCTION

1. This memorandum supplements the Memorandum of Economic and Financial Policies (MEFP) attached to our Letter of Intent dated July 9, 2012. It describes recent developments and performance under the ECF arrangement through September 2012, summarizes the Government's recently launched Economic Recovery Plan, and elaborates on policies and structural reforms for the rest of FY2012-13 and the medium term.

2. The main objectives of the program remain macroeconomic stability, sustained high and inclusive growth, and delivery of social-protection programs to mitigate the adverse impact of adjustment measures on the poor. Structural reforms under the program emphasize enhancing domestic revenue mobilization, strengthening public financial management, ensuring the operational independence of the Reserve Bank of Malawi (RBM), deepening the financial sector, and improving the investment climate.

3. The government has implemented strong adjustment measures. Shortly after her elevation to the presidency in April 2012, President Joyce Banda authorized the implementation of a set of bold measures to address long-standing internal and external imbalances in the economy. The key measures entailed: (i) a devaluation that increased the price of foreign exchange by about 50 percent and adoption of a floating exchange rate regime; (ii) removal of restrictions on foreign exchange transactions by banks and foreign exchange bureaus; (iii) relaxation of surrender requirements on export proceeds, allowing them to flow to commercial banks instead of mainly to the RBM; and (iv) increases in the retail prices of petroleum products and adoption of an automatic adjustment mechanism to keep prices in line with import costs. Concurrently, the RBM tightened monetary policy by raising its policy rate and through sales of foreign exchange.

4. The reforms elicited positive responses initially. Increased availability of foreign exchange from private sources eased the shortage of key items such as fuel, and the parallel market for foreign exchange virtually disappeared. Malawi's development partners pledged increased financial assistance, especially in the form of budget support.

5. The external environment has become more difficult than envisaged at the inception of the program. Lower-than-expected tobacco and sugar proceeds and higher foreign exchange requirements to clear the backlog of private sector external payments arrears put substantial pressure on the exchange rate. Continued depreciation of the exchange rate and drought-induced increases in local food prices pushed inflation above its envisaged path. It is estimated that nearly 2 million people (about 12 percent of the total population) are at risk of famine in the period before the next harvest in March/April 2013.

6. The government has recently launched the Malawi Economic Recovery Plan (ERP) which seeks to sharpen priorities within the extensive set of programs and projects in the second Malawi Growth and Development Strategy (MGDS II). The ERP lays out action plans over the short- and medium-term to make rapid progress toward poverty reduction through economic growth and wealth creation. It identifies commercial agriculture, tourism, energy, mining, transport infrastructure, and information and communication technology as key sectors and activities that can lead growth and achieve quick development results.

7. The government is committed to achieving the Millennium Development Goals (MDGs) through the implementation of MGDS II which has been aligned with MDG outcomes. Four MDGs are likely to be met by 2015: (i) reduce child mortality; (ii) combat HIV and AIDS, malaria and other diseases; (iii) ensure environmental sustainability; and (iv) develop global partnership for development. The remaining four are unlikely to be met: (a) eradicate extreme poverty and hunger; (b) achieve universal primary education; (c) promote gender equality and empower women; and (d) improve maternal health. The recently published Integrated Household Survey (conducted in 2010/11) indicates that rapid growth during 2005–10 did not have an appreciable impact on rural poverty. The government will strengthen its efforts to promote more inclusive growth.

## II. Recent Economic Developments

8. Real GDP growth is now projected to fall from 4.3 percent in 2011 to 1.9 percent in 2012. The downward revision for 2012 (from 4.3 percent in the original program) is driven by contractions in the agriculture and manufacturing sectors. Maize production in 2012 is estimated at 3.6 million metric tons, a 7 percent drop from the level in 2011 but still higher than the estimated national requirement of 2.8 million metric tons. The decline is attributable to poor and erratic rainfall in the southern half of the country during the 2011/12 growing season. Tobacco production is estimated to have fallen from 237,000 metric tons in 2011 to only about 80,000 metric tons in 2012, reflecting low prices offered on the auction floors in 2011 and an overvalued exchange rate which served as a disincentive to tobacco growing last year. The manufacturing sector contracted by about 6 percent in 2012, largely due to scarcity of foreign exchange and fuel in the first half of the year. During the second half of the year, the pace of recovery has been slow due to both supply and demand side factors. Although the private sector has cleared most of its external payments arrears, external lines of credit have not yet been re-established as banks and suppliers have adopted a wait-and-see attitude, on concerns of possible policy reversals. On the demand side, there has been reduced uptake of products due to significantly lower disposable incomes associated with the depreciation of the exchange rate and rising inflation.

9. Inflation has accelerated in the aftermath of the devaluation and contraction in domestic food production. On a year-on-year basis, headline consumer inflation increased from 12.4 percent in April to 28.3 percent in September, with both the food and non-food

components of the CPI rising sharply. The non-food CPI has a large import content and as a result, its evolution is influenced strongly by exchange rate movements. In mid-November, the price of foreign exchange had increased by an additional 30 percent since the May devaluation. Factors that have contributed to this marked depreciation of the exchange rate include: the clearance of private sector external payments arrears (estimated at about US$500 million), perceptions in the market of continued scarcity of foreign exchange based on the low level of official international reserves, and weak performance of foreign currency-generating products (tobacco and sugar).

10. Year on year growth in reserve money fluctuated between 38 percent and 72 percent in the first half of 2012, driven by credit to government. After peaking at 80 percent in July the growth rate decelerated sharply to 20 percent in September. Since July, RBM lending to banks has been the principal source of growth in reserve money. Broad money growth remained steady in the range of 31–34 percent a year between January and July 2012 before falling to 20 percent in September. Credit to the government and to the private sector were the principal sources of growth in broad money in the first half of the year. Subsequently, the government reduced its net borrowing, and lending to the private sector has become the principal source of broad money growth.

11. The RBM increased the bank rate from 13 percent to 16 percent in April and to 21 percent in July. Banks responded by increasing both their deposit and lending rates, with prime lending rates increasing from about 18 percent to about 30 percent and the rate on 3-month fixed deposits rising from the 2–6 percent range to about 16 percent. There has also been increased activity on the inter-bank market, reflecting improved liquidity in a number of banks that have become providers of liquidity to some banks.

12. Fiscal performance in FY2011/12 was weaker than envisaged in the last MEFP. The overall deficit was 1.5 percent of GDP larger than projected, driven by lower grants and higher expenditures. Domestic interest payments and development expenditures accounted for the higher level of expenditures. The larger deficit was financed mainly by domestic borrowing. In the first quarter of FY2012/13, fiscal performance was in line with the program.

13. Low production of Malawi's main export, tobacco, translated into significantly lower sales volumes on the auction floors in 2012 compared to 2011. The volume of sales fell to one third of the level in 2011 and only half of what was projected at the beginning of the season. The value of sales fell by 40 percent (from US$294 million to US$178 million), reflecting higher unit prices paid to farmers. Thus, the supply of foreign exchange to the local foreign exchange market declined sharply. Exports of tobacco, however, remained comparable to the level achieved in 2011 due to large stocks of inventories. Sugar exports also declined as a result of drought in central and southern parts of the country. The import bill increased in 2012 due to higher international fuel prices, as well as increased volumes of

fertilizer imports in response to positive price incentives for tobacco production (reflecting the change in exchange rate policy). The import coverage of international reserves has improved slightly from exceptionally low levels in the first half of 2012 due to increased donor assistance to Malawi.

## III. Performance Under the Program

14. Most of the quantitative targets for end-September 2012 were met (Table A1). In particular, the target on government net domestic borrowing was met comfortably. The targets on net international reserves and on external borrowing were also met. The performance criterion on the level of the RBM's net domestic assets and the indicative target on reserve money were missed on account of the extension of liquidity support to the banking system in order to avert a payments system crisis. With respect to the indicative target on priority spending, the government fell short by about MK11 billion, emanating largely from delays in awarding contracts for the procurement of fertilizers for the Farm Input Subsidy Program (FISP). The government made changes to the procurement process with the aim of ensuring increased value for money. The rolling out of other social protection programs (e.g., public works and cash transfer programs) started in the second quarter of FY 2012/13 (October–December) and as a result, we expect increased social spending in this quarter to make up for the shortfall in the first quarter. External grants were broadly in line with programmed levels for the first quarter.

15. All the structural benchmarks scheduled for implementation by end-September were met (Table A2). The Malawi Revenue Authority (MRA) began publishing its monthly revenue collections in newspapers in July, and the RBM posted the financial stability report for March 2012 on its website in August. The Ministry of Finance established quarterly spending ceilings for the first and second quarters. We are on course to meet all the structural benchmarks scheduled for implementation by end-December 2012.

16. Among the set of bold measures implemented by the new administration was a substantial increase in fuel prices to bring them in line with the actual import cost and the restoration of an automatic pricing mechanism to ensure pass through of world prices of fuel. In line with this decision the pump price has been adjusted since July 2012. While there was some delays in adjustment of the pump price in October, the recent adjustment in pump price in November reflected world fuel price developments since the last domestic pump price adjustment.

17. The banking system experienced tight liquidity conditions soon after the May devaluation. Initially, almost all banks resorted to the RBM discount window to meet their liquidity needs. In part, the tight liquidity situation reflected RBM withdrawal of liquidity from the system through foreign exchange sales to the market (a monthly average of US$55 million during May-July). As signs of the liquidity squeeze intensified—e.g., as

evidenced by banks having difficulty settling interbank transactions—the RBM provided liquidity to the banks, including through uncollateralized lending at a premium over the bank rate, in order to avert a crisis. The increased lending to banks was the principal factor behind the non-observance of the end-September NDA performance criterion. In order to bring down NDA, the RBM closed the uncollateralized lending window on [November 30] and has also undertaken open market operations to withdraw liquidity as part of the effort to stabilize the exchange rate. It has also stepped up its monitoring of the frequency of recourse to its discount window by individual banks.

## IV. Medium-term Framework

18. The main changes to the medium-term macroeconomic framework compared to the MEFP that accompanied Malawi's ECF request are:

- Significantly slower growth in 2012, reflecting the estimated contraction in agricultural output and slower-than-expected pace of recovery in other sectors. A strong rebound in growth is envisaged, beginning in 2013, based on the assumption of a return to normal rainfall patterns and improved access to foreign exchange, and taking into account improved price incentives for tobacco production.

- Upward shift in the inflation path for 2012 and the first half of 2013, reflecting recent significant depreciation of the exchange rate and sharp increases in prices of domestically produced food (especially maize). Inflation is projected to decelerate rapidly during the next harvest season (2013 Q2) in response to increased supply of food and the lagged effect of tighter monetary and fiscal policies.

- Little change in external debt and total public debt indicators. In particular, projected external debt service remains low at less than 5 percent of exports for the foreseeable future.

## V. Policies

19. The most pressing challenge facing the government and the RBM is stabilization of the exchange rate in order to avoid a depreciation-inflation spiral. Given the current circumstances—low international reserves and the onset of the lean season for foreign exchange inflows—a tightening of both monetary and fiscal policies is called for.

### A. Exchange Rate Policy

20. We remain committed to a flexible exchange rate regime to allow the kwacha to adjust to domestic and international developments. The main objective of our exchange rate policy is to contribute to enhancing Malawi's external competitiveness. The RBM determines the official exchange rate at the beginning of each business day as a weighted average of rates established by commercial banks the previous day. The RBM will continue to make the

case for a flexible regime to the public, emphasizing that, given the very low level of international reserves, a return to a fixed exchange rate regime will come with a high risk of a quick return to an overvalued exchange rate and the associated problems of foreign exchange shortages that plagued the country in the last few years. The RBM will intervene in the foreign exchange market mainly to ensure orderly market conditions, and will continue to build up its international reserves in order to provide the economy with a buffer against exogenous shocks.

## B. Monetary Policy and Financial Sector Issues

21. The main objective of monetary policy is the achievement of stable low inflation. Other objectives include contributing to a sustainable balance of payments position and to economic growth. The RBM has a liquidity forecasting framework which it uses to guide its monetary operations. The RBM will continue to develop its instruments of indirect monetary control and strengthen its ability to implement monetary policy through changes in interest rates, underpinned by open market operations. The use of treasury bills for monetary operations will be formalized in a Memorandum of Understanding (MOU) between the RBM and the Ministry of Finance by end-December 2012. The MOU will indicate clearly that the Ministry of Finance will be responsible for meeting the interest costs of treasury bills used for monetary operations.

22. In order to contain rising inflation pressures, the RBM has tightened monetary policy by winding down its uncollateralized lending to banks and will stand ready to implement further measures using all instruments available to it to stabilize the exchange rate and contain second round effects of increased fuel prices and utility tariffs. The RBM intends to pursue a more proactive communications strategy toward financial markets and the general public to aid stakeholders better understand its monetary policy actions.

23. Before the devaluation, the banking system was flush with liquidity, a significant portion of which reflected the lack of foreign exchange to meet customers' foreign payments obligations. As part of a financial inclusion drive, some banks embarked on expansion drives to reach a wider customer base. A number of banks used the available liquidity to extend long-term loans and were unable to unwind their long positions quickly when foreign exchange availability improved after the devaluation and customers sought to pay down their external arrears. In order to provide relief to the hardest hit banks and to avoid failure of the payment system and associated adverse impacts on the economy, the RBM introduced a window for providing short term uncollateralized loans to banks that had run out of securities for borrowing through the regular discount window at rates that were initially significantly higher than the policy rate. Safeguarding the payment system and sustaining financial inclusion was the main rationale for RBM support to a couple of banks which have more branches and agencies than the other banks. Most banks have adjusted their balance sheets to the new conditions, though a few continue to have difficulties.

24. Banks have initiated a number of actions to address the liquidity problems they faced after the devaluation. These include deposit mobilization campaigns, curtailment or outright freezing of new loans, recalling overdue loans, securitization of loans, sale of securities, injection of fresh capital, and suspension of expansion drives. The RBM is conducting in-depth assessments of banks that have continued for a long time to rely heavily on borrowing from the RBM or the interbank market to meet liquid reserve requirements. The RBM will enforce its prudential regulations, and if warranted, require the banks to submit time-bound restructuring plans. Restructuring is likely to include securitization of some assets, curtailing the levels of lending and putting on hold expansion plans.

25. Notwithstanding the challenges being faced by some banks, financial stability indicators suggest that the banking sector in Malawi remains sound. Non-performing loans are at low levels—their share as a ratio of total loans was 6.4 percent as at end-September 2012. However, the deterioration in the macroeconomic environment in the last two years and the slow pace of recovery have elevated the risks to banks' portfolios. The RBM has intensified its monitoring and surveillance of the financial system with a view to detecting at an early stage emerging threats to financial stability.

26. The RBM is undertaking a review of the RBM Act with a view to recommending amendments to modernize it. In order to enhance the operational independence of RBM, the government agrees to include an amendment to limit the outstanding amount of the government's total borrowing of all kinds from the RBM. Currently, the RBM Act limits the amount of advances to the government but has no limits on other forms of RBM lending to the government (e.g., through holdings of treasury bills). In line with the recommendations of the recent Safeguards Assessment, the review of the Act will also cover amendments to strengthen RBM's governance structure and its legal and financial autonomy. Proposed amendments will be ready for discussion with government in December 2012, and for submission to parliament by the government by June 2013.

## C. Fiscal Policy

27. The difficult macroeconomic environment characterized by high inflation and continuing depreciation of the exchange rate has put the FY2012/13 budget under stress. In order to meet the increased need for resources to deliver reasonable levels of public services, the government has appealed to development partners to provide additional assistance over and above pledges reflected in the FY2012/13 budget. We now expect to receive about US$662 million in external grants this fiscal year (including US$234 million in budget support), compared to an estimate of US$598 million (of which US$208 in budget support) in the original budget. The additional resources will allow the government to increase expenditure in several critical areas, including social spending and goods and services to maintain basic functions of the government.

28. The government is acutely aware that sole reliance on monetary policy to stabilize the exchange rate and contain inflation may further slow down the recovery in the economy. Thus, fiscal policy needs to contribute to the effort, especially since loose fiscal policies in the last few years have left a legacy of huge domestic arrears that are a major factor in the liquidity problems of some banks. To that end, the government will aim to save some of the additional resources that have become available in order to support the objective of boosting international reserves from the current very low levels. The FY2012/13 budget will be revised to reflect a net buildup in government deposits (or “net repayment” to the banking system) equivalent to about ½ percent of GDP.

29. Revisions to the revenue outlook reflect expectations that corporate income tax collection is likely to fall short of budget estimate (because of slower-than-expected recovery in manufacturing and likely losses by banks), but increased collections from PAYE and VAT are expected to more than make up for the shortfall. On the expenditure side, the largest revisions were increases in the allocations to fertilizer purchases for FISP and goods and services, on account of the impact of the more depreciated exchange rate.

30. On behalf of the government, the World Food Program launched an appeal for US$60 million to undertake emergency operations to deliver food to nearly 2 million people who are food insecure because of drought in some parts of the country. At mid-November, about US$47.2 million had been raised, including government’s contribution of approximately 72,500 MT of maize valued at about US$16.4 million.

31. The government will continue its efforts to strengthen revenue administration and broaden the tax base. The government will enhance its enforcement mechanisms through increased audits and use of modern information and communication technology (ICT) systems to improve revenue collection. Tax revenues are expected to improve through the adoption and use of electronic fiscal devices in the enforcement of VAT and the use of computerized cargo scanners coupled with the implementation of web-based ASYCUDA System for Customs. At the request of the Malawi Revenue Authority (MRA), an IMF technical assistance mission recently visited Malawi to provide advice on a number of issues, including: (i) automating and managing taxpayer compliance to support a full self-assessment system; and (ii) developing and implementing best practice performance indicators for tax and customs administration.

32. In order to strengthen the commitment control and avoid the accumulation of arrears, the Commitment Module in IFMIS is now being piloted having passed Acceptance Testing and should be rolled out soon. In readiness for the roll-out, user training of relevant officers has already been done and a Press Statement to the general public on the procurement rules will be released. Under the Multi-Donor Funded Financial Reporting and Oversight Improvement Project (FROIP), we are also reviewing IFMIS accounting business processes and functional requirements through consultations. These processes should result in better utilization of IFMIS through improvement in financial procedures, as the system will be

reconfigured to allow financial transactions to be processed with very little manual intervention. Information sharing has improved. For instance, daily sharing on total amounts of cheques issued with RBM's Liquidity Management Committee Secretariat is being done. With respect to cash management, data that we have started gathering will improve the forecasting of deficit financing and inform short-term borrowing requirements, allowing us to move away from automatic resort to Ways and Means Advances.

33. The government has initiated steps to reduce the risks to the budget posed by contingent liabilities and operational losses of state-owned enterprises. The contingent liabilities are mainly loans from banks and payment arrears while the operational losses arise from administratively set prices and tariffs that are below cost-recovery levels and generate substantial implicit and explicit subsidies. The government recognizes that the operations of the recently established National Oil Company of Malawi (NOCMA), including government-guaranteed loans for fuel imports, pose severe risks to the budget. For state-owned enterprises, risks are now being mitigated through the approval of realistic tariffs, and NOCMA's operations will be restricted to the management of strategic fuel reserves. The bulk of fuel importation for regular use will remain with the private sector.

34. Most of the MK72 billion stock of arrears indicated in the June MEFP have been verified and certified by National Audit Office. These arrears were accumulated over the last three years by government ministries and departments and parastatals (on behalf of government) to suppliers of goods and services and contractors undertaking construction projects. Several of the suppliers and contractors took out loans from banks which they have not been able to service because of nonpayment by the government. In order to assist the suppliers and contractors, as well as the banks, the government has issued them promissory notes worth MK [38] billion. The promissory notes will be redeemed over a period of four years starting from FY 2013/14.The reference rate for the notes is the 91 day treasury bill of the most recent auction immediately preceding interest payment. This transaction is being incorporated into the medium term fiscal framework.

### D. Business Climate and International Competitiveness

35. Although the recent liberalization of the exchange rate regime has addressed the issue of overvaluation of the kwacha—a key step towards enhancing Malawi's international competitiveness—the government recognizes that further steps are required, especially removal of structural bottlenecks—e.g., reliable and adequate supply of energy—that are holding back growth and diversification of the economy.

36. Malawi ranks low globally and behind its neighbours in indicators of the business environment. For example, it ranks 129$^{th}$ out of 144 countries in the 2012/13 Global Competitiveness Indices (GCI) of the World Economic Forum, and 155$^{th}$ out of 183 countries in the World Bank's 2013 Doing Business Report. Major challenges in doing business in Malawi cited by the private sector include: (i) lack of access to finance;

(ii) inadequate infrastructure; (iii) inefficient government bureaucracy; (iv) policy instability; (v) uncompetitive tax incentives and tax regime; and (vi) inadequate educated and skilled work force. The government is determined to address these competitiveness issues by removing regulatory hurdles in the areas of starting a business, obtaining permits, registering property, enforcing contracts and trading across borders. The Ministry of Industry and Trade has embarked on a program to create a pro-business environment in consultation with stakeholders in the private sector, civil society, and public sector.

37. The government has developed a National Export Strategy (NES) through a participatory process involving a broad range of stakeholders. The NES, which is expected to be launched in [date], supports the second Malawi Growth and Development Strategy (MGDS II) and the Economic Recovery Plan (ERP) by presenting a strategy to develop Malawi's capacity to export. The NES is a prioritised road map for developing Malawi's productive base to allow for both export competitiveness and economic empowerment. This strategy focuses on four main areas: (i) export-oriented clusters for diversification; (ii) conducive environment; (iii) supportive economic institutions to build the productive base of the economy; and (iv) competencies, skills and knowledge development. These components will be implemented through the NES' implementation mechanism, which is based on the Trade, Industry and Private Sector Development Sector Wide Approach. This SWAp will be largely funded by donors and contain seven technical working groups whose mandate will be to ensure the implementation.

## VI. INFORMATION SHARING, DATA QUALITY AND CAPACITY BUILDING

38. In order to enhance economic policy making, we will strengthen processes and practices to achieve timely information sharing in the following areas: (i) delays in reconciliation of fiscal and monetary accounts involving the Malawi Revenue Authority, MOF and RBM, which have recently produced large statistical discrepancies between above-the-line fiscal data and below-the-line financing data from the RBM; and (ii) inadequate provision of information on government operations to feed into the RBM's liquidity forecasting framework that guides monetary operations.

39. The government is grateful for the assistance it has received from the IMF and other partners to build capacity for the compilation and dissemination of economic statistics. We continue to need assistance to improve the quality of a wide range of statistics, including national accounts, prices, and the balance of payments. We are also in need of assistance to build capacity for the production of high frequency indicators of economic activity to guide timely policy making.

## VII. PROGRAM MONITORING

40. Program implementation will be monitored with quantitative financial targets and structural benchmarks (Tables A1 and A2). Modifications to the quantitative targets for December 2012, March 2013 and June 2013 are proposed to reflect the updated macroeconomic framework. The second review is scheduled to be completed by mid-March 2013 based on the end-December 2012 test date, the third review by mid-June 2013 based on the end-March 2013 test date, and the fourth review by mid-December 2013 based on the end-September test date. Definitions of key concepts and indicators, as well as reporting requirements, are set out in the accompanying Technical Memorandum of Understanding.

## ATTACHMENT II. TECHNICAL MEMORANDUM OF UNDERSTANDING (TMU)

### I. INTRODUCTION

1. This memorandum sets out the understandings between the Malawian authorities and the International Monetary Fund regarding the definitions of quantitative performance criteria, benchmarks, and indicative targets for the program supported by the ECF arrangement, and the related reporting requirements.

2. **Coverage:** The central government includes all 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 RBM. Monetary aggregates under the program are based on the twelve-bank monetary survey.

### II. QUANTITATIVE PERFORMANCE CRITERIA: DEFINITIONS AND DATA SOURCES

#### A. Floor on Net International Reserves of the RBM

3. **Definition of net international reserves (NIR) of the RBM:** 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 for the various currencies and then converted into kwacha using the program exchange rate for the U.S. dollar–kwacha exchange rate. The program exchange rate of the Malawi Kwacha to the U.S. dollar is set at MK320 = US$1. The corresponding cross exchange rates and program gold price for the duration of the program are in Table 3.

4. **Gross reserve assets of the RBM** are defined in 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).

5. **This concept includes the following:** (1) monetary gold holdings of the RBM; (2) holdings of SDRs; (3) the reserve position in the IMF; (4) foreign convertible currency holdings; (5) deposits held in foreign central banks, the Bank for International Settlements, and other banks; (6) loans to foreign banks redeemable upon demand; (7) foreign securities; and (8) other unpledged convertible liquid claims on nonresidents. It excludes the following: (1) any foreign currency claims on residents; (2) capital subscriptions in international institutions; (3) foreign assets in nonconvertible currencies; (4) 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; (5) gross reserves that are in any way encumbered or pledged, including, but not limited to: (i) assets blocked when used as collateral for third party loans and third-party payments, pledged to investors as a condition for investing in domestic securities, (ii) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and foreign reserves blocked for letters of credit.

6. **Gross reserve liabilities of the RBM** are defined as the sum of the following: (1) SDR allocations; (2) outstanding medium and short-term liabilities of the RBM to the IMF; and (3) all short-term foreign currency liabilities of the RBM to nonresidents with an original maturity of up to, and including, one year.

7. **Definition of budget support:** 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, including food security funding from the European Union and loan financing from the IMF, and donor inflows (in kwacha) from the U.S. dollar–denominated donor pool accounts for the health SWAp, education SWAp, agricultural SWAps, and National AIDS Commission (NAC) held in the Malawi banking system.

8. **Adjustment clause on NIR—budget support:** The floor on the NIR of the RBM will be adjusted upward by the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline (See Table 1). The floor on NIR of the RBM will be adjusted downward by the full amount up to a maximum of US$ 10 million by which the cumulative receipts from the budget support are less than the program baseline. Budget support is measured as the cumulative flow from the beginning of the fiscal year.

9. Adjustment clause on NIR—donor accounts for the social sector (including health, education, and other SWAps, and National AIDS Commission (NAC): The floor on the NIR of the RBM will be adjusted downward by the amount by which the donor inflows (in kwacha) from the U.S. dollar–denominated donor accounts for SWAps and NAC held in the RBM are smaller than the donor inflow (in kwacha) to those accounts in the program baseline. The downward adjustment will be capped at US$ 30 million. Donor inflows are measured as the receipts (in kwacha) by the budget from the beginning of the fiscal year.

10. **Adjustment clause on NIR—debt service payments:** The floor on NIR of the RBM will be adjusted upward (downward) by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of (exceed) the program baseline. The cumulative amount will be measured from the beginning of the fiscal year.

11. The total downward adjustment to NIR from a shortfall of (i) budget support and (ii) donor inflows to the donor accounts for the social sector relative to the program assumptions, and (iii) an excess of debt service payments to the World Bank and the African Development Bank (ADB) relative to the program assumptions will be capped at US$40 million. The floor on the NIR of the RBM will be adjusted upward by the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline and by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of the program baseline.

12. For this target and those for external debt and arrears, valuation will be in U.S. dollars, using the above defined program exchange rates.

13. Data on NIR, including its components, will be reported by the RBM on a weekly and end-month basis.

## B. Ceiling on the Net Domestic Assets of the Reserve Bank of Malawi and Reserve Money

14. **Definition of net domestic assets (NDA) of the RBM:** NDA of the RBM are defined in kwacha terms as end-quarter reserve money less NFA of the RBM at the program exchange rate. Reserve money consists of currency issued by the RBM and balances of commercial banks' accounts with the RBM. It includes required reserves held for Malawi kwacha deposits and any other domestic currency reservable liabilities and other demand and time deposits held with the RBM. The NDA program ceilings are the indicative money targets defined below less the NFA of the RBM.

15. **Definition of NFA of the RBM:** The NFA of the RBM are defined as the above-defined NIR plus other foreign assets of the RBM—including but not limited to: (1) capital subscriptions in international institutions; (2) foreign assets in nonconvertible currencies; and (3) gross reserves that are in any way encumbered or pledged, less any medium- and long-term foreign liabilities of the RBM.

16. **Adjustment clause on NDA—budget support:** The ceiling on NDA of the RBM will be adjusted downward by the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline. The ceiling on NDA of the RBM will be adjusted upward by the amount by which the cumulative flow of receipts from budget support are less than the program baseline, up to a maximum of US$10 million. The kwacha value of the cumulative shortfall (excess) will be calculated at the program exchange rate. Budget support is measured as the cumulative flow from the beginning of the fiscal year.

17. **Adjustment clause on NDA—donor pool accounts for the social sector (including health, education, and other SWAps, and NAC):** The ceiling on NDA of the

RBM will be adjusted upward by the amount by which the donor inflows (in kwacha) from the U.S. dollar–denominated donor accounts for the SWAps and NAC held in the RBM fall short of the donor inflow (in kwacha) to those accounts in the program baseline. The upward adjustment will be capped at US$30 million. Donor inflows are measured as the receipts received (in kwacha) by the budget. Donor inflows are measured from the beginning of the fiscal year.

18. **Adjustment clause on NDA—debt service payments:** The ceiling on NDA of the RBM will be adjusted downward (upward) by the full cumulative amount by which debt service payments to the World Bank and the ADB falls short of (exceeds) the program baseline (Table 1). The cumulative amount will be measured from the beginning of the fiscal year.

19. The total upward adjustment to NDA from a shortfall of (i) budget support (ii) donor inflows to the donor accounts for the social sector relative to the program assumptions and (iii) an excess of debt service payments to the World Bank and the African Development Bank (ADB) relative to the program assumptions will be capped at US$40 million. The downward adjustment to NDA will reflect the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline and by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of the program baseline.

20. **Adjustment clause on NDA—liquidity reserve requirement:** The ceiling on NDA of the RBM will be adjusted downward for a decrease in the reserve requirement ratio on domestic deposits, and will be adjusted upward for an increase in the ratio. The adjustment will be spread equally over two quarters, starting in the quarter in which the reserve requirement ratio is reduced. The adjuster will be calculated as follows: (one minus the existing required percentage of reserve assets) multiplied by (the program baseline required reserve ratio minus the new required reserve ratio) multiplied by (the amount of average reservable deposit liabilities in commercial banks during the last month before the change in regulation).

## C. Ceiling on Central Government Net Domestic Borrowing (CGDB)

21. **Definition of CGDB:** CGDB is computed as the sum of (1) net borrowing from the RBM (including ways and means advances, loans, holdings of local registered stocks, government bonds, and holdings of treasury bills minus deposits); (2) net borrowing from commercial banks (including advances, holdings of local registered stocks, and holdings of treasury bills minus deposits); (3) net borrowing from nonbanks (including, but not limited to, holdings of local registered stocks and holdings of treasury bills); and (4) holdings of promissory notes. The treasury bills and locally registered stocks are valued at cost rather than face value. The ceiling is measured as the change in the stock of CGDB since June 30, 2012, including promissory notes and securities transferred to the RBM from the

treasury since the beginning of the fiscal year. 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 CGDB.

22. **Definition of domestic arrears:** 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, and tax refunds. 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. Domestic interest payments are in arrears when the payment is not made on the due date. Payments for goods and services are deemed to be in arrears if they have not been made within 90 days of the date of invoice, or—if a grace period has been agreed—within the contractually agreed grace period.

23. **Adjustment clause on CGDB—budget support:** The ceiling of CGDB will be adjusted downward (upward) by the full amount by which cumulative kwacha receipts from budget support are greater (less than) the program baseline. The upward adjustment will be capped at US$10 million. In the event of excess budget support, the ceiling on CGDB will be adjusted by the full amount less US$30 million. The kwacha value of the cumulative shortfall (excess) will be calculated at the program exchange rate. Budget support is measured as the cumulative flow from the beginning of the fiscal year.

24. **Adjustment clause on CGDB—donor accounts for the social sector (including health, education, and other SWAps, and NAC):** The ceiling on CGDB will be adjusted upward by the full amount by which the donor inflows (in kwacha) from the U.S. dollar–denominated donor accounts for health, education, and other SWAps, and NAC held in RBM are smaller than the donor inflows (in kwacha) to those accounts in the program baseline. The upward adjustment will be capped at US$30 million. Donor inflows are measured as receipts received (in kwacha) by the budget. Donor inflows are measured from the beginning of the fiscal year.

25. **Adjustment clause on CGDB—debt service payments:** The ceiling (floor) on CGDB will be adjusted downward (upward) by the full cumulative amount by which debt service payments to the World Bank and the ADB fall short of (exceed) the program baseline. The cumulative amount will be measured from the beginning of the fiscal year.

26. **The total upward adjustment to CGDB** from a shortfall of (i) budget support (ii) donor inflows to the donor accounts for the social sector relative to the program assumptions and (iii) an excess of debt service payments to the World Bank and the African

Development Bank (ADB) relative to the program assumptions will be capped at US$40 million. The downward adjustment to NDA will reflect the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline and by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of the program baseline.

## D. Ceiling on External Payment Arrears

27. **Definition of external payment arrears:** 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.

## E. Ceiling on Nonconcessional External Debt

28. Definition **of nonconcessional external debt:** The definition of debt, for the purpose of the limit, is set out in Executive Board Decisions No. 6230-(79/140) August 3, 1979, and as amended by Decisions **No. 11096-(95/100), October 25, 1995; 12**274–(00/85) August 24, 2000; and 14416-(09/91), August 31, 2009. For program purposes, short-, medium-, and long-term debt is nonconcessional if it includes a grant element of less than 35 percent, as indicated in Decision No. 11248-(96/38), April 15, 1996. The ceiling on nonconcessional debt applies to the contracting and guaranteeing of debt with nonresidents by the central government, the RBM, public enterprises, and other official sector entities, 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.

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

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

31. Excluded from the limit is the use of IMF resources, and any kwacha-denominated treasury bill and local registered 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.

## III. Quantitative Indicative Targets and Structural Benchmarks

32. **Definition of reserve money:** 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. The reserve money targets are the projected end-quarter values starting with end-September r 2012 to end-December 2013.

33. **Definition of social spending:** Using functional classification of expenditure, social spending is computed as the sum of central government spending on health, education, the farm input subsidy program, and government social protection (comprising the government expenditures by the ministry of gender, children and social welfare, the ministry of disability and elderly affairs, and the local development fund) . In order to maintain Malawi's commitment and progress toward poverty reduction and the MDGs, the social spending allocations in the government budget will not be adjusted downward to meet fiscal targets of the program (Table 4).

## IV. Reporting of Certain Transactions in the Fiscal Accounts

34. **Donor pool–funded expenditures in support of the SWAps:** The Government of Malawi has embarked on an integrated program of service delivery in the health and education sectors (the so-called SWAps). In support of the health and education SWAps, some donors pool resources (the donor pool), and release these resources through normal government procedures (i.e., recurrent budget or development Part II budget) to the relevant sector. Financial flows into and out of this account will be reported on a monthly basis from the beginning of the fiscal year.

35. **Farm input subsidy program:** The government has embarked on a program of subsidizing agricultural inputs, in particular, fertilizer, to smallholder farmers to improve agricultural production, financed by the budget. The spending on the farm input subsidy program will be reported quarterly from the beginning of the fiscal year.

## V. Exchange Regime

36. **Avoiding multiple currency practices and exchange restrictions:** The RBM will ensure on-going assessment of the foreign exchange regime with support from IMF to ensure the consistency of the regime with Malawi's obligations under Article VIII. The RBM will continue to work towards ensuring that the spread between the official exchange rate and other market determined rates (bureau and parallel market rates) fall within 2 percent. The RBM will abide by the continuous PC on non-introduction or intensification of exchange restrictions and multiple currency practices.

## VI. Reporting Requirements

37. Monitoring of the program requires that the information listed in Table 5 below be reported to the IMF within the timeframe indicated.

**Table 1a. Malawi: Quantitative Targets (September 2012)[1]**

| | Criteria [2] | End-Mar 2012 Stock Act. | End-June. 2012 Stock Proj. | 2012 Stock Act. | Sept. 2012 Prog. | Sept. 2012 Act. | Status |
|---|---|---|---|---|---|---|---|
| **I. Monetary targets (millions of kwacha)** | | | | | | | |
| 1. Ceiling on net domestic assets of the RBM [3,4,5,6] | PC | 116,861 | 114,579 | 142,513 | 109,417 | 117,737 | NM |
| 2. Ceiling on reserve money[3] | IT | 89,168 | 76,178 | 101,398 | 88,210 | 95,657 | NM |
| **II. Fiscal targets (millions of kwacha)** | | | | | | | |
| 3. Ceiling on central government's net domestic borrowing [5,6,7] | PC | 176,588 | 178,847 | 188,853 | -11,988 | -41,220 | M |
| 4. Floor on social spending [8] | IT | | | | 39,034 | 27,959 | NM |
| **III. External sector targets (US$ millions, unless otherwise indicated)** | | | | | | | |
| 5. Floor on net international reserves of the RBM[3,5,6,9] | PC | -20 | -63 | -74 | 17 | 17 | M |
| 6. Ceiling on the accumulation of external payments arrears [7,10] | PC | | | | 0 | 0 | M |
| 8. Ceiling on new nonconcessional external debt maturing in more than one year [7,10] | PC | | | | 0 | 0 | M |
| 9. Ceiling on new nonconcessional external debt maturing in one year or less [7,10] | PC | | | | 0 | 0 | M |
| 10. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [10,11] | PC | | | | | | M |
| *Memorandum items:* | | | | | | | |
| Net foreign assets of the RBM (US$ millions) | | -107 | -148 | -158 | -82 | -85 | |
| Budget support (US$ millions) | | | | | 86 | 89 | |
| Budget support (millions of kwacha) | | | | | 21,945 | 23,210 | |
| Debt service payments to the World Bank and African Development Bank (millions of kwacha) | | | | | | | |
| Health SWAp receipts (millions of kwacha) | | | | | 5,248 | 7,732 | |
| Education SWAp receipts (millions of kwacha) | | | | | 8,378 | 7,227 | |
| NAC receipts (millions of kwacha) | | | | | 4,777 | 1,538 | |
| Program exchange rate (kwacha per US$) | | 260 | 260 | 260 | 260 | 260 | |

Sources: Reserve Bank of Malawi; Malawi Ministry of Finance; and IMF staff estimates.

[1] Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.
[2] "PC" means Performance Criterion, and "IT" means Indicative Target.
[3] Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).
[4] Target is subject to an adjuster for liquidity reserve requirement.
[5] Targets are subject to an adjuster for budget support and debt service payments.
[6] Targets are subject to an adjuster for donor-funded social sector expenditures consistent with the TMU.
[7] Defined as a cumulative flow.
8 Priority social spending as defined in the TMU and quantified in the authorities' budget.
9 Adjusted for Letters of credit with cash cover as at end-March and end-June.
10 Evaluated on a continuous basis.
11 Other standard PCs include introducing or modfying MCPs, concluding bilateral payments agreements that are inconsistent with Article VIII, and imposing or intensifying import restrictions for balance of payment reasons.

## Table 1b. Malawi: Quantitative Targets (December 2012–September 2013)[1]

| | Criteria [2] | End-Sept. 2012 | End-Dec. 2012 | | End-Mar. 2013 | | Indicative End-Jun. 2013 | | End-Sept. 2013 |
|---|---|---|---|---|---|---|---|---|---|
| | | Act. | Prog. | Rev. Prog. | Prog. | Rev. Prog. | Prog. | Rev. Prog. | Prog. |
| **I. Monetary targets (millions of kwacha)** | | | | | | | | | |
| 1. Ceiling on net domestic assets of the RBM [3,4, 5, 6] | PC | 117,737 | 118,542 | 118,293 | 106,256 | 132,082 | 100,930 | 114,444 | 94,132 |
| 2. Ceiling on reserve money[3] | IT | 95,657 | 97,809 | 96,615 | 99,120 | 99,095 | 105,830 | 107,845 | 111,830 |
| **II. Fiscal targets (millions of kwacha)** | | | | | | | | | |
| 3. Ceiling on central government's net domestic borrowing [5,6,7] | PC | -41,220 | 18,500 | -17,756 | 11,609 | 4,444 | 0 | -15,021 | -5,218 |
| 4. Floor on social spending [8] | IT | 27,959 | 94,044 | 95,156 | 121,798 | 144,922 | 151,899 | 185,511 | |
| **III. External sector targets (US$ millions, unless otherwise indicated)** | | | | | | | | | |
| 5. Floor on net international reserves of the RBM[3, 5, 6] | PC | 17 | 19 | 32 | 71 | -3 | 118 | 79 | 155 |
| 6. Ceiling on the accumulation of external payments arrears [7,9] | PC | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 8. Ceiling on new nonconcessional external debt maturing in more than one year [7,9] | PC | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 9. Ceiling on new nonconcessional external debt maturing in one year or less [7,9] | PC | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 10. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [9,10] | PC | | | | | | | | |
| *Memorandum items:* | | | | | | | | | |
| Net foreign assets of the RBM (US$ millions) | | -85 | -80 | -68 | -27 | -103 | 19 | -21 | 55 |
| Budget support (US$ millions) | | 89 | 86 | 170 | 151 | 176 | 208 | 234 | 49 |
| Budget support (millions of kwacha) | | 23,210 | 21,945 | 49,038 | 38,926 | 54,934 | 53,864 | 73,542 | 15,752 |
| Debt service payments to the World Bank and the African Development Bank (US$ millions) | | 0 | | 2 | | 1 | | 3 | 7 |
| Debt service payments to the World Bank and African Development Bank (millions of kwacha) | | 0 | | 684 | | 420 | | 827 | 2,174 |
| Health SWAp receipts (millions of kwacha) | | 7,732 | 5,364 | 7,876 | 7,771 | 10,778 | 7,771 | 11,173 | 3,224 |
| Education SWAp receipts (millions of kwacha) | | 7,227 | 13,221 | 9,614 | 17,073 | 14,994 | 19,049 | 18,194 | 4,800 |
| NAC receipts (millions of kwacha) | | 1,538 | 7,315 | 5,101 | 10,019 | 8,719 | 12,220 | 12,281 | 3,563 |
| Program exchange rate (kwacha per US$) | | 260 | 260 | 320 | 260 | 320 | 260 | 320 | 320 |

Sources: Reserve Bank of Malawi; Malawi Ministry of Finance; and IMF staff estimates.

[1] Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.

[2] "PC" means Performance Criterion, and "IT" means Indicative Target.

[3] Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).

[4] Target is subject to an adjuster for liquidity reserve requirement.

[5] Targets are subject to an adjuster for budget support and debt service payments.

[6] Targets are subject to an adjuster for donor-funded social sector expenditures consistent with the TMU.

[7] Defined as a cumulative flow.

8 Priority social spending as defined in the TMU and quantified in the authorities' budget.

9 Evaluated on a continuous basis.

10 Other standard PCs include introducing or modfying MCPs, concluding bilateral payments agreements that are inconsistent with Article VIII, and imposing or intensifying import restrictions for balance of payment reasons.

**Table 2. Malawi: Structural Benchmarks, 2012–13**

| Measure | Status/Target Date | Macro Rationale | Status |
|---|---|---|---|
| **Prior Actions** | | | |
| ***Approval of the arrangement*** | | | |
| Parliamentary passage of a budget for FY 2012/13 in line with program objectives | | Toward fiscal sustainability | Met |
| ***First review*** | | | |
| Shut down RBM's uncollateralized lending to banks | | | |
| **Structural benchmarks** | | | |
| **Fiscal transparency** | | | |
| Publish monthly revenue collections of the Malawi Revenue Authority in newspapers within two weeks of the end of the month. | 7/31/2012 | Build credibility after recent incidents of inflation of revenue data by the Ministry of Finance. | Met |
| **Public financial management** | | | |
| Provide Ministries, Departments and Agencies with quarterly spending ceilings consistent with quarterly fiscal targets in the program, and enforce ceilings. | Begin in Sept 2012 for FY2012/13 Q2 and quarterly thereafter | Keep spending within available resource envelope. | Met for Q2 |
| Verify existing stock of government domestic arrears and formulate a plan for settling verified claims. | 31-Dec-12 | Ascertain magnitude of government obligations. | |
| Configure the IFMIS Purchase Order (PO) module to support commitment control. | 31-Dec-12 | To restrain creation of arrears. | |
| Progressively extend processes for capturing donor funded project transactions in IFMIS to all projects where bank accounts are controlled by the government of Malawi. | 31-Mar-13 | Fuller accounting for impact of aid flows on the budget. | |
| **Monetary Policy** | | | |
| Amend RBM Act to limit the outstanding amount of RBM's total lending to government. | 30-Jun-13 | Reduce fiscal dominance to enhance effectiveness of monetary policy. | |
| **Financial sector** | | | |
| RBM to publish a financial stability report on a semi-annual basis, with a lag of no more than four months. Start with publication of report for quarter ending March 2012. | Semi-annual, starting in July 2012. | Promote financial stability. | Met |
| Obtain approval and begin implementation of the Financial Sector Development Strategy | 31-Dec-12 | Financial deepening. | |

**Table 3. Malawi: Cross Rates for Nominal Exchanges Rate and Gold Price for the 2012–13 Program**

| | September 30, 2012 |
|---|---|
| Gold bullion LBM[1] US$/troy ounce | 1,774.810 |
| SDR to US$ exchange rate | 0.648 |
| Euro to US$ exchange rate | 0.773 |
| Yen to US$ exchange rate | 77.570 |
| Yuan to US$ exchange rate | 6.341 |
| Rand to US$ exchange rate | 8.305 |
| UK £ to US$ exchange rate | 0.618 |

Source: IFTS, RBM

[1] LBM connotes London Bullion Market.

## Table 4. Malawi: Breakdown of Social Expenditures in 2012/13

| | 2012/13 | Q1 Act. | Q2 | Q3 | Q4 |
|---|---|---|---|---|---|
| **Health Expenditure** | | | | | |
| Wages | 14,736.67 | 3,932.97 | 3,364.00 | 3,670.00 | 3,769.70 |
| Other Recurrent | | | | | |
| *Ministry of Health ORT* | 9,606.48 | 1,988.59 | 2,510.00 | 2,550.00 | 2,557.89 |
| *Local Assemblies ORT* | 9,076.92 | 2,287.18 | 2,100.00 | 1,336.87 | 3,352.87 |
| *Subvented Organisations* | 100.00 | 25.00 | 25.00 | 25.00 | 25.00 |
| Development Part II | 3,461.00 | 479.68 | 993.00 | 800.00 | 1,188.32 |
| Total Health | 36,981.07 | 8,713.41 | 8,992.00 | 8,381.87 | 10,893.78 |
| **Education Expenditure** | | | | | |
| Wages | 35,946.48 | 8,531.71 | 8,251.71 | 9,400.00 | 9,763.07 |
| Other Recurrent | | | | | |
| *Ministry of Education ORT* | 12,537.59 | 2,657.99 | 3,100.00 | 3,400.00 | 3,379.60 |
| *Local Assemblies ORT* | 5,691.99 | 1,778.59 | 1,170.00 | 1,210.00 | 1,533.40 |
| *Subvented Organisations* | 19,149.03 | 4,567.73 | 4,500.00 | 5,000.00 | 5,081.30 |
| Development Part II | 5,126.45 | 1,128.63 | 1,100.00 | 1,300.00 | 1,597.82 |
| Total Education | 78,451.55 | 18,664.65 | 18,121.71 | 20,310.00 | 21,355.19 |
| **Farm Input Subsidy Program** | 54,904.50 | 100.00 | 34,742.00 | 14,742.00 | 5,320.50 |
| **Gender, Children and Social Welfare** | | | | | |
| Wages | 518.29 | 129.57 | 129.57 | 129.57 | 129.57 |
| Other Recurrent | 169.53 | 49.17 | 49.17 | 30.00 | 41.19 |
| Development Part II | 295.00 | 62.09 | 62.09 | 62.09 | 108.73 |
| Total Gender, Children and Social Welfare | 982.81 | 240.83 | 240.83 | 221.66 | 279.49 |
| **Disability and Elderly Affairs** | | | | | |
| Wages | 53.40 | 12.88 | 12.88 | 12.88 | 14.75 |
| Other Recurrent | 158.94 | 82.09 | 30.00 | 30.00 | 16.85 |
| Development Part II | 80.75 | 10.00 | 30.00 | 30.00 | 10.75 |
| Total Disability and Elderly Affairs | 293.09 | 104.97 | 72.88 | 72.88 | 42.35 |
| **Local Development Fund** | 13,783.87 | 120.00 | 5,000.00 | 6,000.00 | 2,663.87 |
| **Poverty and Disaster Management Cost Centre under the Office of the President and Cabinet** | 113.53 | 15.22 | 27.45 | 37.45 | 33.42 |
| **Total Social Expenditure Projections** | **185,510.42** | **27,959.09** | **67,196.87** | **49,765.86** | **40,588.60** |
| **Cumulative Quarterly Targets** | | **27,959.09** | **95,155.95** | **144,921.82** | **185,510.42** |

Source: Malawi authorities.

**Table 5: Reporting Requirements**

| Data Description | Data Freq. | Reporting Agency | Reporting Freq. | Delivery Lag | Delivery Date | Delivery Mode |
|---|---|---|---|---|---|---|
| Gross international reserves, exchange rate, and foreign exchange purchases and sales | D | RBM | W | 2 | F | E |
| Reserve money and its components (NDA and NFA), OMO transactions, and RBM conversion of treasury bills; RBM balance sheet | W | RBM | M | 30 | 30 | E |
| Daily exchange rate | D | RBM | W | 1 | F | E |
| Treasury bill auction results | W | RBM | W | 2 | F | E |
| Spread between bureau midrate and the official exchange midrate | W | RBM | M | 30 | 30 | E |
| Spread between commercial bank midrate and the official exchange midrate | W | RBM | M | 30 | 30 | E |
| International Reserve and Foreign Currency Liquidity Data Template | M | RBM | M | 30 | 30 | E |
| Central government domestic borrowing | M | RBM | M | 30 | 30 | E |
| Interest rates | M | RBM | M | 30 | 30 | E |
| Holdings of local registered stocks and treasury bills | M | RBM | M | 30 | 30 | E |
| Detailed issue and maturity profile for treasury bills | M | RBM | M | 30 | 30 | E |
| Excess reserves by bank | W | RBM | M | 30 | 30 | E |
| Details of project and balance of payment support | M | RBM | M | 30 | 30 | E |
| FCDA Holdings | M | RBM | M | 30 | 30 | E |
| RBM foreign exchange cash flow | M | RBM | M | 30 | 30 | E |
| Foreign exchange exposure limits by bank | M | RBM | M | 30 | 30 | E |
| Bank statements of the Health SWAp account held at RBM | M | RBM | M | 30 | 30 | E |
| Full banking survey (on monthly basis) | M | RBM | M | 45 | 15 | E |
| Financial soundness indicators by banks | Q | RBM | Q | 45 | T15 | E |
| NAC consolidated statement of sources and uses of funds (cashflow statement) | M | MOF | M | 30 | 30 | E |
| Health SWAp statement of sources and uses of funds | M | MOF | M | 30 | 30 | E |
| Fiscal table (GFS) including revenue, expenditure, and financing | M | MOF | M | 30 | 30 | E |
| Revenue data (from MRA) | M | MOF | M | 30 | 30 | E |
| D\ata on expenditure for domestically financied capital projects | M | MOF | M | 30 | 30 | E |
| New external loans contracted or guaranteed by the central government[1] | Q | MOF | Q | 30 | T30 | E |
| External debt services (actual and projections) | Q | MOF | Q | 30 | T30 | E |
| Borrowing of all major parastatals[2] | Q | MOF | Q | 45 | T15 | E |
| Annual Financial reports of the eight (8) major parastatals and MSB | A | MOF | Q | 90 | 30 | H |
| Report on IMF program performance | Q | MOF | Q | 45 | T15 | E |
| Statement on new arrears | Q | AuG | Q | 45 | T15 | E |
| Consumer price index and monthly statistical bulletin | M | NSO | M | 30 | 30 | E |
| Import and export data | M | NSO | M | 45 | T15 | E |
| Balance of payments, and quarterly statistical bulletin | Q | NSO | Q | 45 | T15 | E |
| National accounts, balance of payments, and quarterly statistical bulletin | A | NSO | BA | 45 | T15 | E |

D- Daily, W-Weekly, M-Monthly, Q-Quarterly, BA-Bi-annual, F-Friday, 30-Every 30th, T30-Every third 30th, E-Electronic, H-Hard Copy

[1] 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.

[2] Agriculture Development and Marketing Corporation, Air Malawi, Electric Supply Company of Malawi. M*alawi Development Corporation,* Malawi Housing Corporation, Malawi Postal Corporation, Malawi Telecommunications Ltd., Northern Regional Water Board.

## APPENDIX II. MALAWI: REAL EXCHANGE RATE ARRANGEMENT[1]

*This note assesses the degree of exchange rate misalignment in Malawi until end-September 2012, using a high frequency time-series equilibrium real exchange rate (ERER) approach. The results suggest that the Kwacha is broadly in equilibrium as at end-September 2012.*

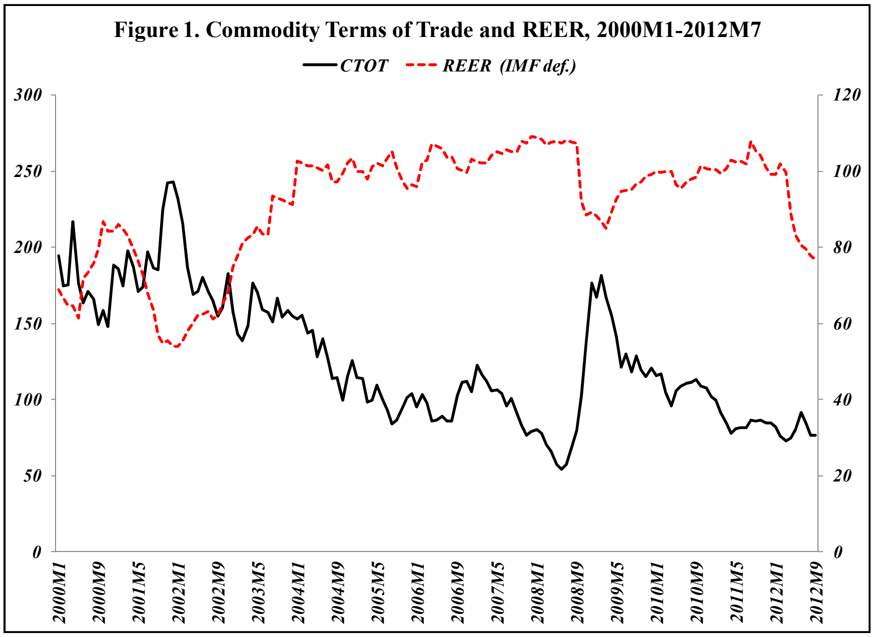
**The reduced-form time series ERER approach to exchange rate assessment consists of three steps.** First, a measure of monthly Commodity Terms of Trade (CTOT) is constructed for Malawi between 1990M1 and 2012M9 and a cointegrating relationship between the CTOT and the monthly Real Effective Exchange Rate (REER) is established. Second, fitted values of the equilibrium real effective exchange rates are derived from the estimated cointegrating vector. Third, the percentage deviations of the actual real effective exchange rates from their predicted values are calculated and treated as a measure of the exchange rate misalignment.

**Fluctuations in the REER in Malawi have been negatively associated with changes in the commodity terms of trade in the last decade (Figure 1).** Due to restrictive foreign exchange policies in the past, the REER has been moving in the opposite direction of the commodity terms of trade since 2000, resulting in an overvalued exchange rate in the first half of 2012. Our measure for the CTOT index is defined as:

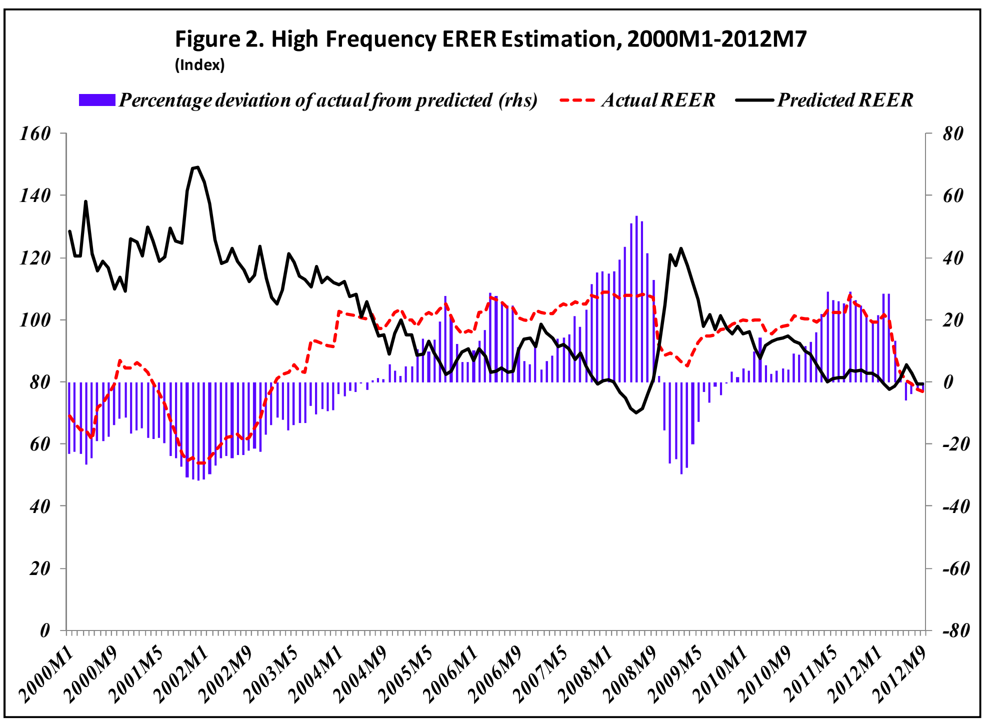
$$CTOT_t = \prod_j \left(\frac{P_{jt}}{MUV_t}\right)^{X_j} / \prod_j \left(\frac{P_{jt}}{MUV_t}\right)^{M_j}$$

where $MUV_t$ is a manufacturing unit value index used as a deflator, $X_j$ ($M_j$ ) is the share of exports (imports) of commodity j in country i's GDP, and $P_{jt}$ is the individual commodity price at time t. The commodities are: Tobacco, Uranium, Tea, Sugar, Cotton, Rice, Coffee, Maize, Petroleum Products, and Fertilizers. By construction, the movements in the CTOT index are due to changes in commodity prices as the export and import shares are taken as fixed and so remain constant over time. For empirical application, we calculate $X_j$ and $M_j$ as the average value of these shares between 1990 and 2011.

[1]Prepared by Mehdi Raissi (SPR).




**The ERER approach suggests that the kwacha is broadly in equilibrium.** A high frequency estimation of the cointegrating relationship between the real exchange rate and the commodity terms of trade (as the only explanatory variable) shows that these two variables are cointegrated (with a statistically significant elasticity coefficient of 41.8 percent). The estimation suggests that the kwacha is broadly in equilibrium as at end-September 2012 (See Figure 2).



## APPENDIX III. FUEL PRICING MECHANISM IN MALAWI[1]

### Background

Until May 2000, all fuel importation was done by the Petroleum Control Commission (PCC), with the government setting retail prices. In 2000, an automatic adjustment mechanism was introduced whereby fuel prices would move up and down in line with world prices, with the Multi Sector Energy Pricing Committee overseeing the setting of prices. After the introduction of the automatic price adjustment mechanism, 80 percent of the country's fuel began to be imported by Petroleum Importers Limited, (PIL), with the remaining 20 percent still being imported by PCC.[2]

In 2007, the Malawi Energy Regulatory Authority (MERA) was established to regulate the energy sector, including petroleum products. The automatic price adjustment mechanism (APM) ceased to operate and was replaced by a system, whereby the final retail price was determined by building up profit margins and taxes, including levies on artificially low landed costs.

A Price Stabilization Fund (PSF) was created into which payments were to be made when the total costs of importing fuel (including transportation, taxes, levies, wholesale and retail margins etc) were lower than the retail pump price, and from which withdrawals were to be made when the retail price was higher than the total costs. Prices were expected to be adjusted whenever the PSF was depleted. But since prices were adjusted infrequently, the PSF accumulated arrears.

The fuel importation system came under stress with the intensification of restrictions on foreign exchange transactions in August 2011 and severe shortage of foreign exchange. Shortly thereafter, the National Oil Company of Malawi (NOCMA) which had been established in [June 2011] to manage the country's strategic reserves of fuel, displaced PIL as the principal fuel importer. NOCMA benefitted from favorable access to foreign exchange, including loans from the PTA Bank, facilitated by the Reserve Bank of Malawi.

In May 2012, following the devaluation of the kwacha and the liberalization of the foreign exchange regime for current account transactions, the government increased fuel prices to bring them in line with import costs and re-introduced the automatic adjustment mechanism for fuel prices. The government also decided that NOCMA's activities would be limited to its original mandate of overseeing the country's strategic reserves and that importation of fuel for regular consumption will revert to the private sector.

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[1] Prepared by Manuk Ghazanchyan (AFR).

[2] PIL is a private company owned by the oil companies in Malawi and managed through a body of directors drawn from each oil company.

**Fuel supply and demand**

Malawi uses three products of fuel: petrol diesel and paraffin (Table 1). [3] Annual demand for all fuel products is about 400 million liters. The total supplied volume for fuel in 2011 was about 287 million liters, much lower than the estimated demand. With the adoption of automatic fuel adjustment pricing mechanism, the supply volumes of petrol, diesel and paraffin is projected to amount to about 369 million liters in 2012.

Malawi's current storage capacity is 20 days, and 60 days advanced planning is needed to get fuel supplies on time. Malawi receives its fuel supply through three main ports: Beira (80 percent) and Nicala (5 percent) (Mozambique) and 15 percent through Dar es Salaam (Tanzania). Nacala port is often cited to be the best route for Malawi to get most of its fuel supplies as it is connected by both rail and road.

**Table 1. Malawi: Fuel volumes (mln liters) 1/**

| | Petrol | Diesel | Parafin | Total |
|---|---|---|---|---|
| 2011 | 83.2 | 164.9 | 38.5 | 286.6 |
| 2012 | 120 | 227.0 | 22.0 | 369.0 |
| Percent change | 44 | 38 | -43 | 29 |

1/ On calendar year basis.

**Fuel pricing and taxation**

The key in determining the final pump price and the amount of taxes is the In Bond Landed Cost (IBLC) which reflects the actual cost of landing the product in the country (Table 2). Until May 2012, the government chose to apply levies and taxes on an outdated (historical) IBLC base, which artificially lowered both the fiscal revenues of the government and the pump price of fuel products. Since May, the IBLC price reflects the actual cost of landing the product in the country. As a result, in May, the pump price for petrol increased from K380 (US$1.23) to K490/litre (US$1.59) representing a 29 percent increase and the price of diesel jumped from K360 ($1.17) to K475/litre ($1.54), representing a 32 percent hike. The price of paraffin for domestic use was kept at K171 per litre, but the price of industrial paraffin was increased to K388/litre, representing a 130 percent increase. Continuing in this vein, the price adjustment in November 2012 produced the following schedule of prices (Table 2): petrol is now priced at K606.3 ($1.85) per liter (up from K539 per liter in September), diesel has been adjusted up to K597.40 ($1.82) per Liter (up from K521.90), paraffin for industrial use is at K509.9 (($1.55) per liter (up from K434.3), while the cost of paraffin for domestic use remains unchanged at K171 per Liter. The November price adjustments also reflected

[3] The average daily demand of total fuel has been estimated at 1.124 million liters, which translates to 33.6 million liters per month, making the annual demand to stand around 403.2 million liters.

increases in: the wholesale margins for Oil Marketing Companies, retail margins for Service Station Operators, and Road Freight Rates for Fuel Tanker Operators, in order to enable these entities to cover their operational costs.

Considering that the price fluctuations are very frequent on the international market, the APM is set to respond to IBLC changes within a ±5 percent threshold. When the change in IBLC is more than 5 percent, prices are adjusted upwards and vice versa.

**Table 2. Malawi: Petroleum Products Price Build up in Malawi**
**Effective 8th November, 2012**

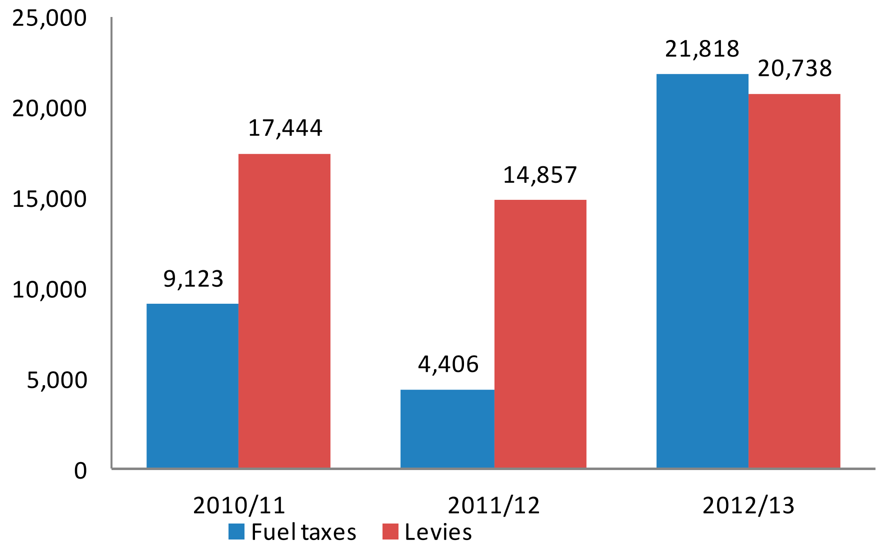
(Given in tambala per litre)

| | Petrol | Diesel | Paraffin |
|---|---|---|---|
| FOB | 28,998.84 | 30,773.53 | 31,970.92 |
| ROAD FREIGHT | 4,456.83 | 4,497.86 | 4,612.30 |
| INS/HANDLING | 228.8 | 215.68 | 195.7 |
| LOSSES | 160.87 | 114.78 | 183.24 |
| **IBLC (BT/LL)** | **33,845.34** | **35,601.85** | **36,962.16** |
| ENERGY REGULATORY LEVY | 300 | 300 | 300 |
| ROAD LEVY | 3,500.00 | 3,000.00 | - |
| MBS CESS | 67.69 | 71.20 | 73.92 |
| RURAL ELECTRIFICATION LEVY | 2728.35 | 2688.3 | 2294.5 |
| STORAGE LEVY | 500 | 500 | 500 |
| IBLC LOSS RECOVERY | 4,401.40 | 2,517.85 | 255.17 |
| PRICE STABILIZATION FUND | 1,692.27 | 1,780.09 | 1,848.11 |
| **DUTY FREE PRICE** | **47,035.05** | **46,459.27** | **42,233.91** |
| DUTY | 3,384.53 | 3560.19 | 1,848.11 |
| EXCISE DUTY | 3,722.99 | 3,916.20 | 1,940.51 |
| **DUTY PAID PRICE** | **54,142.57** | **53,935.66** | **46,022.53** |
| DISTRIBUTION MARGIN | **233.00** | **233.00** | **233.00** |
| GROSS MARGIN | 2,622.54 | 1,989.83 | 1,648.24 |
| **WHOLESALE PRICE** | **57,198.11** | **56,358.49** | **48,103.77** |
| RETAIL MARGIN | 3,431.89 | 3,381.51 | 2,886.23 |
| PUMP PRICE | **60,630.00** | **59,740.00** | **50,990.00** |
| **Kwacha per litre** | **606.30** | **597.40** | **509.90** |
| **Percentage Change** | **12.49** | **14.47** | **17.41** |

Besides excise and import duties, Malawi's fuel pump prices reflect various other government levies including energy regulation levy to finance operational activities of MERA; road levy for road's infrastructure development and rehabilitation; safety net levy for development projects. Storage levy for setting up strategic fuel reserve storage facilities, and rural electrification levy for electricity supply projects.

The levies constitute 34 percent of the pump price of petrol, 27 percent of the pump price of diesel, and 21 percent of the pump price of paraffin. Figure 1 shows the share of each tax item in total fuel tax revenues.

**Figure 1. Malawi: Fuel taxes, Levies and Price Stabilization Fund (billion Kwacha)**




**Fiscal impact**

The recent adoption of automatic adjustment price mechanism (APM) for fuel prices based on the actual costs of imports provided a significant boost to the 2012/13 budget revenues of about 1 ½ percent of GDP. This is calculated based on the new estimated import volumes for 2012/13, the true cost of fuel imports and adjusted tax rates after the adoption of APM.

**Table 3. Malawi: Evolution of Fuel Taxes and Levies**

| | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|
| | (Billions of Kwacha) | | |
| Total fuel taxes and levies | 26,567 | 19,263 | 42,556 |
| Fuel taxes | 9,123 | 4,406 | 21,818 |
| Excise | 6,936 | 3,322 | 10,397 |
| Import duty | 2,187 | 1,085 | 11,421 |
| Levies | 17,444 | 14,857 | 20,738 |
| PSF | 13,330 | 23,073 | 2,670 |
| | (Percent of total tax and non-tax revenues) | | |
| Total fuel taxes and levies | 12.8 | 9.3 | 16.3 |
| Fuel taxes | 4.4 | 2.1 | 8.3 |
| Excise | 3.3 | 1.6 | 4.0 |
| Import duty | 1.1 | 0.5 | 4.4 |
| Levies | 8.4 | 7.2 | 7.9 |
| | (Percent of GDP) | | |
| Total fuel taxes and levies | 3.1 | 2.0 | 3.6 |
| Fuel taxes | 1.1 | 0.5 | 1.8 |
| Excise | 0.8 | 0.3 | 0.9 |
| Import duty | 0.3 | 0.1 | 1.0 |
| Levies | 2.1 | 1.5 | 1.7 |
| *Memorandum items* | | | |
| Total tax and non-tax revenues (billions of Kwacha) | 207,571 | 207,525 | 261,690 |
| Total tax and non-tax revenues (percent of GDP) | 24.5 | 21.6 | 22.1 |
| Nominal GDP | 846,097 | 960,516 | 1,185,527 |

## Annex I. Malawi—Relations with the Fund

(As of October 31, 2012)

**Membership Status**

Joined: July 19, 1965; Article VIII

**General Resources Account:**

| | SDR Million | %Quota |
|---|---|---|
| Quota | 69.40 | 100.00 |
| Fund holdings of currency (exchange rate) | 66.96 | 96.69 |
| Reserve tranche position | 2.44 | 3.52 |

**SDR Department:**

| | SDR Million | %Allocation |
|---|---|---|
| Net cumulative allocation | 66.37 | 100.00 |
| Holdings | 0.59 | 0.89 |

**Outstanding Purchases and Loans:**

| | SDR Million | %Quota |
|---|---|---|
| ESF Arrangements | 34.70 | 50.00 |
| ECF Arrangements | 70.02 | 100.89 |

**Latest Financial Arrangements:**

| Type | Date of Arrangement | Expiration Date | Amount Approved (SDR Million) | Amount Drawn (SDR Million) |
|---|---|---|---|---|
| ECF | 07/23/2012 | 07/22/215 | 104.10 | 13.02 |
| ECF[1/] | 02/19/2010 | 02/18/2013 | 52.05 | 13.88 |
| ESF | 12/03/2008 | 12/02/2009 | 52.05 | 34.70 |

[1]Formerly PRGF.

**Projected Payments to Fund [1]**

**(SDR Million; based on existing use of resources and present holdings of SDRs):**

| | Forthcoming | | | | |
|---|---|---|---|---|---|
| | 2012 | 2013 | 2014 | 2015 | 2016 |
| Principal | | 5.37 | 16.66 | 17.35 | 17.86 |
| Charges/Interest | 0.01 | 0.15 | 0.29 | 0.25 | 0.20 |
| **Total** | 0.01 | 5.52 | 16.94 | 17.60 | 18.06 |

[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] | 1057.00 |
| *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 Post-Catastrophe Debt Relief (PCDR):** Not Applicable

**Safeguards Assessments:**

An update safeguards assessment for the Reserve Bank of Malawi is substantially complete. The RBM continues to publish financial statements that are prepared and audited in accordance with international standards. However, the assessment reiterates a key safeguards concern – the lack of operational autonomy - and recommends that already envisaged amendments to the

RBM Act to limit lending to government be expanded to strengthen RBM autonomy more broadly. Other recommendations focus on enhancing oversight of foreign reserves management and improvements to data compilation procedures. The latter includes measures to strengthen transparency of contingent liabilities arising from letters of credit that can have implications for program data. The RBM is committed to implementing the assessment's recommendations. The recommendations of the assessment do not require action in the context of the first review and will be closely monitored going forward.

**Exchange Arrangements:**

During the second review of the PRGF arrangement in August 2006, a multiple currency practice (MCP) under Article VIII emerged (manifested by the significant spread between the commercial bank exchange rates and the rates at foreign exchange bureaus). In May 2012, the government liberalized the foreign exchange regime, devalued the kwacha by about 33 percent and adopted a floating exchange rate regime. Staff is in the process of reviewing recent reforms to make an assessment of Malawi's exchange rate system. Malawi maintains restrictions on the capital account. While the de jure exchange rate arrangement is floating, staff's latest assessment classified the de facto arrangement as "other managed".

**Article IV Consultation:**

Malawi is on a 24-month Article IV consultation cycle. The last Article IV Consultation mission was conducted in conjunction with the discussions on the new ECF-supported program arrangement in May/June 2012. The Executive Board concluded the last Article IV consultation with Malawi on July 23, 2012.

**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).

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:**

| Date of Delivery | Department | Ministry/Agency | Purpose/Topic | Modality |
|---|---|---|---|---|
| 11/12 | STA | NSO | Prices Statistics | Mission |
| 10/12 | MCM | RBM | Liquidity Management, Monetary Operations and Related Issues | Mission |
| 10/12 | FAD | Ministry of Finance/MRA | Revenue Administration | Mission |
| 05/12 | STA | NSO | Consumer Price Indices Mission | Mission |
| 04/12 | STA | NSO | Balance of Payments Statistics | Mission |
| 04/12 | STA | NSO | Provide advice to improve the GDP methodology and assist with improving the data sources and indicators | Mission |
| 04/12 | STA | NSO | Balance of Payments and International Investment Position Statistics | Mission |
| 03/12 | FAD | Ministry of Finance | Strengthening the IFMIS control environment | Mission |
| 03/12 | FAD | Ministry of Finance | Public Financial Management (PFM) Reforms | Report |
| 03/12 | FAD | Ministry of Finance/MRA | Follow-up and Consolidating Headquarters functions and Customs Risk Management Mission | Mission |
| 01/12 | MCM | RBM | Review of Implementation of Risk Based Supervision | Report |
| 01/12 | FAD | Ministry of Finance | Developing a Draft Budget Framework Document (BFP) | Mission |
| 12/11 | FAD | Ministry of Finance | Public Financial Management (PFM) Reforms | Mission |
| 12/11 | MCM/LEG | RBM | Review the Foreign Exchange Regime | Mission |
| 11/11 | FAD | Ministry of Finance | Macro fiscal training | Mission |
| 11/11 | MCM | RBM | Development of asset management manual. | Mission |
| 11/11 | MCM | RBM | Further Development of a Framework for Consolidated Supervision | Report |
| 11/11 | FAD | Ministry of Finance | Improving capacity in Business process re-engineering and IT implementation. | Mission |
| 10/11 | FAD | Ministry of Finance | Program Budgeting and Developing the Medium-term Expenditure Framework Cycle | Mission |
| 06/11 | FAD | Ministry of Finance | Measures for Tax Reform and Taxation of Mining | Mission |
| 06/11 | FAD/MRA | Ministry of Finance | Enhancing taxpayer compliance and revenue performance | Mission |

| Date of Delivery | Department | Ministry/Agency | Purpose/Topic | Modality |
|---|---|---|---|---|
| 06/11 | STA | Ministry of Finance | Government Finance Statistics | Report |
| 06/11 | FAD | Ministry of Finance | Macro-fiscal training, scoping and needs assessment | Mission |
| 06/11 | MCM | RBM | Developing AML/CFT Offsite Supervisory Tools and Practices | Mission |
| 06/11 | FAD | Ministry of Finance/MRA | Malawi: Enhancing Tax Compliance and Revenue Performance | Report |
| 06/11 | FAD | Ministry of Finance/MRA | Tax Administration | Mission |
| 06/11 | FAD | Ministry of Finance | Measures for Tax Reform and the Taxation of Mining | Mission |
| 05/11 | FAD | Ministry of Finance | Fixed Assets and Financial Reporting | Mission |
| 05/11 | FAD | Ministry of Finance/MRA | Report on Strengthening Headquarters functions and Customs Risk Management Mission | Mission |
| 04/11 | STA | NSO | Incorporate new source data in the balance of payments and develop new worksheets | Mission |
| 04/11 | MCM | RBM | Assisting Reserve Bank of Malawi to further develop a framework for consolidated supervision | Mission |
| 04/11 | MCM | RBM | Developing Capacity for Stress Testing - Mission Report to the Reserve Bank of Malawi | Report |
| 02/11 | STA | NSO | Assess SUT and B-I prerequisites, data sources, compilation and dissemination for NAS | Mission |
| 02/11 | STA | NSO | Review of National Accounts Statistics | Report |
| 01/11 | FAD | Ministry of Finance | Streamlining Budget Documentation, Revising Budget Circular, Reintroducing MTEF | Mission |
| 11/10 | FAD | Ministry of Finance | Integrated Financial Management Information System (IFMIS): Review And Implementation Strategies | Report |
| 11/10 | STA | RBM | Monetary and Financial Statistics | Mission |
| 11/10 | MCM | RBM | Regulation and Oversight of Mobile Payments and Related Issues | Mission |
| 10/10 | STA | NSO | Assist in reviewing and modifying the PPS and PPI. | Mission |
| 10/10 | FAD | Ministry of Finance | IFMIS/Cash Management | Mission |
| 10/10 | FAD | Ministry of Finance | Program Budgeting/Output Budgeting | Mission |
| 10/10 | FAD | Ministry of Finance | In-year Fiscal Reporting/Budget Documentation | Mission |
| 10/10 | FAD | Ministry of Finance | Joint review of PFMRP | Mission |
| 10/10 | FAD | Ministry of Finance | Strengthening Program Budgeting, Performance Measurement, and Budget | Report |

| Date of Delivery | Department | Ministry/Agency | Purpose/Topic | Modality |
|---|---|---|---|---|
| | | | Documentation. | |
| 08/10 | FAD | Ministry of Finance | Revenue Policy and Administration | Report |
| 07/10 | FAD | Ministry of Finance | Strengthening the large taxpayers office | Mission |
| 07/10 | FAD | Ministry of Finance | Installation of expert and revenue Administration follow up mission (including review of ITAS implementation) | Mission |
| 07/10 | STA | NSO | Implementation of Balance of Payments Standards | Mission |
| 07/10 | STA | NSO | Balance of Payments and International Investment Position Statistics | Report |
| 06/10 | FAD | Ministry of Finance | Issues in Tax Policy and Taxation of Mining | Mission |
| 05/10 | MCM | RBM | Training in Techniques of Stress Testing of Prudential Data | Report |
| 05/10 | FAD | Ministry of Finance | Revenue Policy and Administration | Report |
| 01/10 | FAD | Ministry of Finance | Output-based budget and expenditure tracking | Mission |
| 01/10 | STA | NSO | Balance of payments statistics | Mission |
| 10/09 | MCM | RBM | Central bank policy | Mission |
| 10/09 | MCM | RBM | Central banking | Mission |
| 09/09 | FAD | Ministry of Finance | Improving output budgeting | Mission |
| 08/09 | LEG | Ministry of Finance | Tax procedure code | Mission |
| 05/09 | LEG | Ministry of Finance | Tax procedure code | Mission |
| 05/09 | FAD | Ministry of Finance | Linkage between policy and budgetary allocations | Mission |
| 04/09 | FAD | RBM | Monetary operations and reserves management | Mission |
| 03/09 | FAD | Ministry of Finance | Revenue administration | Mission |
| 03/09 | FAD | Ministry of Finance | Prepare modernization plan and support tax administration | Mission |
| 02/09 | FAD | Ministry of Finance | Integration of accounting systems and fiscal reporting | Mission |
| 02/09 | MCM | RBM | Currency handling and reform | Mission |
| 02/09 | MCM | RBM | Monetary operations/money markets | Mission |
| 01/09 | STA | RBM | DFID: Money and banking statistics | Mission |
| 01/09 | MCM | RBM | Monetary operations/money markets | Mission |
| 01/09 | MCM | RBM | Macro and FSI Analysis | Mission |
| 01/09 | MCM | RBM | TA coordination/evaluation | Mission |

## ANNEX II. MALAWI—JOINT MANAGERIAL ACTION PLAN

| Title | Products | Provisional Timing of Missions | Expected Delivery Date |
|---|---|---|---|
| **A. Mutual information on relevant work programs** | | | |
| Bank work program in the next 12 months | **Analytical and Advisory Activities:**<br>1. Public Expenditure Review<br>2. Agriculture PER<br>3. Diagnostic Trade Integration Study<br>4. Rural Poverty Policy Note<br>5. Higher Education and Skills Development Policy Note<br>6. Decentralization Note<br>7. PPP Pipeline Screening Assessment<br>8. Update of Malawi Transport Costs Study<br>**Lending:**<br>1. First Programmatic Development Policy Operation (budget support)<br>2. Higher Education and Skills Development Project<br>3. Agricultural Productivity Program for Southern Africa (APPSA) | <br>Nov.<br>Sept<br>Nov<br>On-going<br>On-going<br>On-going<br>Work being finalized<br>TBA<br><br>Nov<br>Feb, 2013<br>December | <br>Aug 2013<br>Apr 2013<br>Aug 2013<br>Apr 2013<br>Jun 2013<br>Apr 2013<br>Jan 2013<br>Dec 2013<br><br>May 2013<br>Jul 2013<br>Mar 2013 |
| IMF work program in next 12 months | 1. First review of ECF-supported program.<br>2. Second review of ECF-supported program.<br>3. Third review of ECF-supported program.<br>4. Fourth review of ECF-supported program. | November, 2012<br>February, 2013<br>May 2013<br>November 2013 | December, 2012<br>March, 2013<br>June 2013<br>December 2013 |
| **B. Requests for work program inputs** | | | |
| Fund request to Bank | 1. Information on budget support and costing of social safety net programs. | | February-<br>March 2013. |
| | 2. Updates on Public Expenditure Review work. | | December 2012,<br>January 2013<br>August 2013 |
| Bank request to IMF | 1. Regular updates of medium-term macro projections. | | Continuous |
| **C. Agreement on joint products and missions** | | | |
| Joint products in next 12 months | 1. Debt Sustainability Analysis (update). | | March 2013 |

## ANNEX III. MALAWI—RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of October 31, 2012)

AfDB operations in Malawi date back to 1969. The Malawi Field Office was opened in 2007 and officially launched in July 2008 by AfDB President Dr. Donald Kaberuka. As at October 31, 2012, the Bank had provided significant and diversified support to Malawi, with cumulative commitments worth UA 775.6 million (about US$ 1.2 billion) to finance 95 operations including 11 studies and 2 lines of credit.

Currently, AfDB's assistance to Malawi is anchored on the Interim Country Strategy Paper (ICSP) covering 2011–12, which was approved by the Bank's Board of Directors on 11th May 2011. The ICSP was framed within the context of the Malawi Growth and Development Strategy (MGDS, 2006–11) and the Bank's Medium-Term Strategy (2008–12). The ICSP identified two pillars, infrastructure development and private sector development to be the focus of the Bank's development assistance to Malawi. During the ICSP period, the ADF XII allocation for Malawi for 2011 amounted to UA 70 million (about USD 108 million) with 44 percent of the resources provided as grants.

**Box 1. AfDB Ongoing Operations**

The Bank's ongoing operations comprise the following: two projects in the agriculture sector: Agriculture Infrastructure Support Project (AISP) and the Small-holder Crop Production and Marketing Project (SCPMPg). The Bank is also implementing the National Water Development Programme (NWDP) in collaboration with AusAID and the Water and Sanitation Access project for the Urban Poor in the City of Blantyre (grant from the African Water Facility) aimed at improving access to improved water supply and sanitation services. There are currently three projects providing support to the social sector: (i) the Health SWAp Programme which is constructing and rehabilitating a total of 57 health facilities across the country; (ii) the Education V project is rehabilitating and providing equipment in 18 Community Day Secondary Schools across the country; and (iii) the Local Economic Development project is developing infrastructure in four rural growth centres of Jenda, Malomo, Monkey Bay and Chitekesa. In the transport sector the Bank is implementing the Trunk Roads Rehabilitation Project which includes Blantyre-Zomba road rehabilitation project (60km), the Lilongwe Bypass construction project (13km) which is yet to commence and the Multinational Nacala Road Corridor. As at the end of October 2012, the overall disbursement rate was about 41 percent, a marginal increase from 39 percent recorded in December 2011. In line with the ICSP indicative program, the Bank approved two new operations, the Competitiveness and Job Creation Project in Private Sector (CJCSP), and the Higher Education, Science and Technology (HEST). The CJCSP was approved in December 2011 and HEST was prepared in 2011 and approved in February 2012.

Since the ICSP 2011–12 will expire at the end of 2012, the Bank is in the process of finalizing a full Country Strategy Paper (CSP, 2013–17) to be presented to the Board of Directors in January 2013. The new CSP is fully aligned to the second Malawi Growth and Development Strategy (MGDS II) covering the period 2011–16, the Bank's corporate priorities in the new Long Term Strategy (LTS, 2013–22) and the Regional Integration Strategy Paper for Southern Africa (Southern African RISP, 2011–15). The Bank has held extensive consultations with all relevant key stakeholders to determine the priorities for intervention. The new CSP will focus on two pillars: (i) addressing infrastructure bottlenecks to competitiveness and growth; and (ii) supporting actions to expand private sector investment and trade. To ease challenges posed by Malawi's landlocked position, the Bank will scale-up support to regional infrastructure to deepen the country's integration with its neighbors. Accordingly, more than 50 percent of the indicative lending operations are regional and will be financed with ADF XII, XIII and XIV resources. The Bank will also support Public Private Partnerships (PPPs) in infrastructure development.

Following Governments reengagement with the IMF and the approval of a new US$ 157 million Extended Credit Facility (ECF) arrangement for Malawi in July 2012, the Bank approved a new ADF Grant for the Crisis Response Budget Support operation for Malawi in July 2012, in the amount of US$ 40 million. The Bank designed a Restoration of Fiscal Stability and Social Protection (RFSSP) program whose objective is to contribute to restoring fiscal stability and enhancing public finance management in Malawi, 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. In order to support this agenda, the RFSSP has two components: (i) strengthened PFM transparency and accountability, and (ii) strengthened social protection system. The grant of US$40 million is the largest single tranche budget support provided by the ADF in Malawi. The Bank is encouraged by the government's renewed commitment to restoring and sustaining sound fiscal and monetary policy reforms for recovery and sustained growth.

The Bank has also provided support for non-lending activities, including feasibility studies and analytic work to inform the design of new operations and policy dialogue. Currently, the Bank is finalizing preparation of the Malawi Private Sector Profile.

## ANNEX IV. MALAWI—STATISTICAL ISSUES

### Introduction

1. Although economic data provision has some shortcomings, it is broadly adequate for surveillance.

2. The data module of the Report on the Observance of Standards and Codes (data ROSC), published February 17, 2005, found that, while the institutional framework for the production of macroeconomic statistics was broadly adequate, there were shortcomings in the scope, accuracy, and reliability of data. The weakest areas are: national accounts, balance of payments statistics, government finances statistics, and monetary and financial statistics. A key STA recommendation was to formally assign the responsibility for the compilation of government finance statistics to the Ministry of Finance and responsibility for the compilation of monetary statistics to the RBM.

3. The authorities are making efforts to improve the quality and timeliness of economic and financial data through participation in the Fund's General Data Dissemination System (GDDS) and the GDDS Project for Anglophone African Countries. Malawi is participating in the GDDS/PRSP and the monetary and financial statistics modules of the project. GDDS metadata have been posted on the Fund's Dissemination Standards Bulletin Board (DSBB) since February 2007.

### National accounts

4. The accuracy and reliability of the real sector data (including national accounts, prices, and trade) are affected by inadequate source data and timeliness. STA has recommended remedial actions, including the need for additional resources for the National Statistics Office (NSO). A long-term technical assistance program in the area of national accounts is being provided under a project by Norwegian counterparts. The NSO have revised the national accounts methodology to implement the SNA93 and to better account for the activities in the informal sector. New estimates for Real and Nominal GDP based on the base year 2007 are submitted.

### Consumer prices

5. A consumer price index (CPI) is available on a timely basis. The CPI base is 2000, drawing on the 1997/98 household survey, and data (on urban and rural price indices) are collected on a monthly basis by regional price collectors. There are plans to revise the CPI weights based on the 2010 planned Integrated Household Survey (IHS).

**Government finance statistics**

6. The accuracy and reliability of the data are affected by inadequate source data. A key shortcoming in this area is inadequate system of recording source data. In addition, there are serious quality problems, including data inconsistencies, that complicate program monitoring:

- While tax revenue data are received in a timely fashion, it is not always possible to reconcile them with deposits in the Malawi Government (MG) Account.

- Nontax revenue, including capital revenues collected by line ministries are not properly accounted for in the fiscal reports prepared by the Ministry of Finance.

- Data on recurrent expenditure suffer from serious shortcomings partly related to insufficient bank reconciliation between expenses records prepared by line ministries and financing information prepared by the Ministry of Finance. Line ministries submit spending reports to the Ministry of Finance based on recorded expenses, while the Ministry of Finances estimates expenses based on funding data (from the Credit Ceiling Authority). At times, there are sizable discrepancies between these two sources of data for both wages and other recurrent transactions—to some extent reflecting the widespread practice of reallocation across budget lines.

- Domestically financed development expenditure estimates are based on funding released to line ministries, and estimates on externally funded expenditure are based on reported project grants and loans. Owing to differences in timing and financing modalities (e.g., some donors require prefinancing of expenditure before reimbursement), there are substantial differences between the flow of expenses and corresponding financing data. In addition, many donor projects are still not incorporated in the budget, and hence the corresponding expenditure is not captured in government finance statistics. Some externally funded development expenditures are likely recurrent and reported capital expenditure therefore overstated.

- Data on expenditure arrears are likely incomplete, as reporting from the Commitment Control System appears to be only partial, and ministry level data are not consistent from report to report.

- Malawi's current budget classification includes economic and program classification and program, but does not include an effective administrative/organizational classification.[10] Expenditure data is loosely mapped to functional classification based on the CoFoG classification.

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[10] Economic classifications were upgraded to GFS 2001 compatible framework in FY 2006/07.

- The budget classification and chart of accounts may be adequate for some administrative, economic, functional and program classifications. An output-oriented activities-based budget classification (ABB) is used for the presentation of the budget. However, pro-poor expenditures that have been protected in line with the PRSP are only identified in the ABB classification. As no bridge table exists to map the ABB classification into the program classification used for expenditure reporting and accounting, pro-poor expenditures cannot be monitored. Under the ECF program, the government is expected to develop a mechanism for properly monitoring social expenditures.

- The government nomenclature program/subprogram currently used for the functional classification seems appropriate considering the nature of the items classified under this group. The items currently classified under this group include functions, programs and administrative levels. Although substantial elements of the current output based budget structure appear to be predominately functional in nature, it is not clear whether they are cleanly linked to classification of functions of government (CoFoG). As such, the government should review the current budget structure and the functional classification based on CoFoG (GFSM2001) to verify that they are aligned.

- The absence of a financial administrative structure, complete with vertical hierarchy of responsibilities inhibits the use of Government Finance Statistics (GFS). Budget funds are directed to organizations generally defined as cost centers (e.g., headquarters of ministries down to the level of secondary school principals). As such, there does not appear to be an effective hierarchal financial system. However, to be clear, over the past two years, sub-votes have been introduced to a number of Ministries, but not as yet, a system of warrants and sub-warrants have not been introduced.

- Financing estimates are based on monetary and debt data, rather than on government records of financing. Reporting on treasury bills directly issued to the RBM at times has been slow.

7. The authorities have received significant technical assistance from the Fund and other donors to strengthen expenditure monitoring and reporting, accounting, and statistical reporting, but results have lagged. The government has pledged to strengthen public financial management and fiscal reporting, and renewed efforts are being made to establish a work plan, including utilizing donor technical assistance more effectively. The authorities are currently working with East AFRITAC to modify its chart of accounts and output-based structures so that they could more easily be realigned to the national strategy and can be readily understood.

8. Government finance data are not reported for publication in the *Government Finance Statistics Yearbook (GFSY)* or the *International Financial Statistics (IFS)*. An August 2005

and August 2007 STA mission that visited Lilongwe reiterated the importance of continued efforts to implement the Integrated Financial Management Information System (IFMIS), and encouraged the authorities to improve the coverage and sectorization of government financial operations and to correctly classify transactions according to international guidelines. The mission proposed, and discussed with the authorities, a migration plan and timetable to adopt the *GFSM 2001* methodology.

9. A GFS TA mission visited Lilongwe in June 2011 in the context of the country's participation in the GFS Module under the Enhanced Data Dissemination Initiative funded by DFID. It found that annual and sub-annual data for budgetary central government are compiled in *GFSM 1986* format of the Ministry of Finance, but are not disseminated. A new chart of accounts aligned with the *GFSM 2001* was introduced in the 2011–12 budget cycle, which applies to all general government units. A number of source data issues were identified and recommendations made to address them. Bridge tables linking the national classifications and *GFSM 2001* classifications were prepared by the mission, and should be revised and used to compile GFS in *GFSM 2001* format. A follow up mission is included in the RAP for FY 2013.

**Monetary and financial statistics**

10. Despite recent improvements, monetary and financial statistics (MFS) continue to have shortcomings. These includes irregular reporting to STA, lack of proper legislation to grant the authority to the RBM to require reporting from other institutions[11]; the sectorization of the domestic economy, and classification of financial instruments to ensure that the RBM adheres fully to the methodology of the *Monetary and Financial Statistics Manual*. The 2004, 2008, 2009, and 2010 missions noted and made a number of recommendations for addressing the above shortcomings. In addition to the above tasks, the 2008, 2009, and 2010 STA missions assisted RBM staff in developing the standardized report forms (SRFs) for the central bank accounts (1SR), other depository corporations (2SR), and monetary aggregates (5SR).

**External sector statistics**

11. The external sector statistics in Malawi exhibit serious deficiencies. Concepts and definitions used to compile the balance of payments statistics are in broad conformity with the guidelines presented in the fourth edition of the *Balance of Payments Manual* (*BPM4),* although there has been some progress in the transition to the methodology of *BPM5*. The National Statistical Office of Malawi (NSO) should now adopt the *BPM6* methodology, on the basis of which the Malawi balance of payments metadata should also be updated. Balance of payments data remain weak in a number of key areas. The NSO balance of payments

[11] Some legislation that is designed to address this issue has recently been approved. However, some of the pending legislation would give and strengthen the authority of the RBM in this regard.

section remains crucially understaffed, as it has been since March 2008. Moreover, important data sources for balance of payments compilation ceased to be available during 2006–07, for example exchange control forms, which could supply information on imports of goods, services, and current transfers. Procedures for assessing the accuracy of trade data need to be improved.

12. The NSO had compiled new balance of payments data and validated the results from two key surveys: the BOP Survey and the survey on nonprofit institutions serving households (NPISH), both based on the *BPM*5 methodology. The NSO also compiled information from other important sources as well, namely: a) the 2009 Foreign Private Capital and Investor Perception Survey, b) monetary statistics from the Reserve Bank of Malawi (RBM), and c) other financial data provided by the Ministry of Finance (MoF). However, much remains to be done to improve the quality, coverage, and timelines of the balance of payments statistics.

13. Data on remittances are non-existent, despite anecdotal evidence that there are high remittances. As a first step the money transfer services should be required to report monthly data to the RBM. Data on foreign direct investment and portfolio flows are similarly weak. Project aid is currently classified as current transfers rather than in the capital account, and several large in-kind projects are not captured in the balance of payments data properly.

14. No international investment position statement is prepared. The RBM and Ministry of Finance's Debt and Aid Department need to improve reporting of monetary and external debt data respectively.

## Malawi: Tables of Common Indicators Required for Surveillance

(As of November 30, 2012)

| | Date of latest observation (For all dates in table, please use format dd/mm/yy) | Date received | Frequency of Data[7] | Frequency of Reporting[7] | Frequency of Publication[7] | Memo Items:[8] | |
|---|---|---|---|---|---|---|---|
| | | | | | | Data Quality – Methodological soundness[9] | Data Quality – Accuracy and reliability[10] |
| Exchange Rates | Current | Current | D | D | D | | |
| International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1] | 10/2012 | 11/2012 | M | M | M | | |
| Reserve/Base Money | 10/2012 | 11/2012 | M | M | M | LO, LO, LNO, O | LO, O, O, O, O |
| Broad Money | 10/2012 | 11/2012 | M | M | M | | |
| Central Bank Balance Sheet | 10/2012 | 11/2012 | M | M | M | | |
| Consolidated Balance Sheet of the Banking System | 10/2012 | 11/2012 | M | M | M | | |
| Interest Rates[2] | 10/2012 | 11/2012 | M | M | M | | |
| Consumer Price Index | 10/2012 | 11/2012 | M | M | M | O, LNO, O, O | LNO, O, O, O, NA |
| Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4] | 09/2012 | 10/2012 | M | M | I | O, LO, O, O | O, LO, O, O, LNO |
| Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government | 09/2012 | 10/2012 | M | M | I | | |
| Stocks of Central Government and Central Government-Guaranteed Debt[5] | 09/2012 | 10/2012 | M | M | M | | |
| External Current Account Balance | 09/2012 | 10/2012 | A | A | A | O, O, O, O | LO, O, LO, O, O |
| Exports and Imports of Goods and Services | 09/2012 | 10/2012 | A | A | A | | |
| GDP/GNP | 09/2012 | 10/2012 | A | A | A | LO, LNO, LNO, LO | LNO, LNO, LO, LO, LNO |
| Gross External Debt | 2011 | 6/2012 | M | I | I | | |
| International Investment Position[6] | NA | NA | NA | NA | NA | | |

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

[8] These columns should only be included for countries for which Data ROSC (or a Substantive Update) has been published.

[9] Reflects the assessment provided in the data ROSC or the Substantive Update (published on March 10, 2004, and based on the findings of the mission that took place during May 8–21, 2003) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording, respectively, are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).

[10] Same as footnote 9, except referring to international standards concerning, respectively, source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No.12/498
FOR IMMEDIATE RELEASE
December 19, 2012

International Monetary Fund
Washington, D.C. 20431 USA

**IMF Executive Board Completes First Review Under the Extended Credit Facility for Malawi and Approves US$20 Million Disbursement**

The Executive Board of the International Monetary Fund (IMF) completed today the first review of Malawi's economic performance under a program supported by the Extended Credit Facility (ECF). The Board's decision enables the immediate disbursement of an amount equivalent to SDR 13.02 million (about US$20 million), bringing total disbursements under the program to an amount equivalent to SDR 26.04 million (about US$40.1 million).

In completing the review, the Executive Board approved a request for a waiver of the nonobservance of the end-September 2012 performance criterion on the level of net domestic assets of the Reserve Bank of Malawi (RBM). The three-year ECF arrangement for Malawi in the total amount of SDR 104.1 million (about US$xxx million) was approved on July 23, 2012 (see Press Release 12/273).

Following the Board's discussion, Mr. Naoyuki Shinohara, Deputy Managing Director and Acting Chair, issued the following statement:

"Drought in parts of Malawi lowered overall growth in 2012, and threatened the subsistence of nearly 2 million people. A spike in food prices and the continuing depreciation of the kwacha contributed to a surge in inflation. The external economic environment has also been more difficult than anticipated. Despite these challenges, performance under the Fund-supported program has been satisfactory.

"Tight monetary and fiscal policies are needed now to stabilize the exchange rate and curb inflation. Accordingly, the Reserve Bank of Malawi (RBM) has appropriately discontinued a temporary facility for uncollateralized lending to banks and increased the policy rate in early December. Fiscal policy is also playing a role, including with the reactivation of the automatic adjustment mechanism for fuel prices which has cut untargeted subsidies that mainly benefit the better off. The bulk of the additional external financing provided by Malawi's development partners will allow the government to increase outlays on social protection programs without increasing domestic borrowing, although the authorities are well advised to save a portion of those grants to build up international reserves from very low levels.

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"The RBM has stepped up its oversight of banks with a view to addressing emerging threats to the stability of the financial system. It is paying particular attention to ensuring that banks facing persistent liquidity problems implement restructuring plans that put them back on a sound financial footing.

"The authorities are making good progress in implementing a wide range of structural reforms. On the budget side, reforms focus on strengthening tax and customs administration, as well as improving public financial management though greater expenditure control and the prevention of arrears. The authorities have also committed to removing regulatory hurdles to improve the investment climate and foster sustained and broad based growth."

**Statement by Mr. Momodou Bamba Saho, Executive Director for Malawi**

**December 19, 2012**

We thank staff for the excellent report and for their efforts to assist the Malawi authorities in the implementation of the Extended Credit Facility (ECF). My Malawi authorities would like to thank staff and Management for their candid assessment of recent economic developments and constructive dialogue and their support for Malawi's request for completion of the first review under the ECF. They are especially thankful to the Executive Board and Fund Management for their continued support and valuable policy guidance against the backdrop of a very difficult domestic and global economic environment.

In view of the good performance under the program—with end-September 2012 quantitative performance criteria observed except for the level of the RBM's net domestic assets (NDA) target as a result of the RBM's extension of liquidity support to the banking system, and implementation of structural reforms on track—they request Directors' support for the completion of the first review under the ECF and waiver of the nonobservance of the missed performance criterion. In addition, my authorities request for modification of performance criteria for the second and third reviews (test dates of end-December 2012 and end-March 2013, respectively) on the basis of a worse external environment than envisaged when the program was designed, a tightening of policies by the authorities, and additional donor support. My authorities want to assure the Executive Board that they will continue the policies agreed under the current Fund-supported economic program.

Malawi is at a historic crossroads. The government headed by President Joyce Banda has been implementing tough but critical macro and structural reforms aimed at turning around the economy. Among other things, these include devaluation of the Kwacha by close to 50 percent, then allowing it to float and the adoption of an automatic adjustment mechanism for retail prices of fuel. The economy however remains fragile, with further depreciation of the Kwacha by an additional 30 percent so far, triggering fluctuations in the prices of fuel. In addition to the reforms, the government has launched an 18 month Economic Recovery Plan (ERP) that focuses on a few priorities that are "pro-growth, represent quick wins, and are highly effective" and necessitates for social protection programs (Farmer Input Support Program and other assistance to small farmers, public works, school feeding, scholarships for girls, cash transfers). The plan also identifies diversified commercial agriculture, tourism, energy, mining and infrastructure/Information Technology and Communications as sectors that can help turn around the economy and provide the initial building blocks towards structural transformation, needed to successfully implement the Second Malawi Growth and Development Strategy (MGDSII.)

## Economic Development Under the ECF

The macroeconomic environment is still fragile and achieving stability remains the overarching goal for my authorities through the continuance of the policy measures instituted so far. The growth estimate for 2012 was revised downwards from 4.3 percent earlier in the year to 1.9 percent owing to drought conditions in some parts of the country contributing to lower crop production and a spike in inflation, highlighting the urgent need for expediting food redistribution.

Driven by increases in fuel and domestically produced food prices as well as continuing depreciation of the exchange rate, the rate of inflation rose to 30.6 percent in October 2012, up from 28.3 percent during the preceding month and 9.8 percent at the beginning of the year. In addition, reflecting the decline in foreign exchange reserves and the increasing inflationary expectations, the Kwacha continued to depreciate faster than anticipated. These developments necessitated the need for measures that would stabilize the Kwacha in order to anchor inflation expectations. To this end, the RBM raised the Bank rate by 400 basis points to 25 percent in November which is in line with developments in both non-food inflation and the Treasury bill yield while keeping the Liquidity Reserve Requirement (LRR) at 15.5 percent. The RBM also closed on November 30th the uncollateralized lending window that it was extending to banks that have relied for a long time on borrowing from the RBM or interbank market to meet LRRs and has placed these banks under heightened scrutiny to ensure that they are on a path to meeting prudential liquidity requirements. The RBM also conducted open market operations to withdraw liquidity as part of its efforts to stabilize the exchange rate.

**Outlook and policies going forward**

Going forward, my authorities remain committed to the current exchange rate regime that allocates foreign exchange through a market-based system. They are also committed to continue modernizing the exchange rate and monetary policy framework.

On the fiscal side, the authorities have decided to tighten further their fiscal stance by committing to a repayment of 1.3 percent of GDP compared to the zero domestic borrowing as was initially planned at the inception of the program. They deem this necessary in order to ensure early attainment of macroeconomic stability. They will also continue to enhance domestic revenue mobilization, strengthen the public financial management systems and reiterate their commitments as outlined in their MEFP.

My Malawi authorities' commitment to the implementation of a wide range of reforms underpins the current program's objectives. Creating an enabling environment for private investment and growth is high on their agenda. Improving the stock and quality of infrastructure is a priority with the aim of enhancing productivity in the primary sectors and competitiveness of the country as a whole. In addition, they aim at expanding and ensuring quality health and education services towards meeting MDGs targets as well as ensuring food security at household and national levels. They also intend to review regulatory hurdles to doing business in Malawi and enhancing the country's international competitiveness.

The conclusion of the ECF's first review is a major achievement. Going ahead, my authorities are fully aware that continued effort is necessary, with the ultimate objectives of stabilizing the macroeconomic environment and restoring sustained inclusive growth. To this end my authorities intend to implement all the measures needed to fully meet the program's targets as well as to adjusting their economic policies for the near term to deal with the emerging challenges and cement macroeconomic stability. They plan to continue directing their fiscal, monetary, exchange and debt policies toward achieving their near-term objectives of high growth, single digit inflation and building up of foreign reserves. In this regard, my authorities will continue to consult with the Fund and seek the support of development partners in formulating their policies. They foresee the continued Fund support to be an essential and timely input that will help them to sustain their effort to maintain macroeconomic stability and lay the foundation for enhanced growth over the medium term.

In closing, I wish to extend my authorities' appreciation for the hard and diligent work of the Fund staff, both on the ground and on mission, and for their patience and professionalism that has made the difficult road so far a good basis for the success of the new program.