INTERNATIONAL MONETARY FUND

MALAWI

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FIFTH AND SIXTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR WAIVERS FOR NON-OBSERVANCE OF PERFORMANCE CRITERIA, EXTENSION OF THE ARRANGEMENT, MODIFICATION OF PERFORMANCE CRITERION, AND REPHASING OF DISBURSEMENTS—DEBT SUSTAINABILITY ANALYSIS

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This debt sustainability analysis for low-income countries (DSA) confirms a moderate risk of external debt distress for Malawi. Except for the present value of external public debt to GDP—which displays a marginal and temporary breach during 2014–15, external debt burden indicators remain below their indicative thresholds under bound tests conducted to show the impact of temporary shocks. However, total public debt has increased substantially in recent years. In the context of a weak institutional environment, such rapid growth of public debt poses a heightened overall risk of debt distress.

BACKGROUND

1. **The last Low Income Country Debt Sustainability Analysis (LIC DSA, IMF country report no. 14/37) conducted in late 2013 concluded Malawi's external public debt faced moderate risk of distress.** All external public debt and debt burden indicators for Malawi were envisioned below their respective thresholds under the benchmark and other scenarios. The baseline envisioned strong enough fiscal and public financial management (PFM) policies that would result in resumption in donor budget support by the end of the 2013/14 fiscal year, but this did not materialize.

2. **The country policy and institutional assessment (CPIA) score for Malawi has deteriorated, changing the category of its policies and institutions to weak, and tightening debt thresholds for DSA analysis.** The CPIA score of Malawi peaked at 3.4 in 2007 but has continuously deteriorated since then and reached a level of 3.1 by 2013, compounded by erosion in the effectiveness of public financial management systems, controls and oversight mechanisms. Relative to the previous DSA, weak policies and institutions as measured by this index resulted specifically in lower thresholds for external public debt relative to the ones used in the previous DSA.[1]

3. **Malawi's public and publicly guaranteed (PPG) gross debt changed from 57% of GDP in 2012 to 72.1% of GDP in 2013 and is expected to reach about 76% of GDP in 2014, reflecting continued increases in both, domestic and external public debt.** The increase in debt reflected in part (two-thirds of the change from 2012 to 2013) recourse to domestic financing in the wake of external financing shortfalls arising from the suspension of external budget support by donors in the wake of weaknesses revealed by a large public financial management scandal. Popularly known as "cashgate", this scandal involved multiple cases of embezzlement of public funds by a number of officials of the government. The increase in total public debt in 2014 also resulted in part from the recognition of significant past payment arrears. A decline in government current expenditures as ratio to GDP and improved domestic revenue performance were insufficient in offsetting the ongoing lack of direct budget support from development partners. A detailed decomposition of the dynamics of domestic and external public debt is discussed below.

Text Table 1. Malawi: Composition of total public Debt, 2012–14

(Percent of GDP)

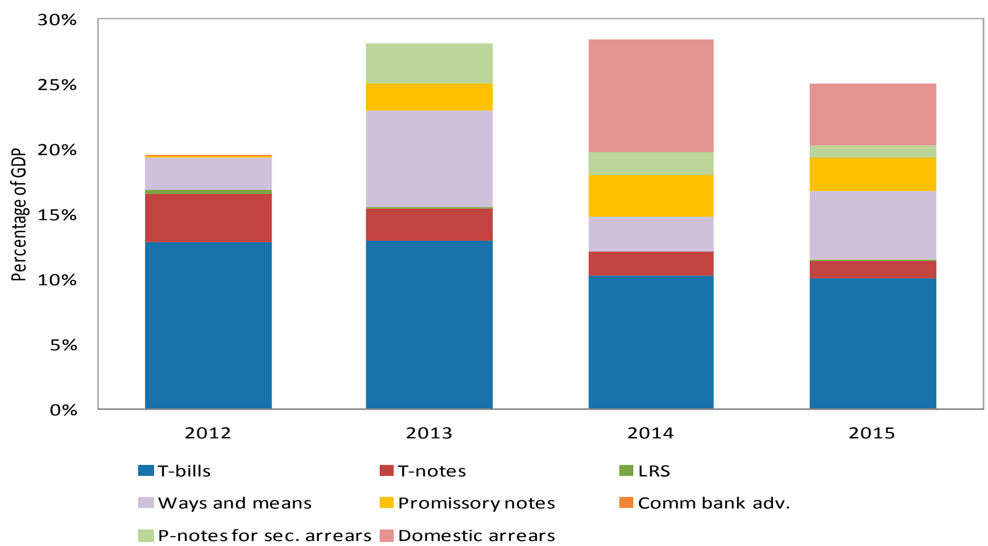
	2012	2013	2014
External debt	37.7	44.0	47.3
Domestic Debt	19.5	28.1	28.5
Total public Debt	57.2	72.1	75.8

Sources: Malawian Authorities and IMF Staff Estimates.

[1] The new thresholds for the indicators related to the present value of public and publicly guaranteed external debt are: 30 percent as a ratio to GDP (down from 40 percent); 100 percent as a ratio to exports (down from 145 percent); and 200 percent as a ratio to revenue (down from 250 percent). Similarly, the thresholds for debt service indicators changed from: 20 to 15 percent, as a ratio to exports, and from 20 to 18 percent as a ratio to revenue.

4. Gross domestic debt increased from MK206.6 billion (19.5% of GDP) at the end of 2012 to MK515 billion (28.5% of GDP) at the end of 2014. As illustrated in Figure A1, this increase is largely due to (i) the rise in the use of ways and means advances from the Reserve Bank of Malawi in 2013 and 2014, following the drop in external financing in the wake of the "cashgate" scandal; (ii) the recognition in late 2014 of pre-audited arrears amounting to MK157 billion (8 percent of GDP) accumulated from previous fiscal years; (iii) the issuance of promissory notes in the amount of MK29 billion (1.6 percent of GDP) by the government to the central bank (RBM) in April 2014 to cover losses arising from the 2012 devaluation of the exchange rate. Gross domestic debt as a percent of GDP is projected to gradually decline from 25 percent of GDP at end-2015 to 15 percent of GDP at end-2020, helped by (i) the repayment of accumulated domestic arrears; (ii) the decline in new ways and means advances as the government's fiscal position improves; and (iii) a projected slower pace of new issuance of Treasury bills and Treasury notes over the long term (due to a lower government deficit).

Figure A1. Composition of the Stock of Gross Domestic Debt



Sources: Malawi authorities and IMF staff calculations

5. Malawi's external public debt increased from US $1.15 billion in 2012 (37.7% of GDP) to US $1.45 billion on 2013 (44% of GDP) and is estimated to have reached US $1.86 (47.3% of GDP) billion in 2014.. The increase of 2013 reflects a continuation of strong external borrowing that resumed in 2012. In terms of GDP half of the increase of the change from 2012 to 2013 can be attributed to exchange rate effects.[2] External support was then subdued in late 2013. During 2014 external public debt increased further, but about half of the increase was due not to accumulation of new debt, but to the sale of existing domestic debt to PTA bank, a regional development bank serving the members of the Common Market of East and Southern Africa (COMESA). The debt was reclassified as external based on the residency criterion despite the debt being denominated in local currency. In terms of source of financing, as illustrated in Table 1 below, most of Malawi's debt is from multilaterals.

[2] The year-on-year Kwacha-Dollar exchange rate depreciated by about 30% in 2013. External debt is converted in Kwacha using end of period exchange rate, which was about 15% higher than the average exchange rate.

Text Table 2. Composition of Total Public and Publicly Guaranteed External Debt
(US$ Millions)

	2012	2013		2014	
	Actual	Actual	Share	Proj.	Share
Total	1149.5	1447.38	100%	1857.4	100.0%
Multilaterals	882.7	1015.2	70%	1365.2	74%
IMF	180.9	198.2	14%	218.2	12%
IDA	322.9	416.5	29%	456.5	25%
ADF	171.2	190.9	13%	210.9	11%
IFAD	77.6	75.6	5%	75.6	4%
Other Multilateral[1]	130.1	134	9%	424.0	23%
Bilateral	266.8	412.5	28%	472.5	25%
France	10.4	10.8	1%	10.8	1%
Belgium	2.2	2.2	0%	2.2	0%
People's Republic of China	175.5	252.4	17%	282.4	15%
India	78.7	106.2	7%	136.2	7%
Others	0	40.9	3%	40.9	2%
Commercial	0	19.7	1%	19.7	1%

Sources: Malawian authorities and staff estimates

[1]The 2014 stock includes US$250 million resulting from the sale of existing government debt to a regional development bank.

6. The scope of debt covered in the present DSA encompasses public and publicly guaranteed debt.

UNDERLYING DSA ASSUMPTIONS

7. Macroeconomic and policy developments during 2013 and 2014 resulted in several areas of underperformance, relative to the projections in the 2013 DSA. Donors withdrew budget support in 2013 and this when combined with weak commitment controls (which were exacerbated in the run up to elections), contributed to increased domestic borrowing, domestic payment arrears and an acceleration in inflation. Economic activity remained resilient, with real GDP estimated at 5½–6 percent range in 2014. The ready availability of foreign exchange and fuel, as a result of policy reforms introduced in May 2012, appears to have supported the expansion of economic activity. The exchange rate came under considerable depreciation pressure in the latter stages of 2014. This was in part a seasonal phenomenon, as the rate usually weakens after the end of the tobacco buying season in August. However, it was particularly acute this time, owing to the unattractive level of real interest rates. The exchange rate begun to stabilize since the stance of monetary policy was tightened in November and the RBM acquired foreign exchange from the debt restructuring operation with PTA.

8. The baseline scenario and macroeconomic outlook have been revised accordingly. For Fiscal year 2014/2015, government expenditures in goods and services, wages, and development are projected 2 percentage points of GDP lower than in the previous DSA. Monetary policy is also expected to remain tight, to support the disinflation process. Tighter policies, and lower than expected worldwide growth, led to revisions in GDP growth forecasts for 2014 and 2015 to 5.7 percent and 5.5 percent, respectively (from 6.1 percent and 6.5 percent in the previous DSA). Long-term GDP growth is assumed at 6 percent. The baseline scenario also maintains the assumption of a gradual reduction in the external current account deficit through export diversification and reliance on grants and concessional financing in the medium term. The merchandise trade balance is expected to improve during 2014 and 2015 relative to the previous DSA, on account of favorable terms of trade and the continued depreciation of the Kwacha. Inflation is programmed to return to single digits by 2016. Targets on international reserves have been met during the program, and a 3 months of import cover is expected to be attained and sustained (or improved) by end-2015. The key macroeconomic assumptions are summarized in Box 1.

Box 1. Baseline Macroeconomic Assumptions

Real GDP is projected to grow at an annual rate of about 6 percent over the longer term, led by the agriculture, trade, manufacturing and mining sectors, and supported by a more competitive exchange rate, structural reforms, and gradually recovering donor support.

Inflation is projected to decline from 24.2 percent by end of the period 2014 to 12 percent by December 2015 and to reach single digits by 2016 as the emphasis of monetary policy switches from accumulation of international reserves to price stability.

The exchange rate is projected to remain constant in real terms after 2015.

Tax revenue is projected to continue increasing with ongoing reforms in tax administration and policy.

External public debt and financing sources. Debt will be contracted mainly from multilateral creditors on concessional terms, with borrowing from bilateral sources also on broadly similar terms. Budget support from development partners is assumed to remain subdued for FY 2014/15 and into the medium term. Project support in the short and medium term is assumed to remain strong (but lower than previously considered). Foreign direct investment is still assumed to be in the 3–4% of GDP range in the short to medium term as strong reforms bring back confidence, while the longer term levels are as in previous DSA analyses, in the range of 1–2% of GDP.

The current account balance will remain at a sustainable level, as improvements in the trade of goods and services balances partially offset the decline in grants.

Text Table 3. Macroeconomic Forecasts and Assumptions (Previous and Current DSA)

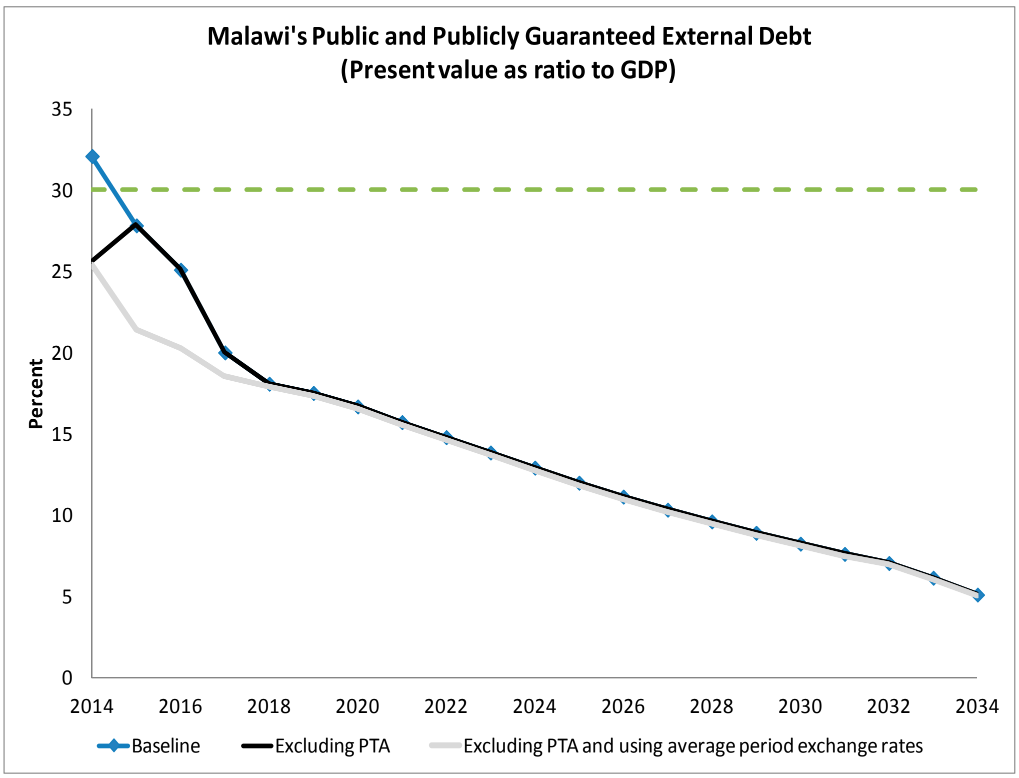
	Real GDP growth		Primary deficit (percent of GDP)		Change in public debt (percent of GDP)	
Year	Previous	Current	Previous	Current	Previous	Current
2013	5.0	5.2	1.2	1.9	12.0	14.9
2014	6.1	5.7	-1.3	-1.6	-13.5	3.7
2015	6.5	5.5	-0.4	-0.9	-5.5	-15.5
2016	6.5	5.7	-0.9	-3.1	-4.3	-3.3
2017	6.2	6.0	0.1	-2.4	-3.2	-6.2
2018	6.3	5.9	0.1	-0.9	-5.1	-1.1
2019	5.9	5.8	1.2	-1.2	-3.1	-1.9
2020	5.8	5.9	1.0	-0.5	-3.5	-1.9
2021	5.9	5.9	1.4	-0.6	-2.3	-1.9
2022	5.9	6.0	1.4	-1.1	-1.9	-2.2
Avg 2023-2034	5.9	6.0	1.2	1.0	-0.2	-2.0

Sources: Malawian authorities and IMF staff calculations and projections.

EXTERNAL PUBLIC DEBT SUSTAINABILITY

9. Except for the present value (PV) of external public debt to GDP, which displays a marginal and temporary breach during 2014–2015, external debt indicators for Malawi remain below their new tighter limits. Malawi's external public debt continued expanding through 2013 and, in present value terms, is estimated to reach 32.2% of GDP by the end of 2014. The resulting breach in the corresponding debt threshold (of 30%) is, nevertheless, expected to be marginal and short lived. As illustrated in Figure A2 below, this breach was due to the aforementioned restructuring of existing domestic debt to PTA bank. The interest rate would be lower by 1000 basis points as a result of the restructuring, resulting in lower debt service costs. PTA bank finances letters of credit for exports in Malawi on a regular basis and thus benefits from the resulting liquidity. In addition to this restructuring operation, the depreciation of the exchange rate during the last quarter of 2014, which appears to have subsided in recent times, also played an important role in causing the breach in the PV of debt to GDP threshold.[3]

Figure A2. Malawi's Public and Publicly Guaranteed External Debt



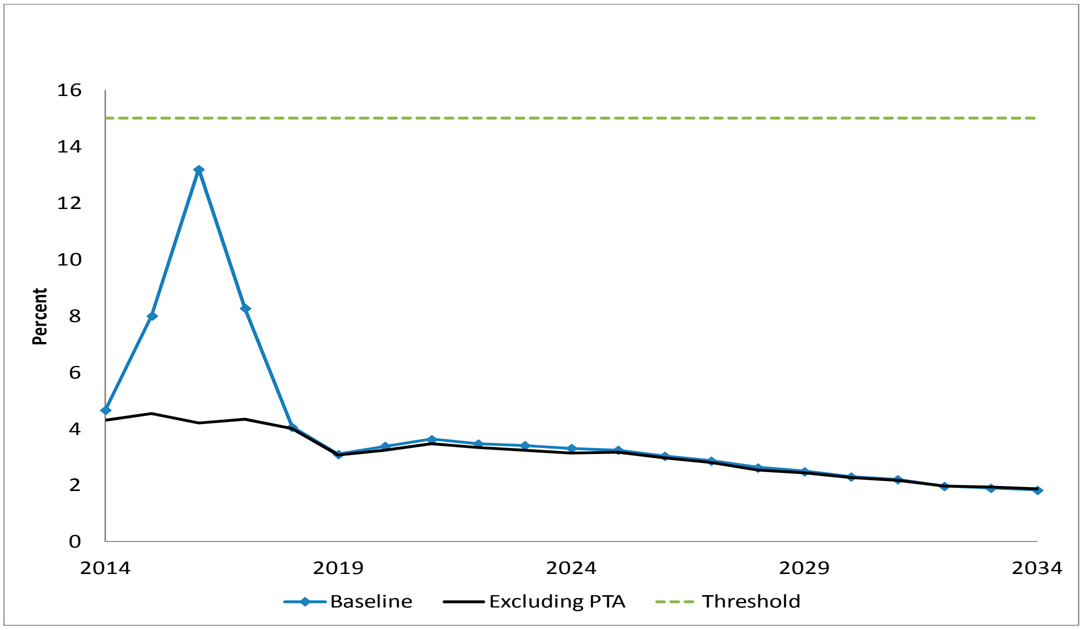
Sources: Malawian Authorities and IMF Staff Calculations

[3] The DSA template employs end of period exchange rate to compute present value of flows of debt service. Of course, not all debt service occurs at the end of the period. In times with sharp exchange rate movements, this artificially inflates external debt indicators. Indeed, Figure A2 shows if one used average exchange rates the threshold for PV of PPG external debt would not be breached.

Another noticeable change, relative to the dynamics of debt in previous DSA, is that, due to the short maturity (3 years) of the loan with PTA, noticeable peaks in debt service emerge during 2015–16.[4] An illustration of debt service trends in the baseline, and excluding PTA is presented in Figure A3. Restrained fiscal and monetary policies, together with PFM reforms envisioned in the current ECF (Extended Credit Facility) program should contribute to a downward trend in key debt indicators.

Figure A3. Malawi's Public and Publicly Guaranteed External Debt Service

(Debt Service as Ratio of Exports)



Sources: Malawian Authorities and IMF Staff Calculations

10. Except for the present value of external public debt to GDP, debt burden indicators remain below their indicative thresholds under bound tests conducted to show the impact of temporary shocks. The strongest impact on the present value of external public debt to GDP requires the combination of shocks to growth, exports and non-debt creating flows (See Table 4a, case B5). In turn, a shock to exports (Table 4a, case B2) is the only shock that could bring a marginal breach in the debt to exports ratio while none of the bound tests considered results in a breach of threshold for the present value of debt to revenue ratio.

STRESS TESTS

11. Standard stress tests indicate that a somewhat weaker debt outcome is possible under certain conditions (Figure 1). Specifically, the present value of debt to GDP ratio remains above its indicative threshold when key variables are kept at their historical levels. This behavior is mostly due to the inclusion of 2012 in the historical period, which effectively allows the exchange rate depreciation in that year to continue to impact nominal GDP in U.S. dollars. The staff considers this to be an unlikely outcome due to authorities' actions to reduce fiscal dominance.

[4] It is important to note that restructuring of debt is not subject to the zero-limit on non concessional external debt.

PUBLIC DEBT SUSTAINABILITY

12. **Total public debt has increased substantially and, in present value terms, stands seventeen percentage points of GDP higher than the recommended benchmark.** Domestic debt has expanded in recent years, in part to cover for the decline in traditional budget support from development partners, but also due to weaknesses in public financial management that gave rise to arrears and budget overruns.[5] By 2013 the present value of total public debt stood at 55.9 percent of GDP, and is expected to peak at 60.7 percent by the end of 2014, partly due to new uncovered arrears (157 billion KW), and in part due to issuance of securities to recapitalize the central bank (29 billion KW). The strong PFM reforms, monetary and fiscal policies envisioned in the present ECF program should contribute towards restoring donor confidence (and bring back external financing), and keeping expenditures within the available fiscal envelope. Domestic debt as a share of GDP is set to decline with fiscal consolidation and the maintenance of a positive primary balance. Standard stress tests suggest that the debt dynamics would deteriorate relative to the baseline (Figure 2 and Table 2). The strongest impact on the indicators arises from a one-time real depreciation shock—again through compression of nominal GDP in U.S. dollars—and an export shock, which is illustrative of the risk inherent in the undiversified nature of Malawi's sources of foreign exchange.[6]

13. **External financing risks exist, but are projected to be addressed by additional fiscal restraint and so should not have an impact on debt.** Budget financing needs required, as in FY2013/2014, an expansion of domestic debt for fiscal year 2014/2015. Fiscal tightening is expected to be the policy response to unexpected negative financing shocks (either from delayed or lower donor support, or lower tax revenue). Additional domestic borrowing would bring additional pressures on the exchange rate and erode perceptions of government commitment to policy reforms, ultimately damaging macroeconomic performance and should be avoided. The authorities should look for additional cuts in domestically financed development expenditure and in goods and services to meet additional shortfalls in external financing. Risks to this include the delicate balance of maintaining macroeconomic stability, versus maintaining core public services – especially for the poor – should government struggle to raise sufficient domestic revenue and/or fail to see a resumption of budget support. Similarly, the government may have to continue confronting political economy challenges of reducing expenditure in politically charged areas, such as fertilizer subsidies, wages and salaries, etc.

14. **Malawi's external public debt remains at moderate risk of debt distress.** However, rapid accumulation of debt and deterioration in the strength of the policy and institutional framework (as measured by the CPIA score) urge prudent debt management policies to guarantee the sustainability of debt.

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[5] It is important to note that, relative to the previous DSA for Malawi, the current analysis reflects bringing a large amount of arrears that were previously off-budget on to the budget through securitization.

[6] In this analysis, the combination bound test B5 (Tables 4a and b) was modified to exclude the non-debt creating flows component. This component was removed as Malawi lacks the access to capital markets required to replace lost grants and foreign investment with borrowing, and would instead be forced to respond with expenditure and import compression.

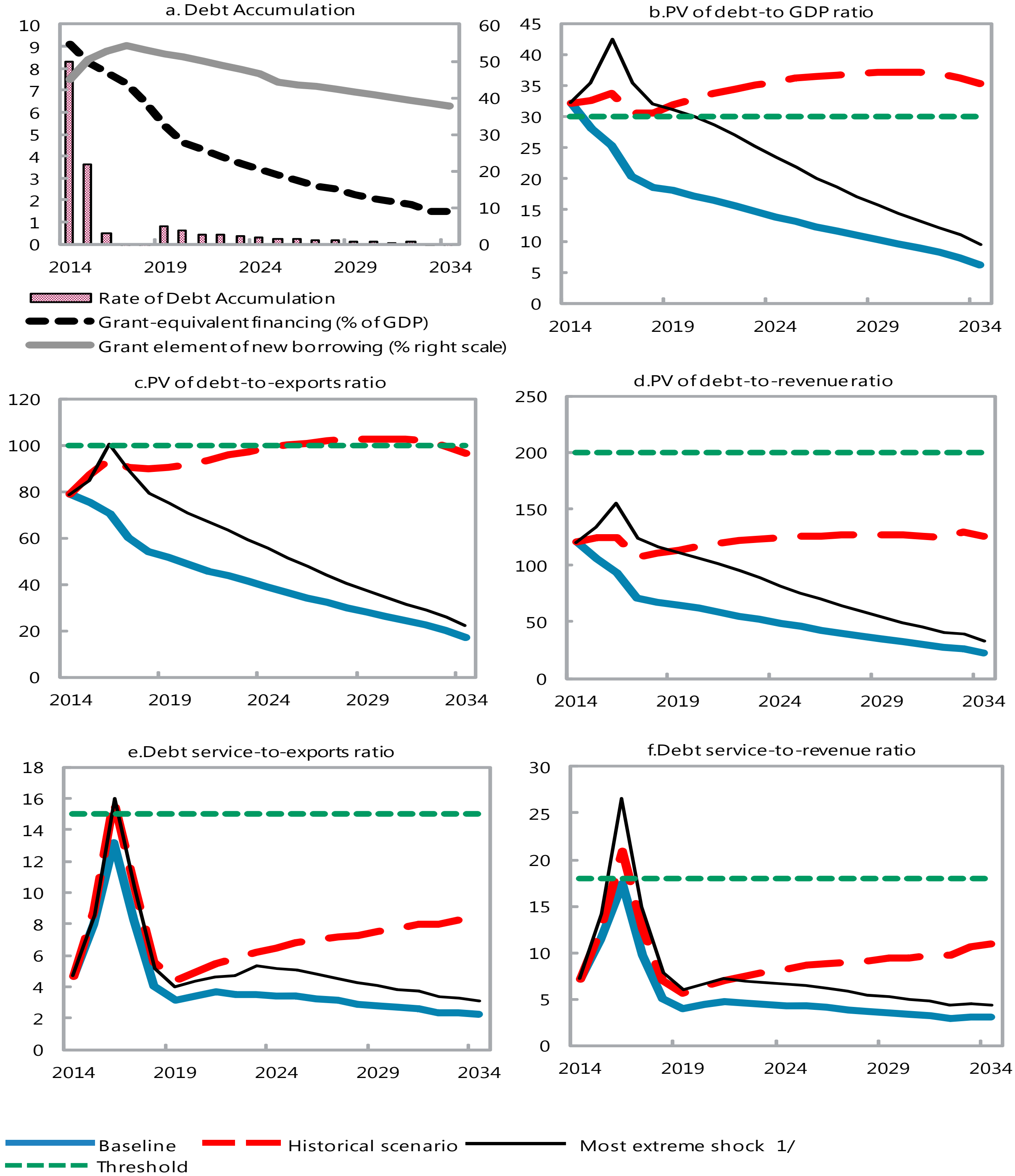
15. Authorities' views. The authorities recognized that Malawi's external public debt to GDP ratio has been growing and is expected to reach 32.2 percent of GDP in net present value terms at end-2014. Nonetheless, they noted that this is not expected to worsen the debt dynamics significantly, as external public debt remains mostly concessional. They pointed out that external public debt service burden remains low, with a debt service ratio in 2014 of only 4.7 percent of exports of goods and services. However, they acknowledged that domestic debt burden is becoming more worrisome and that domestic debt accumulation increased, in part, due to the fact that the "cashgate" scandal resulted in annual shortfalls in external disbursements amounting to almost 6.6 percent of GDP. Furthermore, the authorities noted that their PFM systems proved too weak to enforce the discipline needed to follow the adjustment path agreed under the program. By the end of the 2013/14 fiscal year, domestic financing had increased to about 6 percent of GDP. The authorities emphasized efforts to regularize these and additional payment arrears accumulated from previous years and reforms geared towards strengthening commitment controls.

16. The authorities viewed 2015 as a year to consolidate debt and lay the groundwork for a period of sustained noninflationary growth. In this regard, they envisaged real growth in 2015 to reach 5.5 percent (one percentage point lower than anticipated in the December 2013 MEFP) and to gradually increase to 6 percent in 2017. Inflation will decline to 12.5 percent by end-2015 and to single digit levels towards end-2016. Fiscal restraint and a reliance on concessional foreign borrowing for the majority of financing needs will allow some reduction in the stock of domestic debt relative to GDP to take place. Strong debt management in the near-to medium term will be implemented to ensure that debt is sustainable and the right balance of costs and risks is achieved. They underscored that improvements in debt management would be achieved by resuscitating the Debt Management Committee whose membership will be at senior level, which will look at each borrowing, to ascertain its concessionality and to insure debt sustainability. They reaffirmed their commitment to implementing the Debt Management Reform Programme, that was agreed with IMF and World Bank that is aimed at strengthening the debt management capacity of the Debt and Aid Management Division.

CONCLUSIONS

17. Malawi's debt situation remains at a moderate risk of distress, based on an assessment of external public debt, but with a heightened overall risk of debt distress, reflecting significant vulnerabilities related to domestic debt. Risk of export related shocks remains, given Malawi's limited sources of foreign exchange and reliance on rain-fed agriculture. Additional risks include the loosening of policies as a response to the decline in the volume of donor support, which could further erode donor confidence and jeopardize the resumption of aid. Risks of negative financing shocks in the form of delayed or lower donor support, or lower than expected tax revenue may require additional fiscal restraint, but should not compromise the medium-term debt sustainability of the country. Recent events point to the need for taking steps to arrest the decline in the quality of institutions (as reflected in the CPIA score), to ensure capacity to manage the debt load of the country.

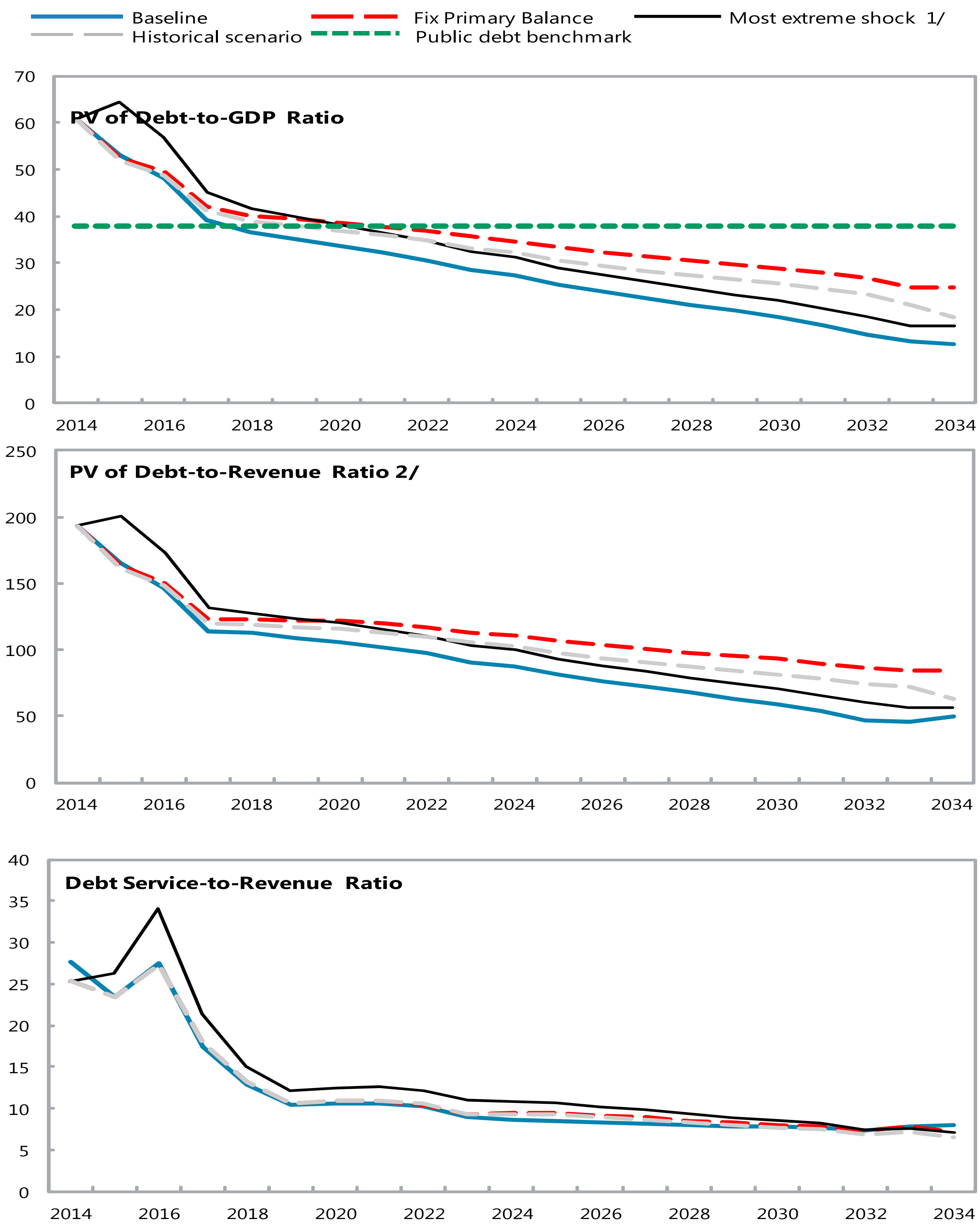
Figure 1. Malawi: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2014–34



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

1/ The most extreme stress test is the test that yields the highest ratio on or before 2024. In figure b. it corresponds to a Combination shock; in c. to a Exports shock; in d. to a Combination shock; in e. to a Exports shock and in figure f. to a GDP deflator shock

Figure 2. Malawi: Indicators of Public Debt under Alternative Scenarios, 2014–34



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

1/ The most extreme stress test is the test that yields the highest ratio on or before 2024.
2/ Revenues are defined inclusive of grants.

Table 1. Malawi: External Debt Sustainability Framework, Baseline Scenario, 2011–14

(In percent of GDP, unless otherwise indicated)

	Actual			Historical 6/ Average	Standard 6/ Deviation	Projections									
	2011	2012	2013			2014	2015	2016	2017	2018	2019	2014-2019 Average	2024	2034	2020-2034 Average
External debt (nominal) 1/	**21.0**	**42.8**	**49.7**			**52.1**	**40.2**	**39.3**	**37.1**	**36.5**	**35.8**		**29.1**	**16.2**	
of which: public and publicly guaranteed (PPG)	16.9	37.7	44.0			47.3	35.3	34.1	31.9	31.5	30.7		24.0	11.1	
Change in external debt	0.5	21.9	6.9			2.4	-11.9	-0.9	-2.2	-0.6	-0.8		-1.4	-1.8	
Identified net debt-creating flows	4.0	8.6	3.7			0.6	-0.8	-1.0	-1.3	-1.3	-1.4		-1.4	-1.1	
Non-interest current account deficit	**5.8**	**3.2**	**1.5**	**5.5**	**4.3**	**4.6**	**2.4**	**2.0**	**2.2**	**2.0**	**1.9**		**1.3**	**0.5**	1.0
Deficit in balance of goods and services	14.7	20.5	18.0			14.9	13.7	12.3	11.6	9.2	8.7		7.6	6.6	
Exports	25.1	33.4	42.5			41.0	37.4	35.9	33.8	34.2	35.1		36.1	36.4	
Imports	39.8	53.8	60.5			55.8	51.0	48.2	45.4	43.4	43.8		43.7	43.0	
Net current transfers (negative = inflow)	-10.9	-20.2	-20.4	-16.3	3.3	-14.9	-14.8	-15.0	-13.8	-12.7	-12.0		-9.5	-6.8	-8.5
of which: official	-6.4	-14.0	-13.2			-6.6	-7.7	-7.7	-7.4	-6.4	-6.0		-4.4	-2.6	
Other current account flows (negative = net inflow)	1.9	3.0	4.0			4.6	3.6	4.6	4.4	5.5	5.2		3.1	0.7	
Net FDI (negative = inflow)	**-1.1**	**-1.9**	**-2.4**	**-2.1**	**1.3**	**-2.0**	**-2.0**	**-1.7**	**-1.7**	**-1.6**	**-1.6**		**-1.2**	**-0.8**	-1.0
Endogenous debt dynamics 2/	**-0.7**	**7.3**	**4.6**			**-2.0**	**-1.3**	**-1.3**	**-1.8**	**-1.7**	**-1.7**		**-1.4**	**-0.8**	
Contribution from nominal interest rate	0.1	0.3	0.3			0.5	1.2	0.7	0.3	0.3	0.3		0.3	0.2	
Contribution from real GDP growth	-0.9	-0.5	-2.5			-2.5	-2.5	-2.0	-2.1	-2.0	-2.0		-1.7	-1.0	
Contribution from price and exchange rate changes	0.1	7.5	6.8			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**-3.4**	**13.3**	**3.1**			**1.9**	**-11.1**	**0.1**	**-0.9**	**0.7**	**0.6**		**0.0**	**-0.7**	
of which: exceptional financing	-2.2	-2.2	-2.6			-4.4	-4.1	-3.6	-3.1	-2.8	-2.1		-1.5	-0.7	
PV of external debt 4/	...	...	33.5			37.0	32.9	30.5	25.5	23.5	23.1		19.1	11.3	
In percent of exports	...	...	78.9			90.4	88.2	85.0	75.4	68.9	65.8		52.8	31.1	
PV of PPG external debt	**...**	**...**	**27.8**			**32.2**	**28.0**	**25.3**	**20.3**	**18.5**	**18.0**		**14.0**	**6.2**	
In percent of exports	**...**	**...**	**65.4**			**78.6**	**74.9**	**70.5**	**60.1**	**54.1**	**51.3**		**38.7**	**17.1**	
In percent of government revenues	**...**	**...**	**107.4**			**120.3**	**106.1**	**92.8**	**70.9**	**67.2**	**64.5**		**48.7**	**22.2**	
Debt service-to-exports ratio (in percent)	**1.4**	**2.0**	**4.6**			**4.7**	**8.0**	**13.2**	**8.3**	**4.1**	**3.1**		**3.4**	**2.2**	
PPG debt service-to-exports ratio (in percent)	**1.4**	**2.0**	**4.6**			**4.7**	**8.0**	**13.2**	**8.3**	**4.1**	**3.1**		**3.4**	**2.2**	
PPG debt service-to-revenue ratio (in percent)	**1.5**	**2.9**	**7.5**			**7.1**	**11.3**	**17.4**	**9.8**	**5.0**	**3.9**		**4.3**	**3.1**	
Total gross financing need (Billions of U.S. dollars)	0.3	0.1	0.1			0.2	0.2	0.3	0.2	0.1	0.1		0.1	0.2	
Non-interest current account deficit that stabilizes debt ratio	5.2	-18.6	-5.3			2.2	14.4	2.9	4.4	2.6	2.7		2.6	2.4	
Key macroeconomic assumptions															
Real GDP growth (in percent)	4.3	1.9	5.2	5.5	2.8	5.7	5.5	5.7	6.0	5.9	5.8	5.8	6.0	6.0	6.0
GDP deflator in US dollar terms (change in percent)	-0.3	-26.5	-13.7	-0.1	11.5	5.5	9.9	9.2	5.5	4.0	1.3	5.9	1.9	2.2	2.0
Effective interest rate (percent) 5/	0.5	0.9	0.6	0.7	0.2	1.2	2.7	2.1	1.0	0.8	0.9	1.4	0.9	1.0	1.0
Growth of exports of G&S (US dollar terms, in percent)	3.6	-0.3	15.7	14.0	15.2	7.5	5.8	11.0	5.2	11.5	10.3	8.5	8.1	8.6	8.4
Growth of imports of G&S (US dollar terms, in percent)	-7.8	1.3	2.1	10.5	15.6	2.9	6.0	9.2	5.3	5.2	8.4	6.2	7.7	8.4	8.0
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	44.9	50.4	52.7	54.3	53.2	52.1	51.3	46.6	37.8	43.6
Government revenues (excluding grants, in percent of GDP)	23.7	23.1	25.9			26.8	26.4	27.3	28.6	27.6	28.0		28.6	28.1	28.8
Aid flows (in Billions of US dollars) 7/	0.5	0.7	0.6			0.3	0.5	0.5	0.5	0.5	0.5		0.4	0.3	
of which: Grants	0.3	0.5	0.3			0.2	0.3	0.3	0.4	0.3	0.3		0.3	0.3	
of which: Concessional loans	0.3	0.2	0.2			0.1	0.2	0.2	0.2	0.2	0.1		0.1	0.0	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			9.1	8.3	7.8	7.3	6.5	5.4		3.4	1.5	2.8
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			62.4	76.2	80.4	83.2	82.5	84.0		80.5	91.1	80.1
Memorandum items:															
Nominal GDP (Billions of US dollars)	5.6	4.2	3.8			4.3	4.9	5.7	6.4	7.0	7.5		11.0	24.2	
Nominal dollar GDP growth	4.1	-25.1	-9.2			11.5	16.0	15.5	11.8	10.1	7.2	12.0	8.0	8.3	8.1
PV of PPG external debt (in Billions of US dollars)			0.9			1.2	1.4	1.4	1.3	1.3	1.3		1.5	1.6	
(PVt-PVt-1)/GDPt-1 (in percent)						8.3	3.7	0.5	-2.1	-0.4	0.8	1.8	0.3	-0.4	0.2
Gross workers' remittances (Billions of US dollars)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of PPG external debt (in percent of GDP + remittances)	...	...	27.8			32.2	28.0	25.3	20.3	18.5	18.0		14.0	6.2	
PV of PPG external debt (in percent of exports + remittances)	...	...	65.4			78.6	74.9	70.5	60.1	54.1	51.3		38.7	17.1	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	4.6			4.7	8.0	13.2	8.3	4.1	3.1		3.4	2.2	

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

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2. Malawi: Public Sector Debt Sustainability Framework, Baseline Scenario, 2011–34

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2011	2012	2013	Average 5/	Standard Deviation 5/	2014	2015	2016	2017	2018	2019	2014-19 Average	2024	2034	2020-34 Average
Public sector debt 1/	40.0	57.2	72.1			75.8	60.2	56.9	50.7	49.7	47.7		37.5	17.4	
of which: foreign-currency denominated	16.9	37.7	44.0			47.3	35.3	34.1	31.9	31.5	30.7		24.0	11.1	
Change in public sector debt	4.9	17.2	14.9	0.0		3.7	-15.5	-3.3	-6.2	-1.1	-1.9		-1.6	-1.5	
Identified debt-creating flows	3.5	10.2	1.0			-7.2	-9.9	-5.3	-5.7	-2.1	-3.1		-2.2	-0.9	
Primary deficit	2.0	0.2	1.9	-0.6	3.2	-1.6	-0.9	-3.1	-2.4	-0.7	-1.4	-1.7	-0.5	0.3	-1.1
Revenue and grants	28.3	34.6	34.0			31.4	32.0	33.0	34.2	32.5	32.3		31.3	29.3	
of which: grants	4.7	11.6	8.1			4.6	5.6	5.7	5.6	4.9	4.3		2.7	1.2	
Primary (noninterest) expenditure	30.3	34.8	35.9			29.8	31.1	29.9	31.8	31.8	30.9		30.8	29.5	
Automatic debt dynamics	1.7	10.2	-0.9			-5.7	-9.0	-2.3	-3.4	-1.5	-1.7		-1.7	-1.1	
Contribution from interest rate/growth differential	0.7	-2.3	-1.9			-2.5	-1.1	-0.8	-1.7	-1.6	-1.9		-1.7	-0.8	
of which: contribution from average real interest rate	2.2	-1.6	0.9			1.4	2.8	2.4	1.5	1.3	0.8		0.5	0.3	
of which: contribution from real GDP growth	-1.5	-0.7	-2.8			-3.9	-3.9	-3.3	-3.2	-2.8	-2.7		-2.2	-1.1	
Contribution from real exchange rate depreciation	1.0	12.5	1.0			-3.2	-7.9	-1.4	-1.7	0.1	0.2		...	...	
Other identified debt-creating flows	-0.3	-0.2	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	-0.3	-0.2	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	1.4	7.0	13.9			10.9	-5.6	2.0	-0.5	1.1	1.1		0.6	-0.7	
Other Sustainability Indicators															
PV of public sector debt	...	19.5	55.9			60.7	53.0	48.1	39.1	36.7	35.1		27.4	12.5	
of which: foreign-currency denominated	...	0.0	27.8			32.2	28.0	25.3	20.3	18.5	18.0		14.0	6.2	
of which: external	...	...	27.8			32.2	28.0	25.3	20.3	18.5	18.0		14.0	6.2	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	5.6	3.6	9.8			7.1	6.6	6.0	3.6	3.5	2.0		2.2	2.4	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	56.4	164.6			193.3	165.4	146.0	114.3	112.9	108.7		87.6	42.7	
PV of public sector debt-to-revenue ratio (in percent)	...	84.7	216.2			226.7	200.8	176.4	136.6	133.1	125.4		95.8	44.6	
of which: external 3/	...	...	107.4			120.3	106.1	92.8	70.9	67.2	64.5		48.7	22.2	
Debt service-to-revenue and grants ratio (in percent) 4/	12.6	9.8	23.2			27.6	23.5	27.5	17.5	12.9	10.5		8.6	8.0	
Debt service-to-revenue ratio (in percent) 4/	15.1	14.8	30.4			32.4	28.5	33.3	20.9	15.3	12.1		9.4	8.3	
Primary deficit that stabilizes the debt-to-GDP ratio	-2.9	-17.1	-12.9			-5.3	14.6	0.3	3.8	0.4	0.6		1.1	1.8	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	4.3	1.9	5.2	5.5	2.8	5.7	5.5	5.7	6.0	5.9	5.8	5.8	6.0	6.0	6.0
Average nominal interest rate on forex debt (in percent)	1.4	2.3	1.5	1.6	0.4	2.7	5.3	4.1	2.0	1.7	1.7	2.9	1.9	2.1	1.9
Average real interest rate on domestic debt (in percent)	12.5	-7.2	4.7	6.5	8.1	3.7	5.0	7.2	7.1	7.7	5.5	6.0	4.1	5.1	4.5
Real exchange rate depreciation (in percent, + indicates depreciation)	6.6	75.3	2.8	5.3	25.3	-7.5	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	4.0	17.7	27.3	13.7	8.2	20.9	16.5	8.7	6.8	6.8	6.5	11.0	5.6	5.5	5.7
Growth of real primary spending (deflated by GDP deflator, in percent)	-2.6	16.9	8.6	2.4	5.9	-12.4	10.1	1.7	12.9	5.8	2.8	3.5	9.3	5.0	5.7
Grant element of new external borrowing (in percent)	...	...	...	...	...	44.9	50.4	52.7	54.3	53.2	52.1	51.3	46.6	37.8	...

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

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 3. Malawi: Sensitivity Analysis for Key Indicators of Public Debt 2014–34

	Projections							
	2014	2015	2016	2017	2018	2019	2024	2034
PV of Debt-to-GDP Ratio								
Baseline	61	53	48	39	37	35	27	13
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	61	52	49	41	39	38	32	18
A2. Primary balance is unchanged from 2014	61	52	50	42	40	39	35	23
A3. Permanently lower GDP growth 1/	61	52	48	39	38	37	34	32
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-20	61	53	51	43	41	40	37	27
B2. Primary balance is at historical average minus one standard deviations in 2015-201	61	54	52	43	41	39	31	15
B3. Combination of B1-B2 using one half standard deviation shocks	61	54	52	43	41	40	34	19
B4. One-time 30 percent real depreciation in 2015	61	64	57	45	42	40	31	17
B5. 10 percent of GDP increase in other debt-creating flows in 2015	61	58	53	43	41	39	31	15
PV of Debt-to-Revenue Ratio 2/								
Baseline	193	165	146	114	113	109	88	50
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	193	162	148	120	119	117	102	63
A2. Primary balance is unchanged from 2014	193	163	150	123	123	122	111	79
A3. Permanently lower GDP growth 1/	193	162	145	115	115	113	107	109
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-20	193	166	154	123	125	124	116	91
B2. Primary balance is at historical average minus one standard deviations in 2015-201	193	168	159	126	125	121	98	51
B3. Combination of B1-B2 using one half standard deviation shocks	193	167	157	125	126	123	108	67
B4. One-time 30 percent real depreciation in 2015	193	201	173	132	128	123	100	57
B5. 10 percent of GDP increase in other debt-creating flows in 2015	193	181	160	126	125	121	98	51
Baseline	28	24	28	18	13	10	9	8
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	25	24	27	18	13	11	9	7
A2. Primary balance is unchanged from 2014	25	24	27	18	13	11	9	7
A3. Permanently lower GDP growth 1/	25	24	28	18	13	11	9	8
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-20	25	24	29	19	14	11	10	8
B2. Primary balance is at historical average minus one standard deviations in 2015-201	25	24	28	18	13	11	10	6
B3. Combination of B1-B2 using one half standard deviation shocks	25	24	28	19	13	11	10	7
B4. One-time 30 percent real depreciation in 2015	25	26	34	21	15	12	11	7
B5. 10 percent of GDP increase in other debt-creating flows in 2015	25	24	29	18	13	11	10	6

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

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Table 4a. Malawi: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014–34

(In percent)

	Projections							
	2014	2015	2016	2017	2018	2019	2024	2034
PV of debt-to GDP ratio								
Baseline	32	28	25	20	19	18	14	6
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	32	33	34	31	31	32	36	35
A2. New public sector loans on less favorable terms in 2014-2034 2	32	27	24	23	23	23	21	13
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	32	29	26	21	19	18	14	7
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	32	30	30	25	22	22	17	7
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	32	35	38	31	27	27	21	9
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	32	30	28	23	21	20	15	6
B5. Combination of B1-B4 using one-half standard deviation shocks	32	35	42	35	32	31	24	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	32	39	34	28	25	24	18	8
PV of debt-to-exports ratio								
Baseline	79	75	71	60	54	51	39	17
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	79	87	94	90	89	90	99	97
A2. New public sector loans on less favorable terms in 2014-2034 2	79	73	67	67	66	64	57	36
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	79	75	69	60	52	50	37	17
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	79	85	100	89	79	75	55	22
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	79	75	69	60	52	50	37	17
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	79	80	78	69	61	58	43	18
B5. Combination of B1-B4 using one-half standard deviation shocks	79	80	88	78	70	66	48	19
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	79	75	69	60	52	50	37	17
PV of debt-to-revenue ratio								
Baseline	120	106	93	71	67	64	49	22
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	120	124	124	107	111	114	124	125
A2. New public sector loans on less favorable terms in 2014-2034 2	120	104	88	79	82	81	72	47
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	120	109	96	74	69	66	50	23
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	120	112	109	87	82	78	58	24
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	120	132	139	108	100	96	72	34
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	120	113	103	81	76	73	54	23
B5. Combination of B1-B4 using one-half standard deviation shocks	120	134	155	124	116	111	82	33
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	120	146	124	97	89	86	64	30

Table 4b. Malawi: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014–34 (continued)

(In percent)

	Projections							
	2014	2015	2016	2017	2018	2019	2024	2034
Debt service-to-exports ratio								
Baseline	5	8	13	8	4	3	3	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	5	9	16	11	6	4	6	8
A2. New public sector loans on less favorable terms in 2014-2034 2	5	8	4	4	4	3	4	3
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	5	8	13	8	4	3	3	2
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	5	9	16	10	5	4	5	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	5	8	13	8	4	3	3	2
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	5	8	13	8	4	3	4	2
B5. Combination of B1-B4 using one-half standard deviation shocks	5	8	14	9	4	3	5	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	5	8	13	8	4	3	3	2
Debt service-to-revenue ratio								
Baseline	7	11	17	10	5	4	4	3
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	7	12	21	13	7	6	8	11
A2. New public sector loans on less favorable terms in 2014-2034 2	7	11	6	5	5	4	4	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	7	12	18	10	5	4	4	3
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	7	11	17	10	5	4	5	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	7	14	27	15	8	6	7	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	7	11	17	10	5	4	5	3
B5. Combination of B1-B4 using one-half standard deviation shocks	7	13	24	14	7	6	8	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	7	16	24	13	7	5	6	4
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	37	37	37	37	37	37	37	37

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

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assu an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

INTERNATIONAL MONETARY FUND

MALAWI

March 5, 2015

FIFTH AND SIXTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR WAIVERS FOR NON-OBSERVANCE OF PERFORMANCE CRITERIA, EXTENSION OF THE ARRANGEMENT, MODIFICATION OF PERFORMANCE CRITERION, AND REPHASING OF DISBURSEMENTS—INFORMATIONAL ANNEX

Prepared By The African Department
(In Consultation with Other Departments)

CONTENTS

RELATIONS WITH THE FUND

(As of December 31, 2014)

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	6.55	9.86

Outstanding Purchases and Loans:	**SDR Million**	**%Quota**
ESF Arrangements	27.76	40.00
ECF Arrangements	93.97	135.41

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
ECF	07/23/2012	07/22/2015	104.10	52.06
ECF[1/]	02/19/2010	07/22/2012	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				
	2015	**2016**	**2017**	**2018**	**2019**
Principal	17.35	17.86	15.71	20.41	11.89
Charges/Interest	0.03	0.03	0.06	0.04	0.14
Total	17.38	17.89	15.77	20.45	12.03

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

Implementation of HIPC Initiative:

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

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

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

Implementation of Multilateral Debt Relief Initiative (MDRI):

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

Debt Relief by Facility (SDR Million)

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

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

Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable

Safeguards Assessments:

An update safeguards assessment of the Reserve Bank of Malawi (RBM) with respect to the 2012 ECF was completed on December 27, 2012. The assessment reiterated the key safeguards concern – the lack of operational autonomy - and recommended that already envisaged amendments to the RBM Act to limit lending to government be expanded to strengthen RBM autonomy more broadly. The assessment also reiterated the need to enhance oversight of foreign reserves management along with measures to strengthen transparency of financial reporting.

Exchange Arrangements:

In 2006 the Fund determined that Malawi maintains a multiple currency practice (MCP) inconsistent with Article VIII, Section 3, due to a spread of more than 2% between the exchange rates of commercial banks and the rates of foreign exchange bureaus. At that time, the Fund determined that the spread resulted from official action by RBM, through informal limitation on the availability of foreign exchange and moral suasion on commercial banks.

In May 2012, the government liberalized the foreign exchange regime, devalued the kwacha by about 33 percent, and adopted a floating exchange rate regime. Since May 2012, the RBM has not set a target rate and allowed substantial volatility in the exchange rate, including recent depreciation to around MK 473.7 per U.S. dollar at end-December 2014. Official actions continue to play a role in influencing the exchange rate, but the exchange rate movements are largely market determined. Therefore, the de jure (as well as de facto) exchange rate arrangement was reclassified to floating from other managed arrangement.

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.

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
11/14	STA	NSO	Assistance with redeveloping data	Mission
11/14	FAD	Ministry of Finance	PFM Action Plan follow-up	Mission
09/14	STA	NSO	Development of direct prices survey for MPIs	Mission
03/14	STA	NSO	Further Assistance on Data Improvement	Mission
03/14	FAD	Ministry of Finance	PFM Reform Program	Mission
11/13	STA	NSO	Balance of Payments Statistics	Mission
09/13	STA	NSO	Price Statistics	Mission
03/13	FAD	Ministry of Finance	Public Financial Management	Mission
02/13	STA	RBM	RBMS' monetary statistics	Mission
02/13	FAD	Ministry of Finance	GFS 2001	Mission
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

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
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
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

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
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 Documentation.	Report
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

JOINT MANAGERIAL ACTION PLAN

(January 12, 2015)

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:**		
	1. MW-DRM	On-going	October, 2016
	2. Malawi Capacity Procurement Building	On-going	October, 2015
	3. MW - Gender Policy Notes	February, 2015	March, 2015
	4. Malawi Policy Note Series	On-going	February 2015
	5. Malawi Primary Education PET-QSD study	February, 2015	April, 2015
	6. Malawi Urbanization Review	January, 2015	March 2015
	7. Renewable Energy Resource Mapping	On-going	September, 2017
	9. Growth and Competitiveness	January, 2015	December 2015
	10. Malawi Economic Monitor (MEM)	Dec '14/Jun '15	Jan/Jul 2015
	Lending:		
	1. Ag. Commercialization & Rural Growth	April 2015	September, 2015
	2. Malawi: EITI Implementation Support	May, 2015	July, 2015
	3. MW: Shire Valley Irrigation Project.	August 2015	December 2015
	4. Project to Improve Public Finance and Economic Management	August, 2015	February 2016
	5. Fiscal Management Development Policy Operation	Ongoing	October 2015
IMF work program in next 12 months	1. Fifth review of ECF-supported program	February 2014	April 2014
	2. Sixth review of ECF-supported program	July/Aug 2014	October 2014
B. Requests for work program inputs			
Fund request to Bank	1. Updates on WB support to Malawi		Continuous
Bank request to IMF	1. Regular updates and exchange of views on medium-term macro projections including sharing detailed excel tables on Real, Monetary, Fiscal and External Sectors		Continuous
C. Agreement on joint products and missions			
Joint products in next 12 months	1. Debt Sustainability Analysis (update)	December 2014	Feb/March, 2015

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of December 31, 2014)

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 December 31, 2014, the Bank had provided significant and diversified support to Malawi, with cumulative commitments worth UA 852.8 million (about US$ 1.3 billion) to finance 100 operations including 12 studies and 2 lines of credit.

The AfDB Board of Directors on 30th January 2013 approved a new Country Strategy Paper (CSP) covering 2013–17. The Bank's current 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 Long Term Strategy (LTS, 2013–22) and the Regional Integration Strategy Paper for Southern Africa (Southern African RISP, 2011–15). The CSP, which is under implementation, focuses 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 has scaled-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, XIII and XIV resources. The Bank will also support Public Private Partnerships (PPPs) in infrastructure development. The CSP mid- term review will be undertaken in 2015.

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 UA 26 million (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 Bank disbursed UA 4 million (US$ 6 million) as additional budgetary support in June 2013. The Bank has completed appraisal of the Protection of Basic Services Program of US $ 30 million, which is expected to be presented for Board approval, the first quarter of 2015. This Sector Budget Support program is designed to protect critical expenditures in health, education and social protection and improve accountability following suspension of general budget support.

Box. AfDB Ongoing Operations.

The Bank's ongoing operations comprise the following: three projects in the agriculture sector: (i) Agriculture Infrastructure Support Project (AISP); (ii) Small-holder Irrigation and Value Addition Project and (iii) Climate Adaptation for Rural Livelihoods and Agriculture Project (grant from Global Environment Facility). The Bank is also financing through the African Water Facility (AWF) grants the Water Sector Monitoring & Evaluation Strengthening Project and the Water and Sanitation Access project for the Urban Poor in the City of Blantyre which is aimed at improving access to improved water supply and sanitation services. There are currently three projects providing support to the social sector and for economic empowerment (i) the the Local Economic Development project is developing infrastructure in four rural growth centers of Jenda, Malomo, Monkey Bay and Chitekesa; (ii) the Competitiveness and Job Creation Project in Private sector which aims to improve the capabilities and the competitiveness of the private sector as well as increase export diversification and job creation ; and (iii) Support to Higher Education Science & Technology Project aims to increase access to technical, entrepreneurship, vocational and training (TEVET) and higher education in Malawi, with particular emphasis to Information and Communication Technology (ICT). In the transport sector the Bank is supporting the Trunk Roads Rehabilitation Project which includes Blantyre-Zomba road rehabilitation project (60 km) and the Lilongwe Bypass construction Project (13km) as part of the Multinational Nacala Road Corridor. As at the end of December 2014, the overall portfolio was rated satisfactory with an average disbursement rate of 29% In line with the CSP indicative program, the Bank approved four new operations in 2013, the Mzuzu-Nkhata Bay Road Rehabilitation Project (US$ 33.20m), Smallholder Irrigation and Value Addition Project (US$39.98m) funded by Global Agriculture and Food Security Project and the African Development Fund, the multinational Nacala Road Corridor Development Project Phase IV (US$65.9m) and the Public Finance Management Institutional Support Project (about US $ 4.5 million). The PFM Project, which the Board approved in October, 2013, is supporting the Government of Malawi in implementing its five-year Public Finance and Economic Management Reform Program (PFEMRP) through improved tax administration and procurement systems. In April, 2014, the Board also approved Phase II of the National Water Development Programme (about US $ 35 million).

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. During 2012–2013 the Bank prepared a Private Sector Profile for Malawi and has also financed jointly with the World Bank and other partners a Public Expenditure Review. In addition, the Bank is supporting the Private Public Partnership Commission (PPPC) with a grant to implement the Capacity Building and Assessment of the Legislative and Institutional Framework for PPPs in Malawi. The Bank also undertook the Domestic Resource Mobilization Study for Malawi in 2013/2014 and provided TA to the Reserve Bank of Malawi to strengthen capacity in macro-economic forecasting.

STATISTICAL ISSUES

Malawi—STATISTICAL ISSUES APPENDIX

As of February 2015

I. Assessment of Data Adequacy for Surveillance

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

National Accounts: National accounts estimates are produced with a two-year lag due to untimely source data. However, progress has occurred on improving methodology, in collaboration with a Norway-funded project. East AFRTAC has been assisting with the development of quarterly national accounts, including improvements to a monthly index of industrial production. Staff resources remain insufficient

Price Statistics: A consumer price index (CPI) is available on a timely basis. The CPI base is 2012, drawing on the 2010/11 Integrated Household Survey; and data (on urban and rural price indices) are collected on a monthly basis by regional price collectors. A 2013 East AFRTAC TA mission began the development of import and export price indexes (for which additional resources are needed) and a review of the new producer price index.

Government Finance Statistics: 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 discrepancies, 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 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 Finance 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 pre-financing 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.[1] Expenditure data is loosely mapped to functional classification based on the classification of functions of government (CoFoG) classification.

- 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 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.

- 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.

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

- 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 2015. Government finance data are reported for publication in the *Government Finance Statistics Yearbook (GFSY).*

Monetary and Financial Statistics: The Reserve Bank of Malawi (RBM) has improved data reporting to the Fund. Monthly monetary and financial statistics (MFS) are reported to STA on a continuous basis. The 2013 and 2015 missions assisted RBM staff in developing the standardized report forms (SRFs) for the central bank accounts (1SR), other depository corporations (2SR), monetary aggregates (5SR), and financial soundness indicators (FSIs). The authorities are expected to begin reporting SRF-based MFS and FSI data to STA by end-2015.

The quality of the reported data has been improved. The RBM has revamped banks' call report forms to include additional breakdowns of assets and liabilities by institutional sector. Repurchase agreements data that were originally reported in the ODCs balance sheet without any breakdowns by holding sector are now reported in a separate annex, which provides the necessary breakdowns of the holding sectors. Similarly, the annex on overdue and nonaccrual loans, leases, and other assets by sector, which was previously reported on a quarterly basis, is now reported on a monthly basis.

Despite this progress, MFS data are still in need of improvements in terms of financial institution coverage. The depository corporation survey (DCS) does not include data for one investment bank which accepts deposits included in broad money, thereby hampering the accuracy of the compiled data. The 2013 and 2015 missions recommended the inclusion of that bank in the DCS. These missions also recommended inclusion in the DCS of saving and credit cooperatives (SACCOs) and their parent body—Malawi Union of Saving and Credit Cooperatives (MUSCCO).

Financial sector surveillance: With regard to FSIs, Malawi currently does not report data to the Fund for dissemination on the Fund website.

External sector statistics: The balance of payments (BOP) statistics in Malawi are compiled by the Balance of Payments Section of the NSO and are prepared in close coordination with the Malawi National Accounts (NA). The estimates are largely based on survey data for private enterprises, trade statistics, banking data, and information from Government Departments. Some of the surveys collect balance of payments and NA data together. Malawi reports the BOP and IIP in the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)* format, reasonably compliant.

The BOP Section collects data via three substantial surveys. The Foreign Private Capital (FPC) survey collects data, essentially for the financial account; the BOP survey collects services and primary income data; and the Non-Profit Institutions Serving Households (NPISH) survey collects secondary income and capital account data. The achievement of the recommendations of the last TA missions (April 2012, November 2012, November 2013, and February 2014) depends on the maintenance of the funding and resources available to the BOP Section. The likely Government budget constraints over the coming years may make funding difficult to achieve. The constraints, especially after the Malawi "Cashgate" scandal, are severe. The funding for the 2015 FPC survey (data for 2013 and 2014) has been agreed for this Spring/Summer, while there was no funding for the BOP and NPISH surveys in 2014.

II. Data Standards and Quality	
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.	Data ROSC was published on February 17, 2005.

Malawi: Tables of Common Indicators Required for Surveillance

(As of January, 2015)

	Date of latest observation	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]	10/2014	01/2015	M	M	M		
Reserve/Base Money	10/2014	01/2015	M	M	M	LO, LO, LNO, O	LO, O, O, O, O
Broad Money	10/2014	01/2015	M	M	M		
Central Bank Balance Sheet	10/2014	01/2015	M	M	M		
Consolidated Balance Sheet of the Banking System	10/2014	01/2015	M	M	M		
Interest Rates[2]	12/2014	01/2015	M	M	M		
Consumer Price Index	12/2014	01/2015	M	M	M	O, LNO, O, O	LNO, O, O, O, NA
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	10/2014	11/2014	M	M	I	O, LO, O, O	O, LO, O, O, LNO
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	10/2014	11/2014	M	M	I		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	10/2014	11/2014	M	M	M		
External Current Account Balance	10/2014	11/2014	A	A	A	O, O, O, O	LO, O, LO, O, O
Exports and Imports of Goods and Services	10/2014	11/2014	A	A	A		
GDP/GNP	10/2014	11/2014	A	A	A	LO, LNO, LNO, LO	LNO, LNO, LO, LO, LNO
Gross External Debt	2014	11/2014	M	I	I		
International Investment Position[6]	2010	2014	I	I	I		

[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 and 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.

Press Release No. 15/133
FOR IMMEDIATE RELEASE
March 23, 2015

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fifth and Sixth Reviews under Malawi's ECF Arrangement, and Approves US$ 18.1 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the fifth and sixth reviews of Malawi's economic performance under the program supported by an Extended Credit Facility (ECF) arrangement.[1] The Board's decision enables the immediate disbursement of SDR 13.02 million (about US$18.1 million), bringing total disbursements under the arrangement to SDR 65.08 million (about US$ 90.3 million).

In completing the fifth and sixth reviews, the Executive Board also approved the authorities' request for waivers of non-observance of performance criteria related to the net domestic assets of the Reserve Bank of Malawi (RBM), net domestic borrowing by the government, the ceiling on new non-concessional external debt maturing in more than one year, and the ceiling on non-accumulation of external payments arrears.

The Board also approved a request for an extension of the current ECF arrangement by six months to May 22, 2016 and the rephasing of disbursements associated with the seventh and eighth reviews.

The three-year ECF arrangement for Malawi in the total amount of SDR 104.1 million (about US$ 144.4 million) was approved on July 23, 2012 (see Press Release No. 12/273).

At the conclusion of the Executive Board's discussion, Mr. Mitsuhiro Furusawa, Acting Chair and Deputy Managing Director, issued the following statement:

"Malawi's macroeconomic outlook and performance under the IMF-supported program was significantly damaged by a large-scale theft of public funds and by policy lapses in the run-up to elections. The breach of governance resulted in the suspension of budget support from

[1] The Extended Credit Facility (ECF) is the IMF's main tool for medium-term financial support to low-income countries. It provides for a higher level of access to financing, more concessional terms, enhanced flexibility in program design, and more focused, streamlined conditionality. Financing under ECF currently carries a zero interest rate, with a grace period of 5½ years, and a final maturity of 10 years.

donors, which has led to increased recourse to central bank financing, accumulation of domestic arrears, exchange rate depreciation, and high inflation.

“The new government is committed to rebuilding trust in public institutions and bringing the IMF-supported program back on track, including through maintaining a flexible exchange rate regime and the automatic fuel pricing mechanism. Bringing inflation down to single digits and boosting official foreign exchange reserves remain key policy objectives.

“Addressing weaknesses in public financial management is necessary to restore confidence in the budget process and foster donor re-engagement. The authorities’ steadfast implementation of a comprehensive strategy in this area remains an urgent policy priority.

“The central bank is committed to tightening monetary policy as needed to keep inflation on a downward path. Measures taken in late 2014 have already helped reduce liquidity and stabilize the currency. Steps underway to curb deficit financing by the central bank should enhance the credibility of monetary policy.

“Improved prudential and regulatory frameworks are key to safeguarding financial sector stability and supporting growth. The recently-completed diagnostic assessments of the banking system will be used to design a strategy to address sector-wide issues.

“Nonconcessional external borrowing in October 2013 gave rise to noncomplying disbursements following the completion of the third and fourth reviews of the Fund-supported program in January 2014. The authorities have taken corrective actions to strengthen their monitoring of the concessionality of new external loans and to enhance communication with Fund staff on this matter. In view of the corrective actions taken by the authorities, the Board decided to waive the nonobservance of the performance criteria that gave rise to the noncomplying disbursements.”

Statement by Mr. Mkwezalamba, Alternate Executive Director, Mr. Tucker, Senior Advisor to the Executive Director and Mr. Sitimawina, Advisor to the Executive Director for Malawi, March 23, 2015

Introduction

1. The Malawian authorities appreciate the meaningful policy advice and guidance of the Fund Executive Board and Management in their efforts to achieve macroeconomic stability, reduce poverty and attain sustainable and inclusive growth. Further, they welcome and commend the constructive policy dialogue with staff during the program discussions.

2. The elections of May 2014 ushered in a new government of Prof. Arthur Peter Mutharika, which is firmly committed to the objectives of ECF supported program, including vigorously pursuing the implementation of the recommendations of the forensic audit report, strengthening PFM systems, and implementing critical structural reforms. Their commitment is manifested through their efforts to stabilize the macroeconomic situation and the continued implementation of various reforms. Most of these reforms have been covered in the staff report and we will emphasize on some of them in our statement. It is against this backdrop that the authorities solicit the Executive Directors' support for their request for completion of the fifth and sixth reviews under the ECF arrangement, the request for waivers for non-observance of performance criteria, extension of the arrangement, modification of performance criterion and the re-phasing of disbursements.

Performance under the ECF arrangement

3. The uncovering in late 2013 of the misappropriation of public funds, referred to in Malawi as 'cashgate', disrupted the progress towards macroeconomic stabilization and structural transformation of the Malawian economy. The authorities' response to the 'cashgate' scandal was swift and robust. Immediately, a forensic audit of the suspected transactions was launched and action to address weaknesses in public financial management (PFM) was initiated. In this regard, prosecutions arising from the audit report are being pursued resulting in convictions and recovery of some assets.

4. However, the ensuing suspension of budget support by development partners exacerbated the economic situation, rendering budget execution and implementation of the Extended Credit Facility (ECF) program challenging. Attempts by the authorities at fiscal adjustments in response to this development proved ineffective, as the programmed domestic borrowing ceiling was breached and large domestic payment arrears accumulated. The pace of reserves accumulation slowed and efforts at managing domestic liquidity was constrained. Consequently, as highlighted in the staff report, several quantitative performance criteria (PCs) in respect of the fifth and sixth program reviews—end-December 2013 and end-June 2014 test dates, respectively—were missed. On the structural reform agenda, some delays in implementation were experienced, though key measures, including verification of the stock of government domestic arrears and third party diagnostics of commercial banks, were implemented.

5. In spite of the challenges, the Malawian authorities have remained committed to implementing sound macroeconomic and structural policies, and returning the program on track. This has been manifested in the attainment of all but one of the informal quantitative targets agreed with the staff team on Net Domestic Assets, Net Domestic Financing and gross official reserves for end-September 2014 and end-January 2015. More importantly, the prior actions agreed upon for completion of the fifth and sixth reviews under the program, in the areas of fiscal policy, public financial management, monetary policy and financial sector, have been fully implemented.

6. The authorities underscore their determination to prevent the recurrence of the breach of the continuous PC on new non-concessional external debt maturing in more than one year and the continuous PC on the non-accumulation of external payment arrears. As expressed in the authorities' response to the Managing Director's letter on the subject and in their Letter of Intent, appropriate remedial measures have been undertaken. These include cancellation and replacement of the Supplier's Credit Agreement with a suppliers' agreement with a much reduced total value of the overall transaction of only US$33 million from US$145.3 million and normalization of all outstanding external payment arrears. In addition, debt management capacity is being enhanced following the resuscitation of the Debt Management Committee. The authorities have also made an undertaking to share with Fund staff all new loan proposals to ensure conformity with program understandings. Against the backdrop of these measures, our authorities request waivers for non-compliance with the missed continuous PCs.

Recent economic developments, macroeconomic outlook and policies

7. The medium-term macroeconomic outlook remains favorable, with policies focused on strengthening the macroeconomic position and sustaining growth on its upward trajectory. Consistent with this outlook, the authorities' short-term priorities will be on restoring macroeconomic stability, reinforcing PFM systems, and preserving the stability of the financial sector. Economic growth is expected to be somewhat resilient on account of increased public investment in infrastructure and an improved policy and business environment. Inflation is to decline from current levels to low double digits by end-2015 and then single digit levels towards end-2016, benefiting from a well-calibrated monetary policy and lower international fuel prices.

8. While real GDP is projected to have grown by around 6 percent in 2014 driven by agriculture, wholesale and retail trade, and information and communication sector, the outlook in 2015 could be affected the by heavy downpour of torrential rains and subsequent worst floods Malawi has suffered in its history. The floods have affected 15 of the 28 districts in the country, causing severe toll in human lives and destroying crucial transport infrastructure and disrupting energy generation. Over 172 people are missing while 106 have died. In addition, livestock, houses and a significant portion of agricultural land have also been destroyed. This will affect growth in the agricultural sector and may in turn affect food security in the next consumption year, with undesirable implications for public finances. This development poses immense risks to the realization of the envisaged near-term growth and inflation outlook. The authorities express their appreciation to the international community for their rapid response to the disaster and their continued support which is helping to alleviate the plight of those affected.

Fiscal and debt management policies

9. In spite of the difficult domestic fiscal environment, the authorities remain committed to pursuing prudent fiscal policy geared towards consolidating the fiscal position while avoiding a further build-up of domestic payment arrears. The current FY2014/15 budget is predicated on large fiscal adjustments, with significant reduction in non-statutory recurrent expenditures and domestically financed capital spending against the backdrop of the dearth of external budgetary support and the constrained space for domestic bank financing. While this has been challenging, the authorities continue to exercise fiscal discipline by restraining budget execution within program limits. Going forward, efforts will continue to strengthen fiscal management and shore up public finances. On the revenue front, policy measures will focus on strengthening tax administration and minimizing tax exemptions. On expenditures, the authorities will seek to further rationalize the budget envelope while preserving allocations to growth-enhancing sectors. Regularizing the large stock of domestic arrears accumulated over the years remains a priority over the medium term. To this end, the authorities are determined to proceed with clearing all audited and verified domestic arrears through cash payments and the issuance of 'zero coupon bonds' over the next three fiscal years.

10. The authorities reiterate their commitment to preserving debt sustainability over the medium to long term. While the country remains at a moderate risk of external debt distress, as assessed by the staffs' debt sustainability analysis, they are mindful of the heightened overall risk of debt distress resulting from the increasing vulnerabilities from domestic debt accumulation. Thus, in addition to the measures highlighted above to strengthen debt management and prevent the incidence of misreporting, they will continue to exercise fiscal restraint while relying mostly on concessional external borrowing to finance critical development projects.

Public financial management

11. A centerpiece of the authorities' near-term reform agenda is the strengthening of public financial management systems to facilitate efficient government financial operations and restore public confidence in budget execution. In this regard, the authorities commend the TA that has been received from FAD. Already, significant progress has been accomplished in strengthening commitment controls, reconciling fiscal accounts, and improving cash management. Further consolidation of these efforts will be sought through judicious implementation of the recently adopted PFM strategy, within the framework of the authorities' Public Finance and Economic Management Reform Programme. In view of the several operational and system deficiencies in the current Integrated Financial Management Information Systems (IFMIS), the authorities have initiated the process of procuring a new, well secured and efficient IFMIS. In the interim, the current system is being enhanced to ensure that efficient government financial transactions continue while prosecutions of the alleged cases of fraud identified in the Forensic Audit report are resolutely being pursued. Subsequently, an assessment of the implementation of these recommendations will be undertaken by a reputable international audit firm.

Monetary and exchange rate policies

12. The Reserve Bank of Malawi (RBM) has demonstrated a strong commitment to stabilizing monetary conditions and bolstering the external reserves position, using monetary policy instruments at its disposal. In response to increased inflationary pressures and a sharp depreciation of the Kwacha in 2014, the Bank raised the policy rate by 250 basis points and increased the liquidity reserve requirement on foreign currency deposits with commercial banks. Further, a ‘currency swap’ arrangement was implemented involving the purchase of government debt denominated in Kwacha by a foreign commercial bank, the Preferential Trade Area (PTA) Bank, using US dollars. These policy actions culminated in a tightening of monetary conditions through a rise in both the interbank and the treasury bills rate, restoration of some order in the foreign exchange market, and the strengthening of the foreign exchange reserves position. Important steps have also been taken to address the perennial problem of fiscal dominance, including amendments to the RBM Act that impose tighter limit on total government borrowing from the central bank, and the prohibition of the automatic conversion of overdrafts into government securities.

13. Over the near term, the RBM will maintain a tight monetary policy stance to return inflation to a downward path and to appropriately anchor inflation expectations. To this end, the Bank’s liquidity forecasting and management framework will be further strengthened to closely monitor the build-up of excess liquidity in the banking system. The current flexible exchange rate regime will be maintained, as it has served the economy well especially in facilitating economic adjustments to exogenous shocks. The RBM will, nonetheless, continue limited interventions in the foreign exchange market to smoothing short-term volatility in the exchange rate and bolster the foreign reserves position.

Financial sector policies

14. The authorities remain committed to taking appropriate steps to address any risks posed by weaknesses in the financial sector. This far, third party diagnostic assessments have been conducted on the banking system, and a restructuring process to resolving issues with two banks identified as weak has commenced. A comprehensive strategy is being developed to address banking sector-wide problems from the assessments. In addition, migration to Basel II Core Principles has been completed, with an increase in total capital requirement ratios of banks. A prompt corrective action framework to strengthen and clarify existing triggers for early remedial action against distressed banks has been adopted. The RBM will continue efforts to strengthen the supervisory and regulatory frameworks of the banking system. On-site inspection and off-site supervision will be intensified, compliance with prudential norms strictly enforced, and loan concentrations closely monitored. Further, the enactment of amendments to the Banking and Financial Services Acts to ensure consistency with international best practices in bank resolution will be pursued.

Request for waiver of non-observance of performance criteria

15. The Malawi authorities deeply regret the misreporting associated with the third and fourth reviews and request a waiver for non-observance of a performance criterion (PC) under the ECF supported program. As explained in EBS/15/13, the misreporting relates to the nonobservance of

the continuous PCs on new non concessional external debt maturing in more than one year and external payments arrears.

16. In line with the Managing Directors report, the Malawi authorities did not, at the completion of the third and fourth reviews, report to the Fund that it had not contracted new non-concessional external loans after the completion of the second review on April 8, 2013, aside from a non-concessional loan with China for which a waiver was requested, and that it had accumulated no external arrears during the review period. The reported observance of the external payments arrears PC, as well as the corrective actions taken by the authorities to address the non-observance of the non-concessional external debt PC at that time formed part of the basis for the Executive Board's completion of the third and fourth reviews. As it turned out, the information provided by the authorities, was inaccurate, leading to non-complying disbursements.

17. The new administration recognized that the terms of the Supply Credit Agreement run counter to the understanding of the ECF arrangement and immediately took corrective measures. The measures which are outlined in the authorities' response of February 19, 2015 to the Managing Director's letter of February 12, 2015, (EBS/15/13), include cancellation and replacement of the Supplier's Credit Agreement with a suppliers' agreement with a much reduced total value of the overall transaction and normalization of all outstanding external payment arrears. In addition, debt management capacity is being enhanced following the resuscitation of the Debt Management Committee. The authorities have also made an undertaking to share with Fund staff all new loan proposals to ensure conformity with program understandings.

Conclusion

18. The authorities reiterate their commitment to implementing sound macroeconomic policies and far-reaching structural reforms, within the framework of the ECF arrangement. On the basis of the progress accomplished by the Malawian authorities in addressing the weaknesses in public financial management and correcting underlying macroeconomic imbalances, our authorities solicit the Executive Directors' support for their request for completion of the fifth and sixth reviews under the ECF arrangement, the request for waivers for non-observance of performance criteria, extension of the arrangement, modification of performance criterion and the re-phasing of disbursements.