IMF Country Report No. 23/375

MALAWI

November 2023

SECOND REVIEW UNDER THE STAFF-MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT AND REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MALAWI

In the context of the Second Review Under the Staff-Monitored Program with Executive Board Involvement and Request for an Arrangement Under the Extended Credit Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on November 15, 2023, following discussions that ended on September 21, 2023, with the officials of Malawi on economic developments and policies underpinning its Staff-Monitored Program with Executive Board Involvement and IMF arrangement under the Extended Credit Facility. Based on information available at the time of these discussions, the staff report was completed on November 8, 2023.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the International Development Association.
- An **Informational Annex** prepared by the IMF staff.
- A **Supplementary Information** updated on November 10, 2023.
- A **Statement by the Executive Director** for Malawi.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

PRESS RELEASE

PR23/394

IMF Executive Board Discussed the Second Review under Malawi's Staff Monitored Program with Executive Board Involvement and Approved a 48-month Arrangement under the Extended Credit Facility

FOR IMMEDIATE RELEASE

- *The Executive Board of the International Monetary Fund (IMF) discussed the Second (and last) Review of the Staff-Monitored Program with Executive Board Involvement (PMB) and approved a 48-month arrangement under the Extended Credit Facility (ECF) for Malawi in an amount equivalent to SDR131.86 million (about US$175 million), with an immediate disbursement of SDR26.37 million (about US$35 million).*
- *Malawi continues to face a challenging macroeconomic environment. Years of unsustainable domestic and external borrowing and the adverse impact of multiple external shocks have resulted in the widening of macroeconomic imbalances, including protracted balance of payment needs.*
- *The ECF-supported program will support the authorities' macroeconomic adjustment and reform agenda aimed at restoring macroeconomic stability, building a foundation for inclusive and sustainable growth, and addressing weaknesses in governance.*

Washington, DC – November 15, 2023: The Executive Board of the International Monetary Fund (IMF) discussed the Second Review of the Staff-Monitored Program with Executive Board Involvement (PMB) and approved a 48-month arrangement under the Extended Credit Facility (ECF) for Malawi with access of 95 percent of quota, equivalent to SDR131.86 million (about US$175 million). The decision allows an immediate disbursement of SDR26.37 million (about US$35 million).

Malawi has struggled to sustain growth for decades despite large inflows of official development assistance. The past three years have been particularly difficult with stagnating growth and widening macroeconomic imbalances due to unsustainable debt and the effects of multiple shocks, including an outbreak of cholera and cyclone Freddy this year alone.

Malawi's external debt is unsustainable and debt service needs are eroding limited fiscal space. Despite sizeable external emergency financing, the large fiscal budget deficit necessitated domestic financing. This has been addressed in large part through monetary financing, putting pressure on the exchange rate and increasing the rate of inflation.

The ECF arrangement aims to support the authorities' commitment to restore macroeconomic stability, build a foundation for inclusive and sustainable growth, including to strengthen resilience to climate-related shocks, and address weaknesses in governance and institutions. The arrangement is also expected to catalyze grant financing and capital inflows including foreign direct investment and trade credit.

Following the Executive Board discussion on Malawi, Ms. Gita Gopinath, First Deputy Managing Director, and Acting Chair, issued the following statement:

"The Malawian authorities have shown unwavering commitment to the Staff-Monitored Program with Executive Board Involvement (PMB) and together with tangible progress on securing debt treatment, have established a track record for an Extended Credit Financing (ECF) arrangement with the IMF. The ECF arrangement will support the ongoing macroeconomic adjustment and reforms, catalyze grant financing and foreign direct investment, and provide a framework for structural reforms".

"Successful external debt restructuring is vital as there is no reasonable mix of adjustment and financing alone that can deliver macroeconomic stability. The Malawian authorities are seeking comparable treatment from all official bilateral creditors and continue to pursue good faith negotiations with commercial creditors. However, time is of the essence for debt relief, as further delays would result in greater financing gaps, which could then only be closed at an undesirably high cost to the population".

"Fiscal discipline, supported by a robust public financial management system and timely production of comprehensive fiscal reports, remains critical. Concerted effort by the authorities and other domestic stakeholders to prepare for fiscal financing challenges is important. Price stability is critical to prevent a further erosion of purchasing power.
Rebuilding international reserve buffers and allowing for greater flexibility in the exchange rate are critically important to bring back trade credit and to reduce Malawi's vulnerability to external shocks. Addressing weakness in governance and institutions will be important".

"Shifting Malawi's growth model from a consumption-driven to a production-driven one and from a government-led to a private-sector-led one is a core principle of Malawi 2063 and is vital to make Malawi's growth inclusive, sustainable, and resilient to climate-related shocks".

"The PMB was sufficiently robust to meet its objectives".

Malawi: Selected Economic Indicators, 2022–28

	2022	2023		2024		2025	2026	2027	2028
	Prel.	PMB 1st Review	Proj.	PMB 1st Review	Proj.				
National accounts and prices (percent change, unless otherwise indicated)									
GDP at constant market prices	0.8	1.7	1.6	3.3	3.3	3.8	4.3	4.5	4.6
Nominal GDP (billions of Kwacha)	11,799	14,768	15,396	17,728	19,900	23,454	26,326	29,279	32,390
GDP deflator	17.3	23.1	28.4	16.3	25.1	13.5	7.6	6.4	5.8
Consumer prices (end of period)	25.4	24.4	40.0	15.2	18.3	9.8	7.6	6.5	6.5
Consumer prices (annual average)	20.8	24.8	30.3	18.3	27.9	14.7	8.1	6.8	6.5
Investment and savings (percent of GDP)									
National savings	10.0	4.7	6.2	2.5	2.1	2.3	0.4	2.0	2.6
Government	-5.6	-6.2	-4.6	-6.4	-5.6	-4.2	-3.9	-1.9	-1.2
Private	15.5	11.0	10.9	9.0	7.7	6.5	4.4	4.0	3.8
Gross investment	13.1	12.7	13.9	11.5	10.6	12.2	9.4	10.2	10.0
Government	10.2	9.9	11.2	8.7	7.9	9.3	6.3	6.4	4.8
Private	3.0	2.8	2.7	2.8	2.6	2.9	3.1	3.8	5.3
Saving-investment balance	-3.2	-7.9	-7.6	-9.0	-8.5	-9.9	-9.0	-8.2	-7.4
Central government (percent of GDP on a fiscal year basis)[1, 2]									
Revenue	14.3	17.4	17.2	17.7	17.2	18.4	18.8	17.6	18.8
Tax and nontax revenue	12.5	13.5	13.3	14.9	14.0	15.8	16.1	15.7	16.6
Grants	1.8	3.9	3.9	2.7	3.2	2.6	2.7	1.8	2.2
Expenditure and net lending	22.6	29.3	28.9	27.5	27.9	26.5	25.9	23.3	22.9
Overall balance (excluding grants)	-10.8	-15.8	-15.6	-13.2	-13.9	-10.7	-9.8	-7.6	-6.3
Overall balance (including grants)	-9.0	-11.8	-11.7	-10.5	-10.7	-8.1	-7.1	-5.7	-4.1
Foreign financing	2.6	3.3	3.3	0.6	0.4	-0.3	0.3	-0.4	-0.6
Total domestic financing	6.9	8.5	8.4	8.4	8.0	5.0	3.5	3.8	2.7
Financing gap/residual gap	0.0	0.0	0.0	1.5	2.4	3.3	3.4	2.4	1.9
Primary balance	-5.0	-6.8	-6.8	-4.9	-5.4	-1.1	0.4	1.7	3.0
Domestic primary balance[3]	-4.4	-3.8	-3.8	-2.8	-3.0	1.0	2.4	2.9	3.7
Money and credit (change in percent of broad money at the end of the period, unless otherwise indicated)									
Broad money	38.8	25.2	30.5	20.0	29.3	17.9	12.2	11.2	10.6
Net foreign assets	-13.8	-5.3	-13.3	8.4	12.6	10.4	6.2	2.5	3.2
Net domestic assets	52.6	30.5	43.8	11.7	16.6	7.5	6.0	8.7	7.4
o/w Net claims on the government	39.0	26.1	43.3	18.8	8.8	12.8	10.9	10.9	9.8
Credit to the private sector (percent change)	24.1	16.0	19.6	8.2	11.2	5.8	8.9	9.1	10.7
External sector (US$ millions, unless otherwise indicated)									
Exports (goods and services)	1,128	1,322	1,428	1,454	1,552	1,653	1,730	1,872	1,984
Imports (goods and services)	1,835	2,487	2,680	2,608	2,695	2,969	3,011	3,136	3,215
Gross official reserves	120	499	394	747	714	967	1,081	1,133	1,135
(months of imports)	0.5	2.3	1.8	3.3	2.9	3.9	4.1	4.2	4.1
Net international reserves[4]	-1,247	-673	-1,052	-594	-667	-468	-366	-306	-232
Current account (percent of GDP)	-3.2	-7.9	-7.6	-9.0	-8.5	-9.9	-9.0	-8.2	-7.4
Real effective exchange rate (percent change)	2.9	...	...	...	...	...	...	...	...
Overall balance (percent of GDP)	-0.1	-2.6	-2.2	0.1	0.1	1.0	-0.4	0.0	0.4
Financing gap (percent of GDP)	0.0	5.8	4.6	2.6	3.1	1.8	2.0	0.9	0.2
Terms of trade (percent change)	-14.2	11.4	15.8	-1.8	0.2	2.9	3.1	3.2	-0.8
Debt stock and service (percent of GDP, unless otherwise indicated)									
External debt (public sector)	34.8	37.1	39.3	35.3	35.2	33.8	31.2	28.8	26.3
NPV of public external debt (percent of exports)	269.9	187.1	178.8	162.3	154.8	142.8	131.3	118.8	108.9
Domestic public debt[5]	40.8	43.2	42.0	44.9	39.8	41.0	42.3	43.0	41.7
Total public debt[5]	75.7	80.2	81.3	80.2	75.0	74.8	73.5	71.8	68.0
External debt service (percent of exports)	11.9	59.8	58.1	25.2	26.1	18.8	18.0	12.8	10.8
External debt service (percent of revenue excl. grants)	7.8	44.7	46.9	23.6	25.4	18.2	17.1	11.9	9.7

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

[1]The financial year, 2021, runs from July 1, 2020 to June 30, 2021. FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year. starting from FY2022/23.

[2]Please note that government fiscal statistics are reported following the Government Finance Statistics Manual (2014) starting 2020 projections and going

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

[4] 2022 NIR is calculated as defined in the TMU at the time of the PMB application. Thereafter, the net international reserves reported not only subtract foreign currency drains (FCD) as defined in the TMU of the First Review of the PMB, but also all outstanding foreign currency debt service to external creditors to which the RBM (including as an agent of the government) is in arrears and or servicing via other means, in line with debt restructuring strategy.

[5]Domestic debt is at face value and future borrowings is at cost value.

INTERNATIONAL MONETARY FUND

MALAWI

November 8, 2023

SECOND REVIEW UNDER THE STAFF-MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT AND REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY

EXECUTIVE SUMMARY

Context and recent developments. Malawi is recovering from a series of shocks. Real GDP is projected to increase by 1.6 percent in 2023, with shortages of foreign exchange still weighing on economic activity. Inflation is expected to average 30.3 percent in 2023 and to start declining next year. The authorities stepped up efforts to meet fiscal targets under the PMB, adjusting expenditure to offset a shortfall in revenue, and containing government borrowing to slow money growth. The Reserve Bank of Malawi (RBM) tightened monetary policy to contain inflationary pressures and resumed foreign exchange auctions. Rebuilding international reserves of the RBM has been slow as access to trade credit has remained limited. The authorities are seeking comparable treatment from all official bilateral creditors. The authorities continue to pursue good faith negotiations with commercial creditors to restructure their external debt and are in arrears on commercial debt while these discussions continue.

Request. Having established a track record, as verified under the second (and final) Review of the Staff Monitored Program with Executive Board Involvement (PMB), the authorities are requesting a new 48-month financing arrangement under the Extended Credit Facility (ECF) of 95 percent of quota (SDR 131.86 million, about $178 million) to restore a stable and sustainable macroeconomic position consistent with strong and durable poverty reduction and growth envisaged in Malawi 2063. The arrangement is expected to catalyze grant financing and capital inflows including trade credit.

Main policy commitments. The ECF-supported program will aim at restoring macroeconomic stability, building a foundation for inclusive and sustainable growth (including strengthening resilience to climate-related shocks), and addressing weaknesses in governance and institutions. Fiscal policy will aim at achieving a debt-stabilizing primary balance in the medium-term through a package of expenditure

adjustment and revenue mobilization measures. The authorities are committed to fiscal discipline, containing domestic borrowing, and improving public financial management (PFM). Monetary policy will remain anchored on containing money growth. It will aim to tame inflation by ensuring positive real interest rates. External sector policies will focus on rebuilding international reserves, reducing shortages of foreign exchange, and facilitating a market-determined exchange rate. The authorities are committed to ramp up their efforts to improve data quality and submit data to IMF staff on a timely basis.

Risks to the Program. Further delays in the restructuring of Malawi's external debt would put at risk macroeconomic stabilization. The risks of moving forward with the ECF arrangement without an agreement in principle (AIP) between the Malawian authorities and their commercial creditors are significant. Relying on domestic financing to fill any part of the unidentified financing gap is a risk as the ability of domestic agents (bank and nonbank) to absorb additional government securities is limited. Delays in strengthening PFM and cash management control and in mobilizing domestic revenue could derail fiscal adjustment and add to the deep-rooted governance vulnerabilities. The RBM's program to scale up net foreign exchange purchases and reduce swap arrangements could face delays, jeopardizing the reserve accumulation path and posing risks to Malawi's capacity to repay the Fund. Loss of market confidence could result in drawdown on deposits in the banking sector resulting in a liquidity crunch and rollover risks in the short-term securities market. Spending pressures related to the general election in May 2025 are an added risk.

Staff's views. Staff assesses that the PMB remains on track to achieve its objectives. Staff supports the authorities' request for the ECF arrangement, conditional upon receipt of financing assurances.

Approved By
Costas Christou (AFR) and Bjoern Rother (SPR)

The discussions in Lilongwe took place September 13–21, 2023; the staff team consisted of Mika Saito (head), Nelnan Fidele Koumtingue (resident representative), Erin Nephew, Jens Reinke, Rohan Singh Ahluwalia (all AFR), and Liam Crowley Reidy (SPR); Jacinta Bernadette Shirakawa and Jung Eun Yoon (both AFR) participated in virtual technical meetings preceding the mission; and Steven Banda (local economist) and Moeti Damane (OED) also joined the discussions. The team met with H.E. President Chakwera (virtually), the Hon. Sosten Gwengwe (Minister of Finance, whose term ended on October 7), Dr. Wilson T. Banda (Governor of the Reserve Bank of Malawi, RBM), other senior government and RBM officials, representatives from the private sector and the international community. Camille Bravo assisted with the preparation of this report.

CONTENTS

ANNEXES

APPENDIX

CONTEXT AND RECENT DEVELOPMENTS

1. **Malawi has struggled to sustain growth for decades despite large inflows of official development assistance (ODA).** Those inflows averaged $1.1 billion or 12 percent of GDP per year during 2005-20 (Annex V of the 2021 Article IV Staff Report). And yet, sustaining growth—which averaged 4.9 percent from 2005-20 compared with an average of 5.9 percent in low-income countries in Sub-Saharan Africa—and exiting fragility[1] has been challenging due to frequent natural disasters and droughts and floods that followed extreme storms partly due to years of deforestation. Frequent natural disasters also led to the concentration of public and ODA resources to recurrent spending (including emergency assistance) away from development assistance that is much needed for sustainable growth.

2. **Moreover, macroeconomic imbalances widened significantly due to several years of unsustainable domestic and external borrowing.** Following the 2013 "cashgate" scandal, Malawi lost access to donor support through the budget, which had averaged 4-5 percent of GDP annually.[2] The government replaced this support with domestic borrowing; and the Reserve Bank of Malawi (RBM) substituted aid inflows with foreign exchange swaps and short-term foreign exchange loans. This resort to debt finance for recurrent spending contributed to a rapid accumulation of public debt and foreign currency liabilities abroad.

3. **The past three years have been particularly difficult.** Malawi was hit by multiple shocks: the COVID-19 pandemic, the food and fertilizer prices shock following the war in Ukraine, a cholera outbreak, and three cyclones. In response, the World Bank front-loaded International Development Association (IDA) commitments and disbursements and mobilized nearly an additional $400 million from IDA's Crisis Response Window' and the IMF disbursed nearly $290 million under the Rapid Credit Facility in the past three years. Moreover, the economy has been experiencing the drag from macroeconomic imbalances, partly inherited but partly due to slow progress in correcting unsustainable fiscal and external policies. Despite this sizeable external financing, the large fiscal budget deficit (10.8 percent of GDP in 2022) necessitated domestic financing. This has been addressed in large part through monetary financing, putting pressure on the exchange rate and increasing the rate of inflation.

4. **Growth remains stagnant due to macroeconomic uncertainty and the lingering effects of external shocks.** Real GDP growth is now projected at 1.6 percent in 2023,

[1] Malawi represents a typical case of a fragile state trapped in low growth, high inflation, and greater incidences of extreme poverty relative to low-income countries with little provision of public goods and services largely due to weaknesses in governance and institutions, and capacity and political fragility. Malawi was, however, removed from the list of Fragile and Conflict-Affected States (FCS) when the Fund adopted a new methodology for FCS classification on March 9, 2022.

[2] "Cashgate" was a major corruption case that highlighted misappropriations of aid by civil servants and led to arrests, trials, and convictions.

from 1.7 percent at the time of the first PMB review[3], reflecting continued shortages of foreign exchange, and tighter monetary policy, offset somewhat by stronger-than-expected tobacco exports. Inflation is now expected to average 30.3 percent in 2023, up from 24.8 percent projected at the time of the first review, due to high food inflation and exchange rate passthrough. The authorities have taken decisive action to increase the monetary policy rate by another 200 basis points in August 2023, bringing it to 24 percent, but inflation has remained elevated against a backdrop of large government deficits, largely financed by costly domestic borrowing and monetary financing, and repeated supply shocks.

5. The RBM has continued to struggle to accumulate international reserves and pressure on the exchange rate persists. International banks stopped confirming letters of credit (LCs) in early 2023, and suppliers' credits also dried up in the middle of the year. The RBM has been stepping in to fill the gap in trade credit to priority sectors.

6. Meanwhile, poverty and food insecurity have been worsening. Poverty incidence is one of the highest in Africa, with over 70 percent of the population living below the international poverty line of $2.15 a day at 2017 PPP. Food insecurity is reported to be worsening, with about 22 percent of the population projected to face hunger during the upcoming lean season (October 2023-March 2024), compared to 15 percent during the previous season.[4]

7. Efforts to stabilize the economy are, however, beginning to get traction and show results under the PMB. Although Malawi continues to experience protracted balance of payments (BOP) challenges and remains vulnerable to shocks, a combination of strong policy effort, increased support from the international community, and more favorable weather recently is now beginning to contribute to macroeconomic adjustment. In a pivot from mixed performance at the time of the first review, the authorities have undertaken important corrective actions, and program performance under the second review was satisfactory. Five out of six end-June and continuous Quantitative Targets (QTs) and all three end-June Indicative Targets (ITs) were met. Seven out of 10 Structural Benchmarks (SBs) were not met, but some progress has been made. Revenue is coming in broadly on target, and expenditure has been contained. The target on net international reserves (NIR) was met at end-June, helped by frontloading of foreign project fund inflows, though official international reserve accumulation has stalled since June as access to trade credit has remained limited. Preliminary data show that NIR stood at -US$993.3 million at end-September 2023.

8. Having demonstrated satisfactory performance for the second review of the PMB, and with tangible progress in securing an external debt treatment operation, the authorities have requested an Extended Credit Facility (ECF) arrangement.

[3] On November 21, 2022, the Executive Board approved a disbursement of $88.3 million (SDR 69.40 million) to Malawi under the Food Shock Window, and discussed a 12-month Staff-Monitored Program with Executive Board Involvement (PMB). On July 28, 2023, the Executive Board discussed the first review of the PMB.

[4] Integrated Food Security (2023).

The arrangement will help Malawi address BOP needs, support the ongoing macroeconomic adjustment, and catalyze grant financing and capital inflows including trade credit.

OUTLOOK AND RISKS

9. **The outlook is predicated on staying on track with the macroeconomic adjustment program.** Near-term growth remains constrained by a sharp macroeconomic adjustment envisaged under the program. Under the proposed program of macroeconomic adjustment and reforms, growth is projected to pick up next year and reach 4.5 percent by 2027 (Text Table 1 and Table 1). Key to generate sustainable and inclusive growth would be to make a smooth transition from demand- to supply-driven private-sector led growth (Section F). Given population growth at about 3 percent, however, Malawi's economy will grow only gradually in terms of per capita income. Inflation is projected to decline gradually and reach single digits only in 2026.
The relatively slow disinflation is pinned down by the pace of feasible fiscal adjustment for Malawi's very fragile economy (Section A). Fiscal adjustment is designed to bring down domestic bank borrowing from 30-40 percent to 10 percent of broad money over three years, supporting the deceleration of money growth, and thereby alleviating pressure on the exchange rate and

Text Table 1. Malawi: Macroeconomic Adjustment Program, 2023–27

	2023	2024	2025	2026	2027	Adjustment
	FY22/23	FY23/24	FY24/25	FY25/26	FY26/27	
Real Sector (percent change)						
Real GDP Growth	1.6	3.3	3.8	4.3	4.5	
Inflation - Annual Average	30.3	27.9	14.7	8.1	6.8	
Central Government (percent of GDP on a fiscal year basis)						
Revenue	17.2	17.2	18.4	18.8	17.6	
Domestic revenue excl. RBM dividend	13.3	13.4	14.4	15.4	15.6	2.3
Expenditure and net lending	28.9	27.9	26.5	25.9	23.3	
Domestic primary exp. excl. RBM recap.	15.7	14.0	13.2	13.1	12.6	-3.1
Overall balance	-11.7	-10.7	-8.1	-7.1	-5.7	5.9
Domestic financing (net)						
o/w Banking system borrowing	5.4	6.6	2.8	1.8	2.2	
o/w Banking system borrowing (% of M2)	33.3	39.9	17.5	10.5	12.4	
Money and Credit (Percent change)						
Broad money	30.5	29.3	17.9	12.2	11.2	
Credit to the private sector	19.6	11.2	5.8	8.9	9.1	
Balance of Payments (Percent of GDP, unless otherwise indicated)						
Current account	-7.6	-8.5	-9.9	-9.0	-8.2	-0.5
Gross official reserves	394	714	967	1,081	1,133	
(months of imports)	1.8	2.9	3.9	4.1	4.2	
Net international reserves	-1,052	-667	-468	-366	-306	
Financing gap (million U.S. dollars)	706	350	200	236	107	1,599
Debt Stock and Service (percent of GDP)						
External debt	39.3	35.2	33.8	31.2	28.8	
Total public debt	81.3	75.0	74.8	73.5	71.8	

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

containing the passthrough. Preliminary data indicate that the bulk of the adjustment in the current account balance (i.e., the national saving-investment gap) has already taken place with the deficit narrowing from about 15 percent of GDP in 2021 to 7.6 percent in 2023. Absent further revisions to the BOP data, no further external adjustment is required during the course of the proposed ECF program, allowing the authorities to focus on a sizeable 6 percentage-point (ppt) of GDP adjustment in the overall fiscal deficit. The rebalancing of public to private demand (and the rebalancing of consumption to investment demand) would allow for an increase in private sector investment (net of saving), enabling private-sector led growth. The programmed buildup in international reserves would reduce Malawi's vulnerabilities to external shocks and create the conditions for renewed capital inflows, including the resumption of trade credit.

10. The balance of risks remains tilted to the downside (Annex I). The risks of deferring policy adjustments or a prolonged debt restructuring process remain high. Weaker-than-expected policy implementation would result in wider financing gaps, greater monetary financing of fiscal deficits, and further and prolonged pressure on inflation and the exchange rate, and thus would undermine efforts to restore macroeconomic stability. Other risks to the outlook include further weather-related shocks or another surge in food, fuel, or fertilizer prices. Upside risks include a faster-than-anticipated macroeconomic impact of policy actions, successful export diversification (including faster-than-expected development of mining projects) and formalization of informal activity, and budget overperformance.

POLICIES SUPPORTING THE PROGRAM

The ECF-supported program will aim at restoring macroeconomic stability, building a foundation for inclusive and sustainable growth (including strengthening resilience to climate-related shocks), and addressing weaknesses in governance and institutions.

A. Creating a Sustainable Fiscal Position

Background

11. Partly due to lack of domestic revenue mobilization and weak public financial management (PFM), revenue shortfalls have been repeatedly filled by unplanned domestic borrowing. An increase in debt service continues to erode fiscal space and increase overall fiscal deficits. Government securities were initially absorbed by resident banks and later by nonresident banks, which led to a rapid increase in external non-concessional debt.

12. The authorities met fiscal targets for the second PMB review, adjusting expenditure to offset a shortfall in revenue, and containing government borrowing to slow money growth. This reflects a marked turn-around in performance from the first review, when fiscal targets were missed. For the first quarter of the fiscal year (April-June), spending remained within the budgeted envelope; however, revenue and financing were lower than expected. Monthly data suggest that spending also remained within the budgeted envelope for the first month of the second quarter of the fiscal year.

13. The authorities also made substantial progress in implementing PFM reforms. To contain expenditure, the authorities now announce quarterly allotments aligned with both the agreed macroeconomic framework and the outturns for revenue, grants, and financing. Ministries, Departments and Agencies (MDAs) may then commit up to this amount through the Integrated Financial Management Information System (IFMIS), however, commitments are not yet being done consistently through IFMIS. MDA payments are limited to monthly cash releases, aligned with allotments, to demonstrate commitment to stronger expenditure control reforms, reducing the risk of accumulating new payment arrears. The extension of this practice to all MDAs was done through announcement in the 2023-24 Budget Policy Statement and has been executed since the beginning of FY2023/24. The authorities began publishing IFMIS reports in October 2023 (see MEFP ¶28 Text Table 2). The Prior Action on rolling out core functionalities of IFMIS to key MDAs with mandatory use has been met, but the authorities continue to work with MDAs on compliance, and IMF staff are continuing to work with the authorities to ensure consistent coverage of transactions.

Key Elements of the ECF-supported Program

14. Fiscal policy will aim at achieving a debt-stabilizing primary balance in the medium-term through a package of revenue mobilization and expenditure adjustment measures. The authorities are committed to fiscal discipline, containing domestic borrowing, and improving PFM. Fiscal policy will be anchored on reaching a debt-stabilizing primary balance as soon as possible, but no later than the end of the program period. The envisaged fiscal adjustment over the FY2023/24–FY 2026/27 program period would be 6 ppts of GDP in terms of overall fiscal balance (Tables 2a and 2b) or 5.4 ppts in terms of domestic primary fiscal balance—1.35 ppt of GDP per year. Fiscal adjustment will be front-loaded, with 1.8 ppts of GDP adjustment in the domestic primary fiscal balance in the first year of the program.

15. This fiscal adjustment path will be supported by various policy measures. The authorities have committed to revenue-enhancing measures in the short term, and also expect several ongoing tax administration measures to start bearing fruit (MEFP ¶20 Text Table 1). For FY2023/24, fiscal consolidation efforts are focused on: (i) stepping up implementation of the Domestic Revenue Mobilization Strategy (DRMS), which aims to increase revenue by 5 ppts of GDP in five years (MEFP ¶22) in a timely manner; (ii) rationalizing and prioritizing expenditures; (iii) introducing and implementing sound commitment control measures; and (iv) implementing well-targeted measures to support low-income households. Moving forward, measures will focus on revenue mobilization. This will include operationalizing a specific tax on secondhand cars (Prior Action (PA)), repealing value-added tax (VAT) relief on motor vehicles for current and former politicians, senior public officials, judges, and other similarly privileged individuals and groups (SB), ensuring that every supply of a motor vehicle is standard rated for VAT purposes (SB), and comprehensively eliminating other VAT exemptions on business inputs and building materials (SB). Taxing motor vehicles will not only raise revenue but will also help contain further drains on international reserves (Section C and Annex II). The full launch of the Integrated Tax Administration System (ITAS) (SB) will enhance revenue collection and improve tax and customs compliance culture. There remains little space for further cuts to primary expenditure, but the authorities are committed to the rationalization of the wage bill and the Affordable Input Program (AIP) (fertilizer subsidies) (MEFP ¶26). Implementation of IFMIS, and institutionalizing reporting and controls, will remain key for budget execution and commitment control, as there is no room for fiscal slippage. The authorities have also prepared a contingency plan as a prior action to close the financing gap in case the baseline fiscal path faces implementation challenges.

B. Achieving Price Stability and Safeguarding Financial Sector Stability

Background

16. Money growth and the rate of inflation have levelled off but remain elevated (Figure 1). Driven by net claims on government, broad money grew 34.2 percent year-on-year in August 2023. Growth in the monetary base has been volatile, increasing to 49.5 percent year-on-year in August partly because of an increase in the Liquidity Reserve Ratio (LRR) after April 2023 in the effort to contain broad money growth. But the RBM has struggled to drain excess liquidity, given strong demand from the banking system and illiquidity in the secondary market for government securities. This has seen the RBM's holdings of government securities continue to increase in 2023.

17. The banking sector remains stable and profitable, though exposure to government securities continues to increase (Table 5). The sector[5] remains financially sound with adequate capital, strong earnings, and sufficient liquidity despite deterioration in asset quality. In particular, earnings continue to grow: the sector's profit after tax (PAT) increased by 95 percent year-on-year to K124 billion (1 percent of GDP) at end-June 2023. Growth in income was largely due to a rise in interest income, as the banking sector balance sheet structure continues to be dominated by investments and securities (48 percent of total assets). Profitability is also reflected in the capital market.[6] The total market capitalization almost doubled from MK2.7 trillion (US$2.6 billion) at end-June 2022 to MK5.9 trillion (US$5.6 billion) at end-June 2023, exceeding banking sector total assets (MK4.1 trillion). The increase was mostly driven by share price gains.

Key Elements of the ECF-Supported Program

18. The RBM has committed to forcefully and proactively tighten monetary policy as needed to contain inflationary pressures. Monetary policy will remain anchored on

---

[5] There are eight banks in Malawi: five foreign-owned and three domestic. Four out of five foreign-owned banks are resident banks. In terms of market share, two banks are dominant, accounting for 46 percent of sector-wide assets.

[6] There are 16 listed companies on the Malawi Stock Exchange, six of which are banks or holding companies and two are telecom companies. In term of market share, these eight companies account for 78 percent of total market capitalization.

containing money growth (Tables 3a and 3b). It will aim to tame inflation by ensuring positive real lending rates on average.

19. The RBM will refine its monetary operations to contain direct exposures to the government and strengthen its capacity to manage banking sector liquidity. This will include greater use of repo for Open Market Operations (OMOs) and the introduction of less favorable terms for its rediscounting facility (which purchases government securities in response to individual banks' liquidity needs). Restoring the functioning of the secondary market for government securities will further support these efforts (MEFP ¶29).

20. The authorities plan to strengthen financial sector oversight and closely monitor risks to financial stability. This will include careful monitoring of any further increases in the exposure of the banking sector to the public sector, in an environment of rising interest rates, and a reassessment of the loan and collateral quality needs of domestic banks.

C. Rebuilding International Reserves and Normalizing the Market for Foreign Exchange

Background

21. Malawi has continued to suffer from shortages of foreign exchange and protracted BOP challenges. Notwithstanding ongoing revisions to the trade data (which are expected to see 2022 imports revised higher), imports have yet to recover to 2021 levels (Tables 4a and 4b). Exports have been supported by a strong tobacco season. But the current account remains in deficit, at a projected 7.6 percent of GDP in 2023, and foreign exchange entering the country is frequently hoarded in light of high levels of macroeconomic uncertainty. This has resulted in intermittent shortages of fuel, fertilizer, cement, and other goods.

22. Pressure on the Kwacha has resulted in a widening spread, of over 52 percent on October 13, between the official rate and that offered at foreign exchange bureaus. At the same time, other parallel rates, for example in the interbank and informal markets, have emerged in response to the difficulty of acquiring foreign exchange at the official rate (see Annex III). In June, the RBM restarted monthly purchases of foreign exchange via auction to aid price discovery, facilitating a 15 percent depreciation against the US dollar during June-September 2023. Participation of authorized dealer banks in these actions has been broad-based, although volumes transacted have been small.

23. Against this backdrop, the RBM has struggled to rebuild its international reserves. Preliminary data show that gross international reserves declined to US$156.1 million (0.6 months of import cover) by end-September 2023, in response to selling pressure to meet demand from fuel importers, who have struggled to acquire trade credit amidst growing demand which grew by 1.6 times in volume and 2.7 times in U.S. dollar value between 2016 and 2022 (see Annex II).

Key Elements of the ECF-Supported Program

24. The RBM will take steps to durably rebuild its international reserves to reduce external vulnerabilities as quickly as possible. The Bank has committed to allow greater flexibility in the exchange rate in order to reduce foreign exchange shortages, facilitate easier accumulation of international reserves, and improve trading conditions in the interbank market. It will increase its purchases of foreign exchange and refrain from interventions, such as unplanned foreign exchange sales to the market, until the level of international reserves reaches at least 4 months of import cover. To support this objective, the RBM will strengthen accuracy of its program monitoring data by (i) instituting a policy to have external auditors verify NIR data within 10 weeks after each test date and will ensure timely submission to Fund staff of the audited NIR results, and (ii) continuing to submit monetary data through standard reporting forms to the Fund on a regular basis (MEFP ¶37). The RBM submitted to the IMF staff audits of NIR from end-September 2022, end-December 2022, end-March 2022, and end-June 2023 (PA).

25. Greater flexibility in the exchange rate will be supported by reforms to the RBM's foreign exchange operations. The RBM has announced as a prior action changes to its operations (i) to increase the frequency of its purchases of foreign exchange via auction to at least a fortnightly basis and to remove any implicit or explicit constraints on access, allotments, or prices submitted; (ii) to allow intermediaries to trade in the foreign exchange market at freely negotiated rates between themselves and their clients; and (iii) if the RBM were to conduct sales of foreign exchange, sales should be done via auction in line with the recommendations of "The Review of the Fund's policy on Multiple Currency Practices—Proposals for Reform", paragraph 15.

26. A sufficient reserve buffer, steady inflows of on-budget aid, and the resumption of trade credit should reduce RBM's dependency on foreign exchange swaps to manage intra-year liquidity constraints. In the near term, the RBM is planning to replace foreign exchange swaps with nonresidents with swaps with residents to reduce rollover risks and to lower funding costs, consistent with plans to reduce its open swap position in the medium term.

27. Greater exchange rate flexibility will be accompanied by expenditure-switching measures to contain BOP pressures. Fuel consumption grew on average 7.7 percent during the past 6 years, partly driven by a rapid increase in imports of used motor vehicles, which more than doubled during the same period (Annex II). Some of the authorities' fiscal policy measures (e.g., operationalizing a specific tax on secondhand cars (PA), repealing VAT relief on motor vehicles for privileged individuals and groups (SB) in ¶15) will also help contain motor vehicles and fuel imports and in turn BOP pressures. Some other measures such as (i) raising import duty, VAT, and excise taxes on motor vehicles to raise the price of motor vehicles to (at least) the regional average, (ii) timely updating the fuel prices to be in line with global prices, and (iii) raising fuel taxes should be considered especially given the persistent lags in upward revisions of fuel prices.[7]

[7] World Bank (2023) *Malawi Economic Monitor*, July (p. 25).

The authorities are planning to adjust the fuel price and committed to adopt (i) and (iii) as soon as possible but no later than the passage of the FY2024/25 budget (MEFP ¶31). To improve tracking of strategic imports, the NSO will start to include reconciled data on imports or strategic commodities in the monthly Trade Bulletin (SB).

28. Under the program, the government will issue a zero-coupon promissory note to recapitalize losses made by the RBM on its net foreign asset position due to fluctuation of the exchange rate as required by the RBM Act. RBM's losses on its foreign exchange position (3 percent of GDP at its peak in FY2023/24) are projected to increase as long as the RBM's net foreign asset position remains negative and the Kwacha loses value against foreign assets. This is transparently documented in the fiscal tables (Tables 2a and 2b).

D. Restoring Debt Sustainability and External Viability

Background

29. Malawi's external debt is unsustainable but would be considered sustainable on a forward-looking basis if the government is successful in its restructuring strategy. The authorities remain committed to bringing external public debt back to a moderate risk of debt distress in the medium term through a combination of policy adjustment, financing, and debt treatment. Under the authorities' external debt strategy, which remains consistent with that announced at the time of approval of the PMB in November 2022, all external solvency and liquidity ratios in the Debt Sustainability Analysis cross their respective thresholds under the baseline forecast in the next five years.

30. Malawi is seeking comparable treatment from all official bilateral creditors. The authorities continue to pursue good faith negotiations with commercial creditors. Malawi is in arrears on commercial debt while these discussions continue.

31. Domestic debt is an increasing source of strain. The domestic interest bill is 5.0 percent of GDP in FY2023/24 and is projected at 5.9 percent of GDP in FY2024/25 (or 35.6 percent and 37.6 percent of domestic revenue, respectively), even if Malawi were to be successful in restructuring its external debt.[8] The risks associated with any fiscal slippage or other shocks are heightened in the context of impaired functioning in the market for government securities (Section B).

Key Elements of the ECF-Supported Program

32. Timely completion of Malawi's external debt restructuring process will ensure a moderate risk of external debt distress in the medium term and reduce near-term debt service needs. All conditions under the Lending-Into-Arrears (LIA) policy are met with respect

[8] The baseline (pre-restructuring) scenario (Tables 2a and 2b) assumes that domestic financing is used to cover the residual external financing gap, overstating the size of the domestic interest bill.

to AFREXIM and TDB since (i) prompt Fund support is considered essential for the successful implementation of Malawi's adjustment program, and (ii) Malawi is pursuing appropriate policies articulated in the LOI/MEFP and is making a good faith effort to reach collaborative agreements with its commercial creditors. With respect to (ii), the authorities have engaged with commercial creditors in good faith, by engaging in an early dialogue with creditors, sharing relevant information with all creditors on a timely basis and providing creditors with an early opportunity to give input on the design of restructuring strategies. The authorities are committed to continue working with all creditors to achieve a debt treatment consistent with program parameters, and that commercial debt will be repaid or restructured only on terms that are consistent with the parameters of the ECF-supported arrangement (MEFP ¶35).

33. The authorities are taking steps to contain borrowing and enhance transparency of contracting and guaranteeing external debt. This will be achieved by improving PFM (MEFP ¶28) and debt management capacity (MEFP ¶36). Guaranteeing and contracting nonconcessional external debt is subject to a continuous zero ceiling performance criterion, and the ceiling on guaranteeing and contracting concessional debt is provided under the program (MEFP Table 3).

34. Domestic revenue mobilization (¶14) and containing the growth of the budget envelope (¶13) are envisaged to reduce domestic (bank and nonbank) borrowing. The net domestic borrowing from the banking system will fall from 5 percent of GDP to 3 percent of GDP over the program period (see the accompanying Debt Sustainability Analysis).

E. Addressing Weaknesses in Governance

Background

35. Weaknesses in governance and institutions of the Ministry of Finance and the Central Bank have serious macroeconomic consequences. For instance, lack of transparency and accountability of fiscal budget execution has contributed to macroeconomic imbalances accumulated since 2012, leading to unsustainable debt and pressures on the exchange rate and inflation. Foreign exchange interventions by the RBM have also led to a rapid increase in external liabilities of the RBM, the custodian of Malawi's foreign exchange reserves, and led to an increase in vulnerabilities of the country against external shocks.

36. The authorities have taken numerous actions since the audit on COVID-19 spending to prevent recurrences of misappropriations of funds in the future. They have published a follow-up report, detailing corrective actions and measures taken to pursue and respond to audit findings, including the follow-up of alleged misappropriation of funds, as well as the coverage of a second audit findings (PA). To avoid recurrence of the misappropriation of government resources, all payments across government MDAs are, since 2021, exclusively being done through Electronic Funds Transfer (EFT).

37. Governance weaknesses at the Export Development Fund (EDF)—a wholly owned subsidiary of the RBM—has been a drain on international reserves and a risk to the

government in terms of contingent liabilities. The authorities have closed the Commodity Market Making Unit of the EDF, which was one of the key sources of past credit losses (MEFP ¶39). The RBM will improve transparency and management of the EDF via improved organizational arrangements and action on audit findings (SB).

Key Elements of the ECF-Supported Program

38. Fiscal transparency should continue to be the cornerstone of Malawi's governance efforts. Continuing to develop and refine timely, accurate, and reliable fiscal data, and making it readily available to the public, will be an important step toward addressing Malawi's governance challenges. Malawi will also undergo a Governance Diagnostic TA over the next 9-12 months and will follow up on its recommendations with an Action Plan (SB and MEFP ¶40). Its effectiveness would be supported by the implementation of other measures previously committed by the authorities (on digitalization and publication of asset declarations and coordination of domestic anti-corruption efforts, MEFP ¶41).

39. The RBM has committed to amend the RBM Act in consultation with Fund staff (SBs). The RMB is also committed to merge the EDF with the Malawi Agricultural and Industrial Investment Corporation, PLC (MAIIC) which is a development financial institution with similar mandate but with the joint ownership of the Government of Malawi, the private sector and international financial institutions and investors (MEFP ¶39, SB).

F. Sustainable Growth and Climate Resilience

Background

40. The little growth the country reaped has been on the demand side of the economy. External and domestic borrowing has been financing recurrent spending in normal times and emergency spending following natural disasters. Fundamentally shifting Malawi's growth model from a consumption-driven to a production-driven one and from a government-led to a private-sector-led one are the core principles of the country's long-term growth strategy "Malawi 2063". The recent growth has been, however, consumption-led growth with strong import growth supported by massive external borrowing and an overvalued exchange rate.

Key Elements of the ECF-supported Program

41. The medium- to long-term growth needs to be underpinned by macroeconomic stabilization and structural reforms. A recovery across all sectors, including the resumption of electricity generation at the Kapichira hydropower plant, will support the manufacturing sector. The agricultural sector also needs to switch from subsistence farming to farming for cash crops supported and facilitated by well-functioning markets and infrastructure connecting the country.

42. Moreover, the long-term growth needs to build resilience to weather-related shocks, given Malawi's vulnerability to climate change. The authorities will continue to engage development partners on the Country Climate and Development Report (CCDR). The authorities have committed to finalize the Disaster Risk Management regulations and related policies (SB).

G. Capacity Development

43. Capacity development efforts will continue to focus on PFM, domestic revenue mobilization, bank supervision and regulation, and statistics (Annex IV). In the area of PFM, the authorities are beginning to produce comprehensive fiscal reports (revenue, expenditure, and financing) in a timely manner, following the engagement of a long-term expert who was posted for four years through April 2023, and with ongoing short-term missions. On domestic revenue mobilization, the Malawi Revenue Authority (MRA) also had a long-term expert (LTX) for several years, and yet tax revenue to GDP ratio remains well below SSA average. Domestic revenue mobilization will be a cornerstone of the ECF-supported program. Significant efforts have been made to modernize the monetary policy framework and have gained traction and yielded results. However, price stability has been achieved in the past several years largely by fixing the exchange rate. Capacity development in improving the quality and regular reporting of data on national accounts, monetary and financial sector, BOP, international reserves, and government finance has gained traction. A special emphasis will be placed on BOP data during the ECF-supported arrangement. Technical assistance will continue to be delivered in a carefully sequenced manner to avoid overwhelming the limited capacity of the authorities.

PROGRAM MODALITIES

Access and Duration

44. Staff propose access of SDR 131.86 million or 95 percent of Malawi's quota over four years. The level of access is appropriate given Malawi's strong and upfront policy adjustment to address its macroeconomic imbalances (Table 6), restore debt sustainability, and rebuild fiscal and external buffers. This access level for the given duration would be within the normal annual and cumulative access limits. It would be equivalent to 11 percent of total external financing gap (Text Table 2), which would help catalyze donor financing and facilitate burden sharing. Access under the program is evenly distributed except for the first and the last reviews (Table 7) to ensure even distribution across the fiscal year from FY2023/24 through FY2027/28 as this access includes 30 percent of each disbursement allocated to direct budget support given Malawi's urgent fiscal needs. Staff assesses that the Lending into Arrears (LIA) policy would apply in this case, given that Malawi is in arrears on its commercial debt and continues to make a good faith effort to reach a collaborative agreement with creditors.

Text Table 2. Malawi: External Financing Gap, 2023–27

	2023-24		2023-27	
	US$ mn	% of total	US$ mn	% of total
Financing gap	1,056	100	1,599	100
IMF ECF	53	5	178	11
Grants/loans (disbursed in 2023)	106	10	106	7
Prospective grants/loans	221	21	329	21
Prospective debt relief	676	64	987	62
Official Bilateral	39	4	99	6
Commercial	636	60	887	55

Sources: Malawian authorities; and IMF staff estimates.

Financing

45. Malawi owes arrears of $418 million on commercial external debt as of end-September 2023. Malawi has engaged in an early dialogue with its creditors and shared relevant information with all of its creditors on a timely basis. Malawi also provided its private sector creditors with opportunities to give input on the design of restructuring strategies. Staff judge that the authorities have made good faith efforts in their debt restructuring discussions and meet the requirements of the Fund's Lending Into Arrears (LIA) policy.

46. The Malawian authorities are seeking comparable treatment from all official bilateral creditors. The Malawian authorities are committed to continue working with all official bilateral and commercial creditors to achieve a debt treatment consistent with program parameters, and staff expects that Malawi's debt to official bilateral creditors will be treated on comparable terms. Fund support is considered essential for the successful implementation of the member's adjustment program and the Malawian authorities are pursuing appropriate policies and are making a good faith effort to reach a collaborative agreement with their commercial creditors which is expected to restore debt sustainability. Arrears are a form of financing for the program. In addition, considering the expected implementation of debt treatments on both official and commercial debt, staff assesses the debt to be sustainable on a forward-looking basis. Staff will continue to assess progress in restructuring as part of the regular financing assurances reviews at each program review.

Poverty Reduction

47. The program will help to address poverty and strengthen growth over the medium term in accordance with the Malawi 2063. The Malawi 2063 aims for Malawi to reach upper-middle income status by 2063. It focuses on inclusive economic growth on three fronts: poverty reduction, human capital investment, and resilience of physical capital to climate shocks, including in the agricultural sector.

Program Monitoring

48. Program performance will be monitored through semi-annual reviews with proposed performance criteria targets (PCs) and indicative targets (ITs) (Table 8 and MEFP Table 3), and SBs (Table 12 and MEFP Table 5).

Capacity to Repay the Fund (Enhanced Safeguards ES1B)

49. Malawi's capacity to repay the Fund would become adequate—but with significant risks—subject to full program implementation of the ECF supported program and the completion of debt restructuring (Table 9). Several indicators on capacity to repay remain above the 75th percentile of past UCT-quality arrangements for PRGT programs during most of the program period (Figure 3). Total outstanding credit to the IMF is projected at about 240 percent of quota by end-2023, equivalent to 31.3 percent of exports, and about 113.7 percent of gross international reserves. Total credit outstanding as a percent of gross international reserves peaks in the beginning of the program, which is 5-6 times the median PRGT arrangement, and gradually converges towards the 75th percentile of past PRGT arrangements over the next 10 years—as Malawi continues payments to the Fund and accumulates international reserves. Total repayments to the IMF are also significant in 2023 (2.8 percent of exports and 10.0 percent of gross official reserves, well above the 75th percentile of the indicators) and would peak at 4.1 percent of exports and 3.9 percent of revenue in 2026.[9] Commitments by official creditors to provide additional concessional financing or grants, the authorities' track record of servicing debt obligations to the Fund, and their strong commitment to implement the needed macroeconomic adjustment are all critical to mitigate risks.

Debt Sustainability and Debt Vulnerabilities (Enhanced Safeguards ES1A and ES2)

50. There is no buffer of restructurable debt. The size of Malawi's de facto senior debt plus other multilateral and collateralized debt as a share of total external debt is 77 percent at program initiation (Table 10) and is projected to increase to 90 percent by 2025 under the baseline scenario.

51. Debt vulnerabilities will be reduced under the program. All four debt burden indicators over the course of the program are on a downward path. Such a path is underpinned by fiscal adjustment, limits on concessional and non-concessional external debt, programed winding down of the RBM's foreign currency swaps, as well as measures to contain fuel and motor vehicles imports.

Risks to the Program

52. Implementation risks remain elevated given Malawi's limited capacity, repeated implementation slippages under the PMB, and misreporting under the previous

[9] The capacity to repay assessment incorporates the plan of the authorities to pay back the SDR allocation by 50 percent in 2026 and fully by 2027 in relation to the authorities' debt restructuring plan and the RBM's reserve management plan.

ECF arrangements. Further delays in the restructuring of Malawi's external debt would put at risk macroeconomic stabilization. The risks of moving forward with the ECF arrangement without an agreement in principle between the Malawian authorities and their commercial creditors on over $877 million (55 percent of total financing gap) of debt relief in line with program parameters are significant. Relying on domestic financing to fill any part of the unidentified financing gap is a risk as the ability of domestic agents (bank and nonbank) to absorb additional government securities is limited. Delays in strengthening the PFM and cash management control and in mobilizing domestic revenue could derail fiscal adjustment and add to the deep-rooted governance vulnerabilities. The RBM's program to scale up net foreign exchange purchases and reduce swap arrangements could face delays, jeopardizing the reserve accumulation path and posing risks to Malawi's capacity to repay the Fund. Loss of market confidence could result in drawdown on deposits in the banking sector resulting in a liquidity crunch and rollover risks in the short-term securities market. Spending pressures related to the general election in May 2025, especially to extend government guarantees or contract external debt, are an added risk.

Safeguards Assessment

53. The RBM has made progress in implementing the 2021 safeguards assessment's recommendations and work is underway to address the remaining areas. The 2021 update safeguards assessment found deterioration of safeguards at the RBM since the 2018 assessment, reflecting, inter alia, findings on misreporting. This included weakened governance and oversight arrangements. A comprehensive governance and legal reform is required to strengthen RBM's internal "checks and balances". Moreover, the RBM's operational autonomy should be safeguarded, including by prohibiting it from conducting quasi-fiscal activities. Remaining recommendations relate to (i) strengthening the role of RBM's Board in the approval of key institutional policies; (ii) approval of a revised reserves management framework, and (iii) submission of audited NIR results (PA). An update safeguards assessment, in connection with the new ECF arrangement, is tentatively scheduled for end-2023.

54. The audit of NIR for end-December 2022 and end-June 2023 conducted as a prior action show a slightly less negative NIR position than the authorities' calculations, mainly reflecting the authorities' more conservative assumptions around the calculation of projected foreign currency drains (FCD).[10] Reported reserve assets of the RBM (RA) are mostly aligned with audited RA for all four periods audited: end-September and end-December 2022, and end-March and end-June 2023. For instance, reported end-December 2022 reported RA was $119.6 million while audited RA was $120.9 million, and the deviations were due to valuation adjustments and timing.[11] Reported FCD were, however, biased upward mostly to be conservative on anticipated FCD relative to FCD that the auditor calculated.[12] This bias has

[10] See International Reserves and Foreign Currency Liquidity (IMF 2013) and Standardized Statistical Definition of Net International Reserves for the concept of FCD.

[11] Given the timing of the audit completed, the macroeconomic framework is still using the reported gross reserve assets for this report. It will be revised for the first review.

[12] For two audited periods in 2022, deviations were particularly large over a failed state-owned enterprise that was anticipated to trigger a forex payment of the government and the undrawn balance on a trade credit facility: the

(continued)

resulted in a downward bias in reported NIR position relative to the NIR calculated by the auditor. An upward bias in the FCD in itself may not be an issue, but the bias has also resulted in an upward bias in the change in NIR for both periods; $49.1 million and $ 2.8 million for end-December 2022 and end-June 2023 QT, respectively. Going forward, the audit should be completed within 10 weeks after the test date so that the audited numbers are available at the time of relevant review missions.

Article VIII

55. Malawi maintains four multiple currency practices (MCP) and three exchange restrictions subject to Fund jurisdiction (Informational Annex).[13] The authorities have requested, and staff supports a temporary approval of the four MCPs and three exchange restrictions, as the approval criteria are met. The MCPs are maintained for BOP reasons, they are temporary, Malawi is endeavoring to eliminate its BOP problems, and they do not give Malawi an unfair competitive advantage. The exchange restrictions are equally maintained for BOP purposes, they are not discriminatory, and they are temporarily used while Malawi is seeking to eliminate the need for them through this program. The authorities have committed to removing the MCPs and exchange restrictions as soon as BOP conditions permit (MEFP ¶32) (SB).

STAFF APPRAISAL

56. Performance under the second PMB review was satisfactory. In a pivot from mixed performance at the time of the first review, the authorities have undertaken important corrective actions, and there are signs that macroeconomic adjustment is now taking place. Having achieved satisfactory performance for the second review under the PMB, and with tangible progress on securing a debt treatment operation, an Extended Credit Financing (ECF) arrangement will support the ongoing macroeconomic adjustment, catalyze grant financing, and provide a framework for structural reforms.

57. Successful external debt restructuring is vital as there is no reasonable mix of adjustment and financing alone that can deliver macroeconomic stability. The Malawian authorities are seeking comparable treatment from all official bilateral creditors and continue to pursue good faith negotiations with commercial creditors. However, time is of the essence for debt relief, as further delays would result in greater financing gaps, which could then only be closed at an undesirably high cost to the population.

58. Fiscal discipline, supported by a robust PFM system and timely production of comprehensive fiscal reports, remains critical. Much progress has been made in this area, and fiscal consolidation plans, consist of enhanced revenue mobilization and expenditure rationalization, will need to be supported by strong cash management and commitment controls.

RBM was including both as anticipated forex payments in FCD, but the auditor included neither as they were not in the confirmation of the creditor.

[13] The MCPs will be assessed under the new MCP policy once it comes into effect.

The authorities have now built a good foundation; steadfast commitment to continued implementation and improvement will be critical.

59. As there is no room for fiscal slippage, concerted effort by the authorities and other domestic stakeholders to prepare for fiscal financing challenges is important. Domestic debt service is now eroding much-needed fiscal space, compromising already-limited delivery of public goods and services and ultimately, the attainment of Malawi 2063, putting pressure on money growth, the exchange rate, and inflation. With very limited scope for additional external financing (grants, concessional loans, external debt relief), strong efforts would be needed to avoid slippages and be ready to address potential financing pressures.

60. Price stability is critical to prevent a further erosion of purchasing power. The RBM needs to persist in its efforts to reduce inflation and anchor inflation expectations by containing reserve money growth, aligning the policy rate with inflation to ensure positive real costs of borrowing, and raising required reserves if needed. The RBM should also remain vigilant to safeguard financial sector stability, given the banking sector's large exposures to government.

61. Rebuilding buffers is critically important to bring back trade credit and to reduce Malawi's vulnerability to external shocks. The RBM's commitment to rebuild its international reserves requires implementation of its strategy to wind down unsustainable policies, including excessive use of foreign exchange swaps and sales of foreign exchange to support strategic imports in the absence of trade credit. Quickly rebuilding RBM's international reserve assets will be critical to restoring the normal functioning of trade credit and the steady supply of essential commodities in the country with little foreign exchange intervention by the RBM.

62. Addressing weaknesses in governance and institutions will be important. The authorities should press ahead with the implementation of their anti-corruption agenda, document progress on recent audits, and publish and reconcile strategic imports data. The upcoming governance diagnostic technical assistance should be used to shape future plans in improving governance and institutions.

63. Fundamentally shifting the sources of Malawi's growth is critical. Shifting Malawi's growth from a consumption-driven to a production-driven one and from a government-led to a private-sector-led one are the core principles of Malawi 2063 and are vital to make Malawi's growth inclusive, sustainable, and resilient to climate-related shocks. In this regard, measures to contain demand for used motor vehicles and fuel imports are urgently needed.

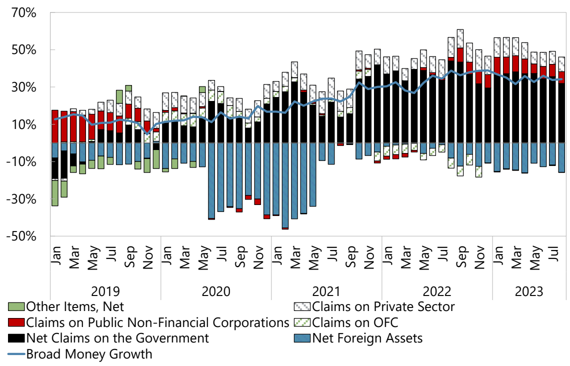
64. Staff assess the PMB remains on track to achieve its objectives. In view of Malawi's large balance of payments needs and based on the strength of the proposed program, the prior actions taken by the authorities, and conditional upon receipt of financing assurances, staff support the authorities' request for a 48-month ECF arrangement with access of 95 percent of quota (SDR 131.86 million, $178 million).

Figure 1. Malawi: Inflation, Money, and Exchange Rate Developments, 2014–23

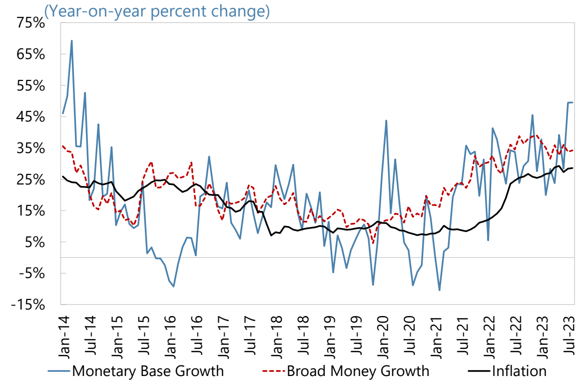
Net claims on the government continue to be the largest contributor to broad money growth, but…

monetary growth and in turn inflation may be decelerating from respective peaks.

Contribution to Broad Money Growth
(Year-on-year percent change)



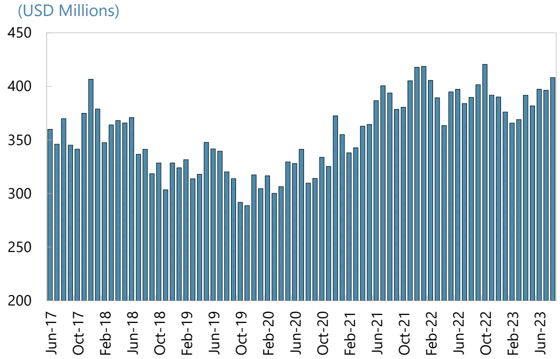
Inflation and Money Supply, Jan 2014-Aug 2023
(Year-on-year percent change)



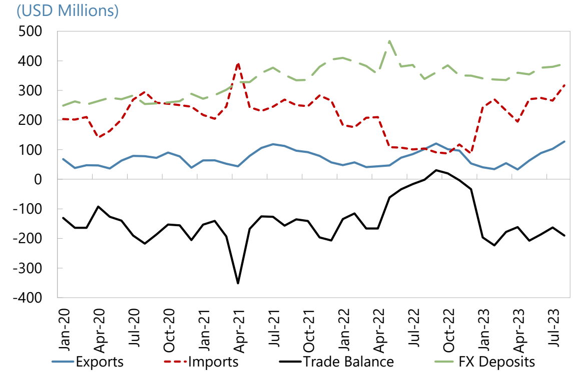
Moreover, the Authorized Dealer Banks (ADB)'s foreign currency deposit (FCD) is rising during the tobacco season…

while reported imports remain depressed.

ADB FCD, Jun 2017-Aug 2023
(USD Millions)



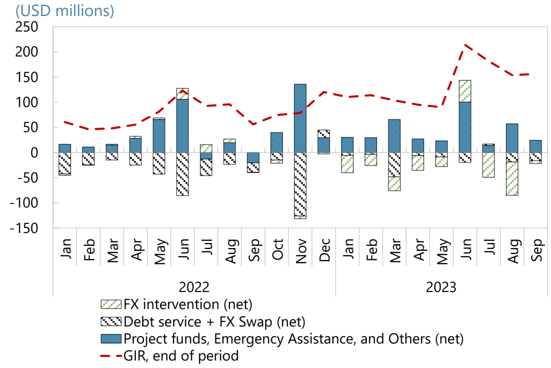
Trade and FX Deposits, Jan 2020-Aug 2023
(USD Millions)



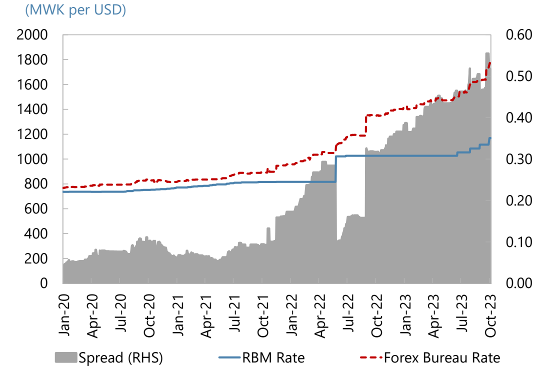
Despite large project-related inflows in June, the RBM struggles to accumulate reserve assets…

and the pressure on the exchange rate seems to remain strong.

FX Cashflow, 2022-23
(USD millions)



Daily Exchange Rates, January 2020-October 6, 2023
(MWK per USD)

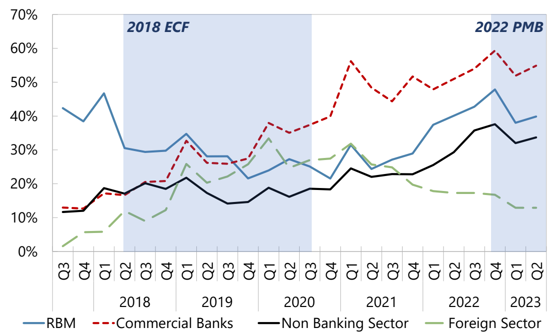


Sources: Reserve Bank of Malawi; National Statistics Office of Malawi; IMF staff estimates; and IMF staff calculations.

Figure 2. Malawi: Banking Sector Developments, 2012–23

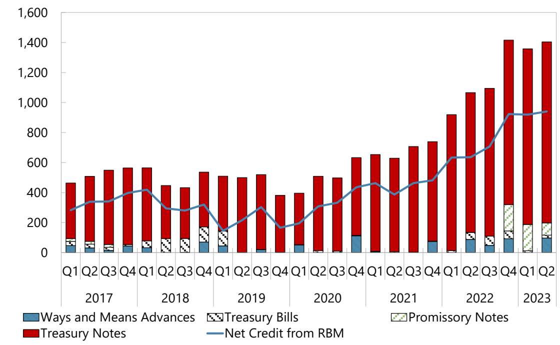
The exposure of the banking sector to the government continues to rise, but…

Government Securities (T-Bills and T-Notes), 2017-23
(percent of GDP)



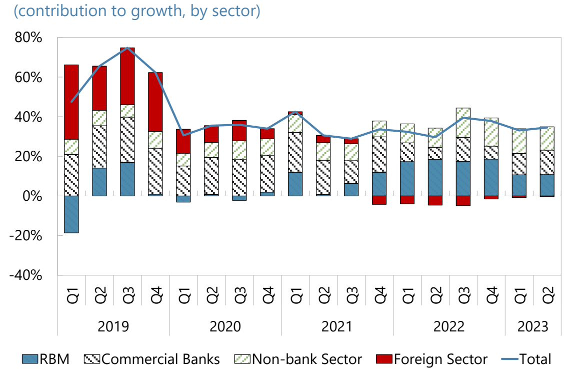
government domestic borrowing from the RBM has plateaued from the beginning of the PMB in 2022Q4.

RBM: Government Borrowing and Deposits, 2017-23
(Billions MWK)



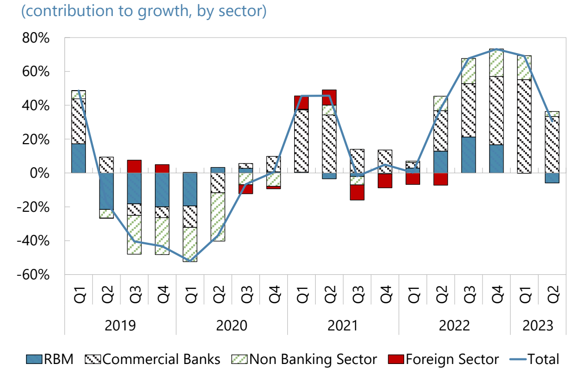
Since 2023, the share of RBM in absorbing the T-Notes has decreased, and…

Treasury Notes, 2019-23
(contribution to growth, by sector)



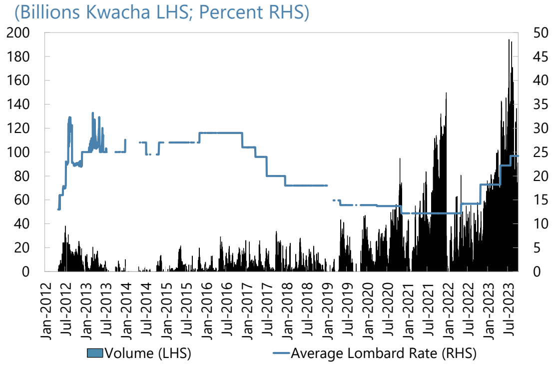
the growth of outstanding T-bills decelerated with RBM cutting back on its holdings of T-bills.

Treasury Bills, 2019-23
(contribution to growth, by sector)



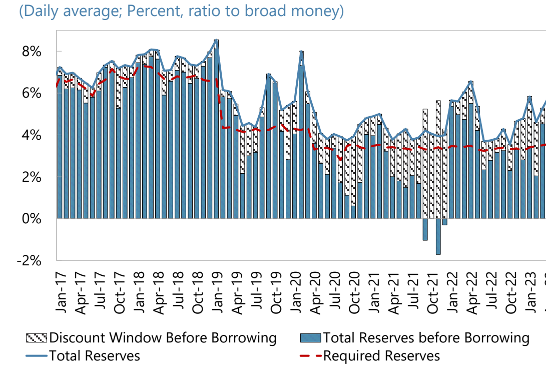
The average interbank and Lombard facility rates rose sharply due to the increase in policy rate in April 2023, but…

Lombard Facility Borrowing/Lending, 2012-23
(Billions Kwacha LHS; Percent RHS)



the tight liquidity condition in the domestic market has led to some banks needing to borrow to meet reserve requirements.

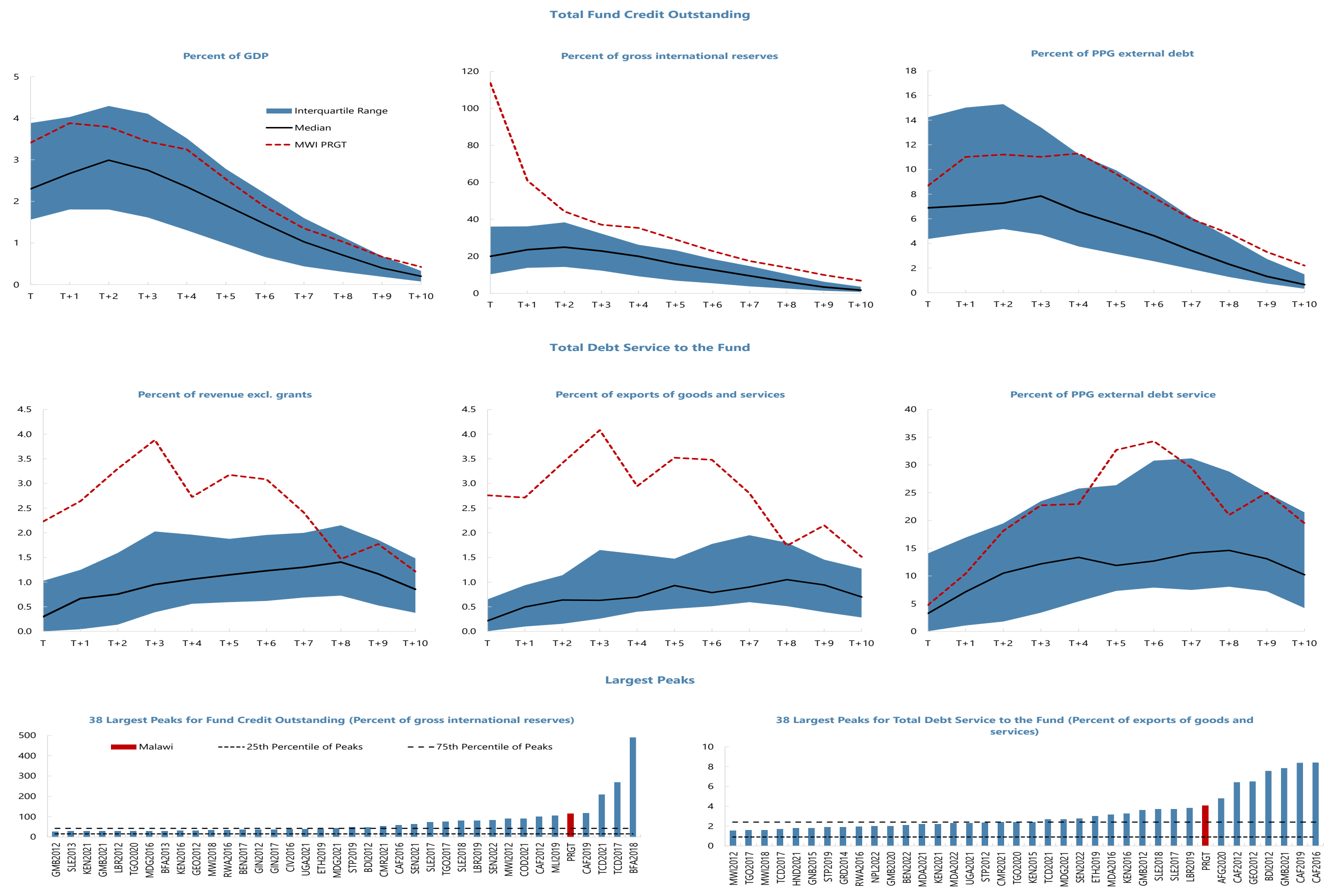
Bank Reserves Developments, 2017-23
(Daily average; Percent, ratio to broad money)



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

Figure 3. Malawi: Capacity to Repay Indicators Compared to UCT Arrangements for PRGT Countries

(In Percent of the Indicated Variables)



Notes:

1) T= date of arrangement approval. PPG = public and publicly guaranteed.
2) Red lines/bars indicate the CtR indicator for the arrangement of interest.
3) The median, interquartile range, and comparator bars reflect all UCT arrangements (including blends) approved for PRGT countries between 2012 and 2022.
4) PRGT countries in the control group with multiple arrangements are entered as separate events in the database.
5) Comparator series is for PRGT arrangements only and runs up to T+10
6) Debt service obligations to the Fund reflect prospective payments, including for the current year.
7) In the case of blenders, the red lines/bars refer to PRGT+GRA. In the case of RST, the red lines/bars refer to PRGT+GRA+RST.

Table 1. Malawi: Selected Economic Indicators, 2022–28

	2022	2023		2024		2025	2026	2027	2028
	Prel.	PMB 1st Review	Proj.	PMB 1st Review	Proj.				
National accounts and prices (percent change, unless otherwise indicated)									
GDP at constant market prices	0.8	1.7	1.6	3.3	3.3	3.8	4.3	4.5	4.6
Nominal GDP (billions of Kwacha)	11,799	14,768	15,396	17,728	19,900	23,454	26,326	29,279	32,390
GDP deflator	17.3	23.1	28.4	16.3	25.1	13.5	7.6	6.4	5.8
Consumer prices (end of period)	25.4	24.4	40.0	15.2	18.3	9.8	7.6	6.5	6.5
Consumer prices (annual average)	20.8	24.8	30.3	18.3	27.9	14.7	8.1	6.8	6.5
Investment and savings (percent of GDP)									
National savings	10.0	4.7	6.2	2.5	2.1	2.3	0.4	2.0	2.6
Government	-5.6	-6.2	-4.6	-6.4	-5.6	-4.2	-3.9	-1.9	-1.2
Private	15.5	11.0	10.9	9.0	7.7	6.5	4.4	4.0	3.8
Gross investment	13.1	12.7	13.9	11.5	10.6	12.2	9.4	10.2	10.0
Government	10.2	9.9	11.2	8.7	7.9	9.3	6.3	6.4	4.8
Private	3.0	2.8	2.7	2.8	2.6	2.9	3.1	3.8	5.3
Saving-investment balance	-3.2	-7.9	-7.6	-9.0	-8.5	-9.9	-9.0	-8.2	-7.4
Central government (percent of GDP on a fiscal year basis)[1, 2]									
Revenue	14.3	17.4	17.2	17.7	17.2	18.4	18.8	17.6	18.8
Tax and nontax revenue	12.5	13.5	13.3	14.9	14.0	15.8	16.1	15.7	16.6
Grants	1.8	3.9	3.9	2.7	3.2	2.6	2.7	1.8	2.2
Expenditure and net lending	22.6	29.3	28.9	27.5	27.9	26.5	25.9	23.3	22.9
Overall balance (excluding grants)	-10.8	-15.8	-15.6	-13.2	-13.9	-10.7	-9.8	-7.6	-6.3
Overall balance (including grants)	-9.0	-11.8	-11.7	-10.5	-10.7	-8.1	-7.1	-5.7	-4.1
Foreign financing	2.6	3.3	3.3	0.6	0.4	-0.3	0.3	-0.4	-0.6
Total domestic financing	6.9	8.5	8.4	8.4	8.0	5.0	3.5	3.8	2.7
Financing gap/residual gap	0.0	0.0	0.0	1.5	2.4	3.3	3.4	2.4	1.9
Primary balance	-5.0	-6.8	-6.8	-4.9	-5.4	-1.1	0.4	1.7	3.0
Domestic primary balance[3]	-4.4	-3.8	-3.8	-2.8	-3.0	1.0	2.4	2.9	3.7
Money and credit (change in percent of broad money at the end of the period, unless otherwise indicated)									
Broad money	38.8	25.2	30.5	20.0	29.3	17.9	12.2	11.2	10.6
Net foreign assets	-13.8	-5.3	-13.3	8.4	12.6	10.4	6.2	2.5	3.2
Net domestic assets	52.6	30.5	43.8	11.7	16.6	7.5	6.0	8.7	7.4
o/w Net claims on the government	39.0	26.1	43.3	18.8	8.8	12.8	10.9	10.9	9.8
Credit to the private sector (percent change)	24.1	16.0	19.6	8.2	11.2	5.8	8.9	9.1	10.7
External sector (US$ millions, unless otherwise indicated)									
Exports (goods and services)	1,128	1,322	1,428	1,454	1,552	1,653	1,730	1,872	1,984
Imports (goods and services)	1,835	2,487	2,680	2,608	2,695	2,969	3,011	3,136	3,215
Gross official reserves	120	499	394	747	714	967	1,081	1,133	1,135
(months of imports)	0.5	2.3	1.8	3.3	2.9	3.9	4.1	4.2	4.1
Net international reserves[4]	-1,247	-673	-1,052	-594	-667	-468	-366	-306	-232
Current account (percent of GDP)	-3.2	-7.9	-7.6	-9.0	-8.5	-9.9	-9.0	-8.2	-7.4
Real effective exchange rate (percent change)	2.9	…	…	…	…	…	…	…	…
Overall balance (percent of GDP)	-0.1	-2.6	-2.2	0.1	0.1	1.0	-0.4	0.0	0.4
Financing gap (percent of GDP)	0.0	5.8	4.6	2.6	3.1	1.8	2.0	0.9	0.2
Terms of trade (percent change)	-14.2	11.4	15.8	-1.8	0.2	2.9	3.1	3.2	-0.8
Debt stock and service (percent of GDP, unless otherwise indicated)									
External debt (public sector)	34.8	37.1	39.3	35.3	35.2	33.8	31.2	28.8	26.3
NPV of public external debt (percent of exports)	269.9	187.1	178.8	162.3	154.8	142.8	131.3	118.8	108.9
Domestic public debt[5]	40.8	43.2	42.0	44.9	39.8	41.0	42.3	43.0	41.7
Total public debt[5]	75.7	80.2	81.3	80.2	75.0	74.8	73.5	71.8	68.0
External debt service (percent of exports)	11.9	59.8	58.1	25.2	26.1	18.8	18.0	12.8	10.8
External debt service (percent of revenue excl. grants)	7.8	44.7	46.9	23.6	25.4	18.2	17.1	11.9	9.7

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

[1]The financial year, 2021, runs from July 1, 2020 to June 30, 2021. FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year. starting from FY2022/23.

[2]Please note that government fiscal statistics are reported following the Government Finance Statistics Manual (2014) starting 2020 projections and going

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

[4] 2022 NIR is calculated as defined in the TMU at the time of the PMB application. Thereafter, the net international reserves reported not only subtract foreign currency drains (FCD) as defined in the TMU of the First Review of the PMB, but also all outstanding foreign currency debt service to external creditors to which the RBM (including as an agent of the government) is in arrears and or servicing via other means, in line with debt restructuring strategy.

[5]Domestic debt is at face value and future borrowings is at cost value.

Table 2a. Malawi: Central Government Operations, FY2021/22–27/28[1]

(Billions of Kwacha)

	2021/22	2022/23	2023/24		2024/25	2025/26	2026/27	2027/28
	Prel.	Est.	PMB 1st Review	Proj.	Proj.			
REVENUE	1,186.5	2,187.3	2,643.0	2,845.9	3,824.0	4,555.2	4,751.7	5,654.7
Taxes	978.3	1,598.2	2,028.6	2,140.8	2,906.7	3,621.8	4,110.0	4,863.8
Taxes on income profits and capital gains	451.3	749.2	955.5	1,024.6	1,387.4	1,782.4	2,023.0	2,577.7
Taxes on goods and services	439.1	691.4	871.6	900.5	1,205.9	1,450.5	1,651.2	1,801.4
Taxes on international trade and transaction	86.8	156.3	199.9	214.1	311.3	386.5	433.1	481.4
Other taxes	1.1	1.3	1.5	1.6	2.1	2.4	2.8	3.1
Grants	149.8	494.5	422.1	529.1	545.0	656.5	499.0	657.2
Current	0.0	35.9	0.0	18.4	0.0	0.0	0.0	0.0
Capital	149.8	440.4	422.1	510.7	545.0	656.5	499.0	657.2
Project grants	123.2	362.3	353.5	434.1	471.3	582.7	417.9	567.9
Dedicated Grants	26.6	78.2	68.6	76.6	73.7	73.8	81.1	89.3
Other Revenue	58.5	94.6	192.3	176.0	372.3	276.9	142.7	133.8
o/w Dividend from RBM			95.0	95.0	280.6	169.3	22.2	0.0
EXPENDITURE	1,920.6	3,671.8	4,267.7	4,618.0	5,501.1	6,272.3	6,306.4	6,881.9
EXPENSE	1,530.5	2,569.6	3,286.3	3,464.9	4,227.5	4,787.5	5,072.9	5,514.7
Compensation of employees	496.4	772.4	927.0	927.6	1,111.7	1,281.8	1,381.0	1,503.6
Purchase of goods and services	310.9	425.0	547.6	569.0	617.0	704.5	694.6	830.5
Interest	271.2	627.0	867.9	884.3	1,444.6	1,815.0	2,018.3	2,121.8
To non-residents	12.6	38.7	50.4	47.6	52.7	52.7	36.7	49.8
To residents other than general government	258.5	588.3	817.5	836.7	1,392.0	1,762.3	1,981.5	2,072.0
Grants	172.7	468.0	678.6	812.2	732.0	603.8	553.5	589.1
Current	157.2	255.2	286.6	282.0	359.7	415.5	466.8	527.4
Capital	15.5	212.8	392.0	530.2	372.3	188.4	86.7	61.7
o/w RBM recapitalization		175.0	348.5	494.7	327.2	143.3	41.6	16.6
Social Benefits	248.8	262.3	248.8	249.3	301.4	358.2	398.5	439.7
Social assistance benefits	171.1	146.3	112.6	112.0	135.2	170.8	188.7	206.7
Fertiliser payments	156.6	144.2	103.3	103.2	92.3	99.5	111.4	123.7
Maize seed subsidy	12.3	0.2	6.6	6.4	8.4	9.2	10.3	11.4
Social Cash Transfer-Government	2.3	2.0	2.8	2.5	34.5	62.1	67.0	71.5
Pensions and gratuities	77.7	116.0	136.1	137.2	166.2	187.4	209.8	233.0
Other Expenses	30.5	14.9	16.5	22.6	20.7	24.1	27.0	30.0
Acquisition of Non-Financial Assets (Development Expenditure)	390.1	1,102.2	981.4	1,153.0	1,273.6	1,484.8	1,233.4	1,367.3
Foreign (Part I)	246.7	872.6	750.7	923.0	988.6	1,146.2	827.2	869.8
Domestic (Part II)	143.4	229.6	230.8	230.0	285.0	338.6	406.2	497.4
Discrepancy	-58.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall Balance (incl. grants and discrepancy)	-792.1	-1,484.4	-1,624.8	-1,772.1	-1,677.1	-1,717.0	-1,554.7	-1,227.2
Primary Balance	-462.9	-857.5	-756.9	-887.8	-232.4	98.0	463.6	894.6
Domestic Primary Balance[2]	-366.0	-479.4	-428.3	-493.8	211.2	587.7	791.8	1,107.2
Domestic Primary Balance (as in TMU)[2]	-366.0	-304.4	…	-94.1	257.8	561.6	811.2	1,123.8
NET FINANCING (Repayment if negative)	792.1	1,484.4	1,624.8	1,772.1	1,677.1	1,717.0	1,554.7	1,227.2
Net Incurrence of Liabilities	844.5	1,484.4	1,624.8	1,772.1	1,677.1	1,717.0	1,554.7	1,227.2
Total Financing	844.5	1,484.4	1,393.4	1,381.8	984.4	903.3	910.4	654.4
Foreign financing (net)	213.9	416.0	89.3	67.7	-60.0	64.4	-113.2	-167.4
Loans	213.9	416.0	89.3	67.7	-60.0	64.4	-113.2	-167.4
Programme Borrowing	0.0	90.7	0.0	0.0	0.0	0.0	0.0	0.0
Project Loans	96.9	413.9	328.6	387.2	443.6	489.7	328.2	212.7
Amortisation	-34.8	-88.5	-239.3	-319.5	-503.6	-425.3	-441.4	-380.0
Domestic financing (net)	569.7	1,068.3	1,105.0	1,314.1	1,044.4	838.9	1,023.6	821.8
Currency and deposits	0.0	0.0	60.6	64.5	0.0	0.0	0.0	0.0
Debt Instruments	630.6	920.0	1,044.5	1,249.7	1,044.4	838.9	1,023.6	821.8
Banking system borrowing	…	684.6	727.5	1,086.5	585.3	441.9	606.7	502.7
RBM[3]	…	285.7	253.5	816.2	-77.3	-120.0	-5.1	16.6
Commercial banks	…	398.9	474.0	270.3	662.7	561.9	611.7	486.1
Nonbank sector borrowing	…	235.4	317.0	163.2	459.1	397.0	416.9	319.1
Change in accounts payable (+ increase / - decrease in arrears)	0.0	148.3	0.0	0.0	0.0	0.0	0.0	0.0
Financing Gap[4]		0.0	430.5	390.3	692.6	813.8	644.3	572.8
ECF budget support		…	14.8	16.6	20.3	23.0	24.6	0.0
Concessional budget support grants (prospective)		0.0	216.6	235.4	161.6	210.6	17.0	0.0
Exceptional financing (prospective)		…	199.1	138.3	510.8	580.1	602.6	572.8
Memorandum items:								
Amortization of domestic securities	90.3	-71.6	-2,901.9	-2,845.9	-1,681.6	-1,507.6	-1,800.5	-1,800.5
Nominal GDP (fiscal year)	8,290.2	12,698.7	15,508.3	16,522.2	20,788.4	24,172.2	27,064.6	30,056.7

Sources: Malawi Ministry of Finance; and IMF staff projections.

[1] FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year starting from FY2022/23

[2] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and non-tax revenues. Those flows related to recapitalization of the RBM (dividend and capital grants) are excluded from the calculation of domestic primary fiscal

[3] RBM financing reported here include those flows related to recapitalization of the RBM.

[4] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

Table 2b. Malawi: Central Government Operations, FY2021/22–27/28[1]

(Percent of GDP)

	2021/22	2022/23	2023/24		2024/25	2025/26	2026/27	2027/28
	Prel.	Est.	PMB 1st Review	Proj.	Proj.			
REVENUE	14.3	17.2	17.7	17.2	18.4	18.8	17.6	18.8
Taxes	11.8	12.6	13.1	13.0	14.0	15.0	15.2	16.2
Taxes on income profits and capital gains	5.4	5.9	6.2	6.2	6.7	7.4	7.5	8.6
Taxes on goods and services	5.3	5.4	5.6	5.5	5.8	6.0	6.1	6.0
Taxes on international trade and transaction	1.0	1.2	1.3	1.3	1.5	1.6	1.6	1.6
Other taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	1.8	3.9	2.7	3.2	2.6	2.7	1.8	2.2
Current	0.0	0.3	0.0	0.1	0.0	0.0	0.0	0.0
Capital	1.8	3.5	2.7	3.1	2.6	2.7	1.8	2.2
Project grants	1.5	2.9	2.3	2.6	2.3	2.4	1.5	1.9
Dedicated Grants	0.3	0.6	0.4	0.5	0.4	0.3	0.3	0.3
Other Revenue	0.7	0.7	1.9	1.1	1.8	1.1	0.5	0.4
o/w Dividend from RBM			0.6	0.6	1.3	0.7	0.1	0.0
EXPENDITURE	22.6	28.9	27.5	27.9	26.5	25.9	23.3	22.9
EXPENSE	17.9	20.2	21.2	21.0	20.3	19.8	18.7	18.3
Compensation of employees	6.0	6.1	6.0	5.6	5.3	5.3	5.1	5.0
Purchase of goods and services	3.7	3.3	3.5	3.4	3.0	2.9	2.6	2.8
Interest	3.3	4.9	5.6	5.4	6.9	7.5	7.5	7.1
To non-residents	0.2	0.3	0.3	0.3	0.3	0.2	0.1	0.2
To residents other than general government	3.1	4.6	5.3	5.1	6.7	7.3	7.3	6.9
Grants	2.1	3.7	4.4	4.9	3.5	2.5	2.0	2.0
Current	1.9	2.0	1.8	1.7	1.7	1.7	1.7	1.8
Capital	0.2	1.7	2.5	3.2	1.8	0.8	0.3	0.2
o/w RBM recapitalization		1.4	2.2	3.0	1.6	0.6	0.2	0.1
Social Benefits	2.5	2.1	1.6	1.5	1.4	1.5	1.5	1.5
Social assistance benefits	1.6	1.2	0.7	0.7	0.7	0.7	0.7	0.7
Fertiliser payments	1.4	1.1	0.7	0.6	0.4	0.4	0.4	0.4
Maize seed subsidy	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social Cash Transfer-Government	0.0	0.0	0.0	0.0	0.2	0.3	0.2	0.2
Pensions and gratuities	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.8
Other Expenses	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Acquisition of Non-Financial Assets (Development Expenditure)	4.7	8.7	6.3	7.0	6.1	6.1	4.6	4.5
Foreign (Part I)	3.0	6.9	4.8	5.6	4.8	4.7	3.1	2.9
Domestic (Part II)	1.7	1.8	1.5	1.4	1.4	1.4	1.5	1.7
Discrepancy	-0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall Balance (incl. grants and discrepancy)	-9.0	-11.7	-10.5	-10.7	-8.1	-7.1	-5.7	-4.1
Primary Balance	-5.0	-6.8	-4.9	-5.4	-1.1	0.4	1.7	3.0
Domestic Primary Balance [2]	-4.4	-3.8	-2.8	-3.0	1.0	2.4	2.9	3.7
Domestic Primary Balance (as in TMU)[2]	-4.4	-2.4	…	-0.6	1.2	2.3	3.0	3.7
NET FINANCING (Repayment if negative)	9.6	11.7	10.5	10.7	8.1	7.1	5.7	4.1
Net Incurrence of Liabilities	10.2	11.7	10.5	10.7	8.1	7.1	5.7	4.1
Total Financing	10.2	11.7	9.0	8.4	4.7	3.7	3.4	2.2
Foreign financing (net)	2.6	3.3	0.6	0.4	-0.3	0.3	-0.4	-0.6
Loans	2.6	3.3	0.6	0.4	-0.3	0.3	-0.4	-0.6
Programme Borrowing	0.0	0.7	0.0	0.0	0.0	0.0	0.0	0.0
Project Loans	1.2	3.3	2.1	2.3	2.1	2.0	1.2	0.7
Amortisation	-0.4	-0.7	-1.5	-1.9	-2.4	-1.8	-1.6	-1.3
Domestic financing (net)	6.9	8.4	8.4	8.0	5.0	3.5	3.8	2.7
Currency and deposits	0.0	0.0	0.4	0.4	0.0	0.0	0.0	0.0
Debt Instruments	7.6	7.2	6.7	7.6	5.0	3.5	3.8	2.7
Banking system borrowing	…	5.4	4.7	6.6	2.8	1.8	2.2	1.7
RBM[3]	…	2.2	1.6	4.9	-0.4	-0.5	0.0	0.1
Commercial banks	…	3.1	3.1	1.6	3.2	2.3	2.3	1.6
Nonbank sector borrowing	…	1.9	2.0	1.0	2.2	1.6	1.5	1.1
Change in accounts payable (+ increase / - decrease in arrears)	…	1.2	1.3	0.0	0.0	0.0	0.0	0.0
Financing Gap[4]		0.0	1.5	2.4	3.3	3.4	2.4	1.9
ECF budget support		…	0.1	0.1	0.1	0.1	0.1	0.0
Concessional budget support grants (prospective)		0.0	1.4	1.4	0.8	0.9	0.1	0.0
Exceptional financing (prospective)		…	1.4	0.8	2.5	2.4	2.2	1.9
Memorandum items:								
Amortization of domestic securities	1.1	-0.6	-18.7	-17.2	-8.1	-6.2	-6.7	-6.0

Sources: Malawi Ministry of Finance; and IMF staff projections.

[1] FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year starting from FY2022/23.

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

[3] RBM financing reported here include those flows related to recapitalization of the RBM.

[4] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

Table 3a. Malawi: Monetary Authorities' Balance Sheet, 2022–28

(Billions of Kwacha, unless otherwise indicated)

	2022	2023					2024				2025	2026	2027	2028
	Dec.	Mar.	Jun.		Sept.	Dec.	Mar.	Jun.	Sept.	Dec.				
	Actual	Actual	PMB 1st review	Prel.	Proj.		Proj.				Proj.			
Monetary base	571	562	615	690	880	931	981	993	1,029	1,173	1,383	1,552	1,726	1,909
Currency in circulation	470	399	...	566	...	...	...	...	...	...	...	...	...	...
Liabilities to other depository corporations	101	161	...	-404	...	...	...	...	...	...	...	...	...	...
Liabilities to other sectors	1	1	...	0	...	...	...	...	...	...	...	...	...	...
Net foreign assets (NFA) [1]	-955	-1,025	-919	-964	-1,008	-1,455	-1,330	-1,257	-1,347	-1,075	-632	-341	-229	-56
Claims on nonresidents	318	241	...	341	416	650	790	975	1,352	1,400	2,121	2,510	2,754	2,883
Official reserve assets	124	109	...	227	...	...	...	...	...	...	...	...	...	...
Other foreign assets	193	132	...	115	...	...	...	...	...	...	...	...	...	...
Liabiliites to nonresidents	-1,273	-1,266	...	-1,305	-1,424	-2,106	-2,120	-2,232	-2,699	-2,475	-2,753	-2,851	-2,984	-2,938
Short -term foreign liabilities	-424	-427	...	-419	...	...	...	...	...	...	...	...	...	...
Other foreign liabilities	-849	-839	...	-886	...	...	...	...	...	...	...	...	...	...
Net domestic assets	1,526	1,586	1,534	1,654	1,889	2,386	2,311	2,251	2,376	2,248	2,014	1,893	1,955	1,965
Net claims on central government	1,080	1,109	1,014	1,131	1,331	1,876	1,926	1,522	1,522	1,849	1,729	1,724	1,740	1,751
Claims on central government	5,207	5,408	...	5,462	...	...	...	...	...	...	...	...	...	...
Liabilities to central government	4,127	4,299	...	4,331	...	...	...	...	...	...	...	...	...	...
Claims on other depository corporations	95	102	108	91	97	104	111	119	126	111	119	126	134	140
Claims on other financial corporations	27	28	...	28	...	...	...	...	...	...	...	...	...	...
Claims on public nonfinancial corportions	323	333	...	352	...	...	...	...	...	...	...	...	...	...
Claims on private sector	31	34	...	35	...	...	...	...	...	...	...	...	...	...
Other items (net)	-31	-19	...	17	...	...	...	...	...	...	...	...	...	...
Memorandum items:														
Money multiplier	4.9	4.8	4.8	4.7	4.0	3.9	3.8	3.8	3.9	4.0	4.0	4.0	4.0	4.0
Annual growth of reserve money (percent)	27.0	28.3	14.4	28.4	62.4	63.0	74.6	44.0	16.9	26.0	17.9	12.2	11.2	10.6
91-day treasury bill rate	11.0	13.0	13.0	13.0	...	...	...	...	...	...	...	...	...	...

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

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

Table 3b. Malawi: Monetary Survey, 2022–28

(Billions of Kwacha, unless otherwise indicated)

	2022	2023					2024				2025	2026	2027	2028
	Dec.	Mar.	Jun.		Sept.	Dec.	Mar.	Jun.	Sept.	Dec.				
	Actual	Actual	PMB 1st review	Prel.	Proj.		Proj.				Proj.			
Broad money liabilities	2,782	2,721	2,804	3,226	3,100	3,630	3,347	3,725	4,015	4,692	5,530	6,207	6,903	7,637
Currency outside depository corporations	398	344	...	504	...	...	...	..	...	...	...	...	...	...
Transferable deposits	1,366	1,292	...	1,580	...	...	...	...	...	...	...	...	...	...
Other deposits	1,018	1,085	...	1,142	...	...	...	...	...	...	...	...	...	...
Net foreign assets (NFA)	-683	-784	-659	-793	-731	-1,053	-923	-828	-826	-595	-109	234	391	611
Monetary authorities	-955	-1,025	-919	-964	-1,008	-1,455	-1,330	-1,257	-1,347	-1,075	-632	-341	-229	-56
Gross foreign assets	318	241	...	341	...	...	...	...	...	...	...	...	...	...
Foreign liabilities	-1,273	-1,266	...	-1,305	...	...	...	...	...	...	...	...	...	...
Commercial banks (net)	272	241	260	172	277	402	406	429	521	480	523	575	621	666
Net domestic assets (NDA)	3,466	3,505	3,462	4,018	3,831	4,683	4,271	4,553	4,840	5,287	5,639	5,973	6,512	7,026
Net claims on central government	2,390	2,537	2,554	2,637	2,947	3,595	3,655	3,311	3,454	3,914	4,516	5,122	5,800	6,474
Claims on central government	6,609	6,944	...	7,093	...	...	...	...	...	...	...	...	...	...
Liabilities to central government	4,219	4,406	...	4,456	...	...	...	...	...	...	...	...	...	...
Claims on other sectors	1,478	1,454	1,524	1,583	1,635	1,706	1,756	1,790	1,840	1,890	1,819	1,846	1,979	2,163
Claims on other financial corporations	52	57	60	59	62	65	69	69	71	72	72	72	72	72
Claims on public nonfinancial corporations	406	394	391	417	411	420	431	441	451	461	311	211	201	203
Claims on private sector	1,020	1,003	1,073	1,107	1,162	1,220	1,257	1,280	1,318	1,357	1,436	1,564	1,706	1,888
Other items (net)	-402	-486	-616	-202	-752	-617	-1,141	-549	-454	-517	-696	-995	-1,266	-1,611
Memorandum items:														
Velocity of money														
(annualized GDP divided by broad money)	4.2	4.9	4.7	4.7	4.7	4.2	4.9	4.7	4.7	4.2	4.2	4.2	4.2	4.2
Annual growth of broad money (percent)	38.8	32.2	18.2	36.0	25.1	30.5	23.0	15.5	29.5	29.3	17.9	12.2	11.2	10.6
Annual growth of credit to the private sector (percent)	24.1	24.9	15.7	19.4	17.9	19.6	25.4	15.6	13.4	11.2	5.8	8.9	9.1	10.7
Nominal GDP (billions of Kwacha)	11,799	15,396	14,768	15,396	15,396	15,396	19,900	19,900	19,900	19,900	23,454	26,326	29,279	32,390

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

Table 4a. Malawi: Balance of Payments, 2022–28

(Millions of U.S. dollars, unless otherwise indicated)

	2022	2023		2024		2025	2026	2027	2028
	Prel.	PMB 1st Review	Proj.	PMB 1st Review	Proj.				
Current account balance	-397.1	-1,023.7	-998.6	-964.1	-950.0	-1,121.6	-1,050.7	-1,005.1	-968.8
Merchandise trade balance	-651.8	-1,163.9	-1,237.5	-1,143.3	-1,126.3	-1,282.9	-1,247.5	-1,194.0	-1,191.8
Exports	937.2	1,127.7	1,234.1	1,253.0	1,351.1	1,444.4	1,513.1	1,645.5	1,746.4
o/w Tobacco	372.9	446.0	530.0	462.4	528.4	537.4	547.0	556.8	568.0
Imports	-1,588.9	-2,291.6	-2,471.6	-2,396.4	-2,477.4	-2,727.4	-2,760.6	-2,839.5	-2,938.2
o/w Petroleum products	-239.1	-208.7	-500.0	-196.6	-500.6	-497.5	-500.3	-506.3	-526.7
o/w Fertilizers	-208.3	-223.7	-235.5	-230.5	-249.4	-253.2	-258.8	-265.6	-273.6
o/w Project related	-421.8	-467.7	-558.1	-335.8	-318.2	-392.5	-234.4	-238.1	-226.7
Services balance	-295.2	-344.8	-361.8	-291.6	-303.8	-317.0	-292.2	-322.2	-311.6
o/w Interest public sector	-42.9	-143.2	-147.0	-72.3	-78.6	-67.7	-34.0	-17.4	-25.6
o/w Other factor payments (net)	-197.5	-201.1	-200.9	-207.8	-207.7	-215.8	-225.2	-235.5	-246.5
Unrequited transfers (net)	549.9	485.0	600.7	470.8	480.1	478.4	489.0	511.0	534.6
Private (net)	479.6	486.3	495.0	472.1	481.3	479.6	490.2	512.3	535.9
Official (net)	70.3	-1.3	105.7	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Capital account balance	781.9	1,109.7	997.2	919.7	1,003.6	1,062.6	844.4	870.7	892.6
Project and dedicated grants	370.3	364.4	456.4	277.1	255.1	347.5	199.1	273.7	272.5
Off-budget project support[1]	411.5	745.3	540.8	642.6	748.5	715.1	645.3	597.0	620.1
Financial account balance	-396.3	-420.9	-286.0	58.9	-40.9	168.3	154.2	134.2	124.5
Foreign direct investment (net)	37.1	53.2	53.8	56.7	58.4	94.0	98.1	113.4	130.0
Portfolio investment (net)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Medium- and long-term loans (net)	214.8	-233.5	-191.8	-2.8	-62.8	54.9	-32.8	-71.8	-38.8
Disbursements	278.6	355.2	402.2	239.5	234.5	256.4	161.5	92.6	76.2
Budget support and other program loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project support loans	278.6	355.2	402.2	239.5	234.5	256.4	161.5	92.6	76.2
Other medium-term loans (official)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	-63.8	-588.7	-594.1	-242.4	-297.2	-201.5	-194.3	-164.4	-115.0
Other inflows	-648.2	-240.6	-148.0	5.1	-36.5	19.4	88.9	92.5	33.2
Overall balance	-11.5	-334.9	-287.4	14.6	12.7	109.3	-52.0	-0.3	48.3
Financing	11.5	334.9	287.4	-14.6	-12.7	-109.3	52.0	0.3	-48.3
Gross reserves (- increase)	-48.5	-378.3	-273.5	-249.0	-320.5	-253.1	-113.9	-51.8	-2.6
IMF (net)	60.0	-38.9	-39.4	-40.7	-41.9	-56.1	-70.5	-55.2	-70.0
Purchases/drawings	90.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases/repayments	36.0	38.9	39.4	40.7	41.9	56.1	70.5	55.2	70.0
Exceptional financing (CCRT)	5.4								
Financing gap[2]	0.0	752.1	600.3	275.0	349.7	199.9	236.4	107.2	24.3
ECF	0.0	35.2	35.5	17.6	17.8	35.6	35.6	53.4	0.0
Concessional budget support grants (prospective)	0.0	248.0	86.0	80.0	135.0	18.0	90.0	0.0	0.0
Other financing (prospective)	0.0	468.9	478.8	177.5	196.9	146.3	110.8	53.9	24.3
Memorandum items:									
Gross official reserves	120.2	498.5	393.7	747.5	714.2	967.3	1,081.1	1,132.9	1,135.5
Months of imports[3]	0.5	2.3	1.8	3.3	2.9	3.9	4.1	4.2	4.1
Net international reserves[4]	-1,247	-673	-1,052	-594	-667	-468	-366	-306	-232
Import price index (2005 = 100)	183.8	170.3	165.7	171.2	164.4	157.4	151.8	147.0	148.4
Import volume (percent change)	-56.9	55.4	72.6	4.0	1.0	15.0	5.0	6.2	2.5
REER (percent change)	2.9	...	...	...	...	...	...	...	...
Terms of trade (percent change)	-14.2	11.4	15.8	-1.8	0.2	2.9	3.1	3.2	-0.8

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

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

[2] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

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

[4] 2022 NIR is calculated as defined in the TMU at the time of the PMB application. Thereafter, the net international reserves reported not only subtract foreign currency drains (FCD) as defined in the TMU of the First Review of the PMB, but also all outstanding foreign currency debt service to external creditors to which the RBM (including as an agent of the government) is in arrears and or servicing via other means, in line with debt restructuring

Table 4b. Malawi: Balance of Payments, 2022–28

(Percent of GDP)

	2022	2023		2024		2025	2026	2027	2028
	Prel.	PMB 1st Review	Est.	PMB 1st Review			Proj.		
Current account balance	-3.2	-7.9	-7.6	-9.0	-8.5	-9.9	-9.0	-8.2	-7.4
Merchandise trade balance	-5.2	-9.0	-9.4	-10.6	-10.0	-11.3	-10.7	-9.7	-9.1
Exports	7.5	8.7	9.4	11.6	12.0	12.8	13.0	13.4	13.4
o/w Tobacco	3.0	3.5	4.0	4.3	4.7	4.8	4.7	4.5	4.4
Imports	-12.7	-17.8	-18.8	-22.3	-22.1	-24.1	-23.7	-23.0	-22.5
o/w Petroleum products	-1.9	-1.6	-3.8	-1.8	-4.5	-4.4	-4.3	-4.1	-4.0
o/w Fertilizers	-1.7	-1.7	-1.8	-2.1	-2.2	-2.2	-2.2	-2.2	-2.1
o/w Project related	-3.4	-3.6	-4.3	-3.1	-2.8	-3.5	-2.0	-1.9	-1.7
Services balance	-2.4	-2.7	-2.8	-2.7	-2.7	-2.8	-2.5	-2.6	-2.4
o/w Interest public sector	-0.3	-1.1	-1.1	-0.7	-0.7	-0.6	-0.3	-0.1	-0.2
o/w Other factor payments (net)	-1.6	-1.6	-1.5	-1.9	-1.8	-1.9	-1.9	-1.9	-1.9
Unrequited transfers (net)	4.4	3.8	4.6	4.4	4.3	4.2	4.2	4.1	4.1
Private (net)	3.8	3.8	3.8	4.4	4.3	4.2	4.2	4.2	4.1
Official (net)	0.6	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0
Capital account balance	6.2	8.6	7.6	8.5	8.9	9.4	7.2	7.1	6.8
Project and dedicated grants	3.0	2.8	3.5	2.6	2.3	3.1	1.7	2.2	2.1
Off-budget project support[1]	3.3	5.8	4.1	6.0	6.7	6.3	5.5	4.8	4.8
Financial account balance	-3.2	-3.3	-2.2	0.5	-0.4	1.5	1.3	1.1	1.0
Foreign direct investment (net)	0.3	0.4	0.4	0.5	0.5	0.8	0.8	0.9	1.0
Portfolio investment (net)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	1.7	-1.8	-1.5	0.0	-0.6	0.5	-0.3	-0.6	-0.3
Disbursements	2.2	2.8	3.1	2.2	2.1	2.3	1.4	0.8	0.6
Budget support and other program loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project support	2.2	2.8	3.1	2.2	2.1	2.3	1.4	0.8	0.6
Other medium-term loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	-0.5	-4.6	-4.5	-2.3	-2.6	-1.8	-1.7	-1.3	-0.9
Other inflows	-5.2	-1.9	-1.1	0.0	-0.3	0.2	0.8	0.8	0.3
Errors and omissions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-0.1	-2.6	-2.2	0.1	0.1	1.0	-0.4	0.0	0.4
Financing	0.1	2.6	2.2	-0.1	-0.1	-1.0	0.4	0.0	-0.4
Gross reserves (- increase)	-0.4	-2.9	-2.1	-2.3	-2.9	-2.2	-1.0	-0.4	0.0
IMF (net)	0.5	-0.3	-0.3	-0.4	-0.4	-0.5	-0.6	-0.4	-0.5
Purchases/drawings	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases/repayments	0.3	0.3	0.3	0.4	0.4	0.5	0.6	0.4	0.5
Exceptional financing (CCRT)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap[2]	0.0	5.8	4.6	2.6	3.1	1.8	2.0	0.9	0.2
ECF		0.3	0.3	0.2	0.2	0.3	0.3	0.4	0.0
Concessional budget support grants (prospective)	0.0	1.9	0.7	0.7	1.2	0.2	0.8	0.0	0.0
Other financing (prospective)	0.0	3.6	3.6	1.6	1.8	1.3	0.9	0.4	0.2
Memorandum items:									
Gross official reserves	1.0	3.9	3.0	6.9	6.4	8.6	9.3	9.2	8.7
Months of imports[3]	0.5	2.3	1.8	3.3	2.9	3.9	4.1	4.2	4.1
Net international reserves[4]	-9.9	-5.2	-8.0	-5.5	-5.9	-4.1	-3.1	-2.5	-1.8
Import price index (2005 = 100)	183.8	170.3	165.7	171.2	164.4	157.4	151.8	147.0	148.4
Import volume (percent change)	-56.9	55.4	72.6	4.0	1.0	15.0	5.0	6.2	2.5
REER (percent change)	2.9	…	…	…	…	…	…	…	…
Terms of trade (percent change)	-14.2	11.4	15.8	-1.8	0.2	2.9	3.1	3.2	-0.8

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

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

[2] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

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

[4] 2022 NIR is calculated as defined in the TMU at the time of the PMB application. Thereafter, the net international reserves reported not only subtract foreign currency drains (FCD) as defined in the TMU of the First Review of the PMB, but also all outstanding foreign currency debt service to external creditors to which the RBM (including as an agent of the government) is in arrears and or servicing via other means, in line with debt restructuring

Table 5. Malawi: Selected Banking Soundness Indicators, 2019–23

(Percent)

Key ratios	Dec-19	Dec-20	Dec-21	Dec-22	Jun-23
Capital Adequacy					
1. Regulatory Tier 1 capital to risk weighted assets	17.0	17.4	17.2	17.7	19.9
2. Total regulatory capital to risk weighted assets	21.0	20.8	20.7	20.9	22.8
3. Total capital to total assets[1]	16.4	13.1	14.3	11.6	12.8
Asset Composition and Quality					
1. Non-performing loans to gross loans and advances	6.3	6.3	4.5	6.3	6.9
2. Provisions to non-performing loans	38.6	32.9	32.5	29.9	35.9
3. Total loans and advances to total assets	33.2	31.2	29.2	29	27.1
4. Foreign currency loans to total loans and advances	20.9	14.7	11.3	11.1	11.5
Earnings and Profitability					
1. Return on assets (ROA)	2.7	3.0	3.4	4.1	5.4
2. Return on equity (ROE)	20.5	22.8	26.0	33.3	41.1
3. Non-interest expenses to gross income	51.8	49.0	43.7	40.3	34.2
4. Interest margin to gross income	59.6	65.6	49.7	52.2	51.8
5. Non-interest income to revenue	33.6	34.4	31.6	30.5	31.8
6. Net interest income to assets	8.4	8.0	7.9	9	5.4
7. Personnel expenses to non-interest expenses	43.0	42.5	43.4	43.7	45.5
Liquidity					
1. Liquid assets to deposits and short-term liabilities	58.9	57.5	52.5	53.5	55.9
2. Total loans to total deposits	54.2	50.0	47.9	42.9	39.7
3. Liquid Assets to total assets	39.8	39.6	37.3	39.4	41.3
4. Foreign exchange liabilities to total liabilities	15.8	16.1	14.2	13.8	15.9

Source: Reserve Bank of Malawi.

[1]In the total capital to total assets series, total capital refers to regulatory capital.

Table 6. Malawi: External Financing Requirement and Source, 2022–28
(Millions of U.S. dollars, unless otherwise indicated)

	2022	2023	2024	2025	2026	2027	2028
Total requirement	-580	-1,972	-1,567	-1,575	-1,358	-1,220	-1,085
Current account, excluding official transfers	-467	-1,104	-949	-1,120	-1,049	-1,004	-968
Debt amortization	-64	-594	-297	-202	-194	-164	-115
Gross reserves accumulation (- increase)	-48	-274	-321	-253	-114	-52	-3
Total sources	580	1,266	1,217	1,375	1,121	1,113	1,061
Expected disbursements (official)	1,131	1,399	1,237	1,318	1,005	962	968
Grants	852	997	1,002	1,061	843	869	891
Medium- and long-term loans	279	402	234	256	161	93	76
Private sector (net)	-611	-94	22	113	187	206	163
IMF (net)	60	-39	-42	-56	-71	-55	-70
Drawings	91	0	0	0	0	0	0
Repayments	31	39	42	56	71	55	70
Financing gap	0	706	350	200	236	107	24
Gross official reserves	120	394	714	967	1,081	1,133	1,135
Months of imports	0.5	1.8	2.9	3.9	4.1	4.2	4.1

Source: IMF staff estimates.

Table 7. Malawi: Proposed Schedule of Disbursements Under the 2023–27 ECF Arrangement

(Millions of SDR)

Amount	% of Quota[1]	Availability date	Conditions Necessary for Disbursement[2]
26.372	19.0	Date of approval of the ECF Arrangement	Executive Board Approval of Four Year ECF arrangement.
13.186	9.5	July 20, 2024	Observance of performance criteria for March 31, 2024 and completion of first review.
13.186	9.5	January 20, 2025	Observance of performance criteria for September 30, 2024 and completion of second review.
13.186	9.5	July 20, 2025	Observance of performance criteria for March 31, 2025 and completion of third review.
13.186	9.5	January 20, 2026	Observance of performance criteria for September 30, 2025 and completion of fourth review.
13.186	9.5	July 20, 2026	Observance of performance criteria for March 31, 2026 and completion of fifth review.
13.186	9.5	January 20, 2027	Observance of performance criteria for September 30, 2026 and completion of the sixth review.
26.372	19.0	July 20, 2027	Observance of performance criteria for March 31, 2027 and completion of the seventh review.
131.860	95.0		Total
Memorandum item:			
Malawi's Quota (in millions SDR)			138.80

Source: IMF staff estimates.

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

[2]Each review is also subject to observance of standard continuous performance criteria.

Table 8. Malawi: Performance Criteria and Indicative Targets Under the ECF Arrangement[1], 2023–24

	Target type [2]	2023	2024		
		End-Dec	End-Mar	End-June	End-Sept
		Proposed Targets			
		IT	PC	IT	PC
I. Monetary Targets (billions of kwacha)					
Monetary base (ceiling on stock) (upper bound)[3]		958.7	1,010.2	1,023.1	1,060.3
Monetary base (ceiling on stock)[3]	PC	930.8	980.8	993.3	1,029.4
Monetary base (ceiling on stock) (lower bound)[3]		902.9	951.4	963.5	998.5
II. Fiscal Targets (billions of kwacha)					
Domestic revenue (floor)[6]	IT	1,621.0	2,223.0	747.0	1,494.0
Domestic primary fiscal balance (floor)[4,6]	PC	-155.7	-94.1	95.5	57.0
RBM financing of central government (ceiling)[6,7]	IT	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0	0	0	0
Social spending (floor)[6,8]	IT	686.7	910.8	290.0	582.8
III. External Sector Targets (US$ millions, unless otherwise indicated)					
Change in net international reserves of the RBM (floor)[5]	PC	253.0	68.7	183.3	221.8
Accumulation of external payments arrears (ceiling)[6,9]	PC	0	0	0	0
Contracting or guaranteeing of nonconcessional external debt (ceiling)[6,9,10]	PC	0	0	0	0
Contracting or guaranteeing of concessional external debt (ceiling)[6]	IT	70	70	0	0
Memorandum items:					
Program exchange rate (kwacha per US$)					

Source: IMF staff projections.

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

[2] "PC" means Performance Criteria and "IT" means Indicative Target. The PC test date for the 1st Review is end-March 2024. The test dates for the future review will be in end-September 2024. End-December 2023 and end-June 2024 targets are ITs.

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

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

[5] Targets are subject to an adjustor for (i) debt service and fees and (ii) general budget support, as specified in the TMU. Defined as cumulative flow, starting from the beginning of the calendar year.

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

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

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

[9] Evaluated on a continuous basis.

[10] For program purposes, a limited exception on NCB may be allowed only in the exceptional circumstance that it is used to wind down maturing swaps and for debt management operation that improves the overall debt profile.

Table 9. Malawi: Indicators of Capacity to Repay the Fund, 2023–36

	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036
Fund Obligations Based on Existing Drawings:														
(SDR millions)														
Principal	22.4	23.1	33.5	47.8	40.5	51.3	47.9	35.0	13.9	13.9	0.0	0.0	0.0	0.0
Charges and interest	7.0	8.1	8.1	4.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fund Obligations Based on Prospective Drawings:														
(SDR millions)														
Principal	0.00	0.00	0.00	0.00	0.00	0.00	5.27	9.23	14.50	22.42	26.37	21.10	17.14	11.87
Charges and interest	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.00
Total Obligations Based on Existing and Prospective Drawings:														
SDR millions	29.4	31.3	41.6	51.9	40.5	51.3	53.2	44.2	28.4	36.3	26.4	21.1	17.1	12.9
US$ Millions	39.4	42.0	56.1	70.4	55.1	70.0	72.7	60.4	38.7	49.6	36.0	28.8	23.4	17.6
Percent of exports of goods and services	2.8	2.7	3.4	4.1	2.9	3.5	3.5	2.8	1.7	2.2	1.5	1.2	0.9	0.7
Percent of debt service	4.8	10.4	18.0	22.6	22.9	32.8	34.4	29.6	21.0	25.1	19.5	15.3	12.4	9.7
Percent of quota	21.1	22.5	30.0	37.4	29.2	37.0	38.3	31.9	20.4	26.2	19.0	15.2	12.3	9.3
Percent of gross official reserves	10.0	5.9	5.8	6.5	4.9	6.2	6.4	5.3	3.4	4.5	3.3	2.7	2.3	1.7
Percent of GDP	0.3	0.4	0.5	0.6	0.4	0.5	0.5	0.4	0.3	0.3	0.2	0.2	0.1	0.1
Projected Level of Credit Outstanding Based on Existing and Prospective Drawings:														
SDR millions	333.2	323.3	316.2	294.7	293.8	242.6	189.3	145.1	116.7	80.4	54.1	33.0	15.8	4.0
US$ Millions	447.7	435.1	427.9	400.0	400.5	331.5	258.7	198.3	159.5	109.9	73.9	45.1	21.6	5.4
Percent of exports of goods and services	31.3	28.0	25.9	23.1	21.4	16.7	12.4	9.2	7.2	4.8	3.1	1.8	0.9	0.2
Percent of debt service	54.0	107.6	137.5	128.7	166.9	155.2	122.4	97.1	86.6	55.6	40.1	23.9	11.5	3.0
Percent of quota	240.1	232.9	227.8	212.3	211.7	174.7	136.4	104.6	84.1	57.9	38.9	23.8	11.4	2.9
Percent of gross official reserves	113.7	60.9	44.2	37.0	35.4	29.2	22.9	17.5	14.0	10.0	6.8	4.3	2.1	0.5
Percent of GDP	3.4	3.9	3.8	3.4	3.3	2.5	1.9	1.4	1.0	0.7	0.4	0.2	0.1	0.0
Net Use of Fund Credit	4.0	-9.9	-7.1	-21.5	-0.9	-51.3	-53.2	-44.2	-28.4	-36.3	-26.4	-21.1	-17.1	-11.9
(SDR milions)														
Disbursement and purchases	26.4	13.2	26.4	26.4	39.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayment and repurchases	22.4	23.1	33.5	47.8	40.5	51.3	53.2	44.2	28.4	36.3	26.4	21.1	17.1	11.9
Memorandum items:														
Exports of goods and services (millions of U.S. dollars)	1,428	1,552	1,653	1,730	1,872	1,984	2,083	2,148	2,224	2,298	2,377	2,451	2,529	2,611
Debt service (millions of U.S. dollars)	829.3	404.2	311.1	310.8	240.0	213.6	211.4	204.3	184.2	197.8	184.3	188.3	188.0	181.2
Quota (SDR millions)	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8

Source: IMF staff projections.

Table 10. Malawi: Debt Decomposition[1], 2022–25

(Millions of U.S. dollars, unless otherwise indicated)

	Actual	Projections		
	2022	2023	2024	2025
Creditor Profile				
Total Debt	**8,699**	**7,577**	**7,619**	**8,003**
External Debt	**4,006**	**3,660**	**3,575**	**3,616**
Multilateral creditors [2]	2,558	2,846	2,956	3,141
IMF	437	443	430	420
World Bank	1,317	1,480	1,592	1,727
AfDB	431	431	435	439
Other Multilaterals	372	492	499	555
Bilateral Creditors	418	382	350	315
Paris Club	4	1	1	1
Non-Paris Club	414	381	349	315
Commercial creditors	1,030	431	269	160
Domestic Debt	**4,693**	**3,917**	**4,044**	**4,387**
Memorandum Items:				
Collateralized debt[3]	503	325	194	100
Multilateral and Collateralized Debt[3,4]				
Multilateral Debt				
Percent of external debt	64	78	83	87
Percent of GDP	22	31	29	29
o/w: IMF and WB				
Percent of external debt	44	53	57	59
Percent of GDP	15	21	20	20
o/w: African Development Bank				
Percent of external debt	11	12	12	12
Percent of GDP	4	5	4	4
o/w: Other multilateral				
Percent of external debt	9	13	14	15
Percent of GDP	3	5	5	5
Collateralized Debt				
Percent of external debt	13	9	5	3
Percent of GDP	4	3	2	1

Sources: Malawian authorities; and IMF staff calculations

1/As reported by country authorities according to their classification of creditors, incl. by official and commercial. Debt coverage is the same as the DSA.

2/Multilateral creditors are defined here as institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears).

3/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.

4/Debt ratios are constructed by converting external debt to MWK using end-period exchange rate and dividing by GDP in MWK.

Table 11. Malawi: Prior Actions Under the ECF Arrangement		
Actions	**Objective**	**Status**
External Sector Reforms		
• RBM to announce, via public circular, changes to its FX operations, to include: (i) increasing the frequency of purchase operations to at least on a fortnightly basis and removing any implicit or explicit constraints on access, allotment or prices submitted; (ii) allowing FX intermediaries to trade at freely negotiated rates with their clients and between themselves; and (iii) if the RBM were to conduct FX sales, sales should be done via auction (in line with the recommendations of "The Review of the Fund's policy on Multiple Currency Practices—Proposals for Reform", paragraph 15).	• To increase transparency, broaden participation and facilitate greater flexibility in the official exchange rate, and to reduce economic distortions and opportunities for corruption.	• Draft received on October 13.
• Submit to IMF staff audits of NIR from end-December 2022, end-March, and end-June 2023.	• Foster transparency and monitoring of foreign exchange reserves. • Improve data quality.	• Draft audit reports received on October 21. • Finalized reports submitted on October 27.
Fiscal Reforms		
• Roll out core functionalities of IFMIS to key MDAs with mandatory use. The core functionalities will include: (i) capturing all existing contracts / commitments in IFMIS, (ii) issuance of quarterly spending limits	• Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption.	• **Met**

Table 11. Malawi: Prior Actions Under the ECF Arrangement (concluded)

Actions	Objective	Status
Fiscal Reforms		
and monthly payment requiring funding, (iii) requiring all financial transactions to be entered through IFMIS at the commitment.	• Ensure new IFMIS delivers on accountability and efficiency in the execution of PFM reforms.	• **Met**
• Prepare a contingency plan to close the financing gap in case the baseline fiscal path faces implementation challenges.	• Minimize fiscal risks associated with shortages in domestic revenue and financing.	• Submitted on October 30.
• Implement the specific tax on second-hand motor vehicles.	• Enhance revenue and improve tax and customs compliance culture. • Enhance revenue and improve transparency in duty rates of secondhand cars, as well as contain secondhand car imports.	• Gazette received on October 28.
Governance Reforms		
• Follow-up action report on the COVID-19 spending audit report and EDF's audit report. Publish a follow-up report related to the COVID-19 spending audit report, detailing the corrective actions and measures to pursue and respond to audit findings, including the follow-up of alleged misappropriation of funds as well as the coverage of a second audit findings.	• Strengthen governance and data transparency.	• Published on October 27.

Table 12. Malawi: Structural Benchmarks Under the ECF Arrangement		
Actions	**Timing**	**Objectives**
Fiscal Reforms		
• Publish the monthly unaudited IFMIS-generated comprehensive fiscal reports on the MOFEA website, within 5 days after end of each month starting end-October 2023.	• Continuous, starting in FY2023/24	• Foster fiscal transparency and monitoring. • Improve the in-year comprehensive monthly fiscal reports.
• Repeal the preferential treatment for motor vehicle and VAT relief for current and former politicians, senior public officials, judges and other similar privileged individuals and groups.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.
• Ensure that every supply of a motor vehicle is standard rated for VAT purposes.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.
• Comprehensively eliminate VAT exemptions and zero-ratings for business inputs. • The sectors under these Customs Procedures Codes will be subjected to subsequent SBs: CPC 402 for (pharmaceutical and fertilizer manufacturing), 405 (health), 406 (education) 445 (priority industry and Government to Government Agreements). • "business" input means all goods imported by businesses specifically for their operations.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.

Table 12. Malawi: Structural Benchmarks Under the ECF Arrangement (continued)		
Actions	**Timing**	**Objectives**
Fiscal Reforms		
• Repeal VAT relief for building materials such that all supplies of building materials, construction services and commercial property are standard rated. • The following sectors will be subject to subsequent SBs: Education, Health, Priority sector and where there is an Agreement between Malawi Government and other Governments or bona fide institutions.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.
• Full launch of the Integrated Tax Administration System (ITAS)	• End-March 2024	• Enhance revenue and improve tax and customs compliance culture
• Approval by the Cabinet of an arrears clearance and prevention strategy for national budget entities that has been in consultation with Fund staff.	• End-March 2024	• Foster financial discipline.
• Publish a performance report outlining the status of project execution and spending for all projects, with a total estimated cost of at least MWK 25 billion in the Public Sector Investment Program (PSIP) on the MOFEA website, within 6 months after the fiscal year.	• Annually, starting in 2025	• Improve public investment management. • Support Malawi 2063

Table 12. Malawi: Structural Benchmarks Under the ECF Arrangement (continued)		
Actions	**Timing**	**Objectives**
Monetary and Financial Sector Reforms		
• Prepare, in consultation with Fund staff, draft amendments to the RBM Act as recommended by the 2021 Safeguards Assessment report and submit those amendments to public consultation	• End-December 2023	• Strengthen RBM governance.
• Submit the RBM Act amendments to Parliament	• End-March 2024	• Strengthen RBM governance.
External Sector Reforms		
• Progressively remove the four multiple currency practices and three exchange restrictions measures identified by Fund staff	• Gradually, starting 2024	• Strengthen the functioning of a market-determined exchange rate.
Governance Reforms		
• MOFEA and RBM jointly design and implement a credible, comprehensive, and cost-effective resolution plan to address challenges identified in the audit of the EDF.	• End June 2024	• Strengthen governance and transparency.
• Improve transparency and management of EDF via improved organizational arrangements and action on audit findings	• End June 2024	• Strengthen governance and transparency.
• NSO to start including reconciled data on imports of strategic commodities in the monthly Trade Bulletin	• End-December 2023	• Develop greater transparency in relation to strategic imports and to reconcile the varying sources of fuel imports data.

Table 12. Malawi: Structural Benchmarks Under the ECF Arrangement (concluded)		
Actions	**Timing**	**Objectives**
Governance Reforms		
• Develop an action plan with specific deliverables and deadlines following the governance diagnostic TA.	• September 2024	• Strengthen governance and transparency.
Climate		
• Submit to Parliament the Disaster Risk Management (DRM) regulations and related policies to address gaps in disaster risk management. • (i) Building policy • (ii) Gazette Disaster Risk Management Regulations	• December 2024 • December 2023 • June 2024	• To guide developments in the area of disaster preparedness, risk reduction, and response and recovery buildings.

Annex I. Risk Assessment Matrix[1]

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Global Risks			
Intensification of Regional Conflict(s)	High	Medium Escalation of Russia's war in Ukraine or other regional conflicts and resulting economic sanctions disrupt trade (e.g., energy, food, tourism, and/or critical supply chain components), remittances, refugee flows, FDI and financial flows, and payment systems.	Strengthen intra-regional trade among sub-Saharan African countries to overcome supply chain disruptions.
Commodity Price Volatility	High	Medium A succession of supply disruptions (e.g., due to conflicts and export restrictions) and demand fluctuations (e.g., reflecting China reopening) causes recurrent commodity price volatility, external and fiscal pressures, and social and economic instability.	Tighten monetary policy, increase exchange rate flexibility, strengthen FX reserve buffer, apply the automatic fuel price adjustment mechanism and replenish the fuel price stabilization to ensure adequate energy supplies and contain fiscal cost/contingent liabilities.
Social Discontent	High	High Supply shocks, high inflation, real wage drops, and spillovers from crises in other countries worsen inequality, trigger social unrest, and give rise to financing pressures and damaging populist policies with possible spillovers to other Emerging Markets and Developing Economies. This exacerbates imbalances, slows growth, and triggers market repricing.	Encourage the authorities to maintain social priority spending in the face of development assistance contraction to build the resiliency of vulnerable populations. Undertake promised reforms in a transparent and equitable manner. Strengthen governance measures.
Systemic Financial Instability	Medium	Medium Sharp swings in real interest rates, risk premia, and assets repricing amid economic slowdowns and policy shifts trigger insolvencies in countries with weak banks or non-bank financial institutions, causing markets dislocations and adverse cross-border spillovers.	Upfront action to address debt sustainability and avoiding external non-concessional borrowing. Resorting to debt management strategy which relies on grants and highly concessional loans.
Abrupt Global Slowdown or Recession	Medium	Medium Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and markets fragmentation.	Encourage the authorities to expand the domestic revenue base in order to compensate for any fall in development assistance.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term (ST)" and "medium term (MT)" are meant to indicate that the risk could materialize within 1 and 3 years, respectively.

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Regional and Domestic Risks			
Delay in Debt Work Out	Medium (assuming that we are moving forward with an ECF request)	**High** Further delays in debt workout can reduce access to trade credit, foreign exchange swaps, and other short-term loans, worsen foreign exchange shortages and result in difficulties in importing key commodities (fuel, medicine and food) and servicing debt; which would in turn exacerbate dire macroeconomic conditions, poverty, and food insecurity.	Work with debt advisor(s) and take decisive policy action that is needed to restore debt sustainability and close financing gap.
Governance Weaknesses	High	**High** Overly ambitious capital investment beyond the country's absorptive capacity and weak institutions can result in a misuse of public resources, resulting in a rise in debt with little impact on growth. Conflicting signals on policy intentions can also adversely affect market participants' confidence.	Strengthen institutions to address weaknesses in governance, roll out of IFMIS, supported by the authorities' credible reforms. Strengthen public investment management (PIM).
Delayed PFM Reforms, Lack of Expenditure Control, and DRM	Medium	**High** Uneven progress of PFM reform, deficient expenditure control, and lack of progress in domestic revenue mobilization (DRM) undermine confidence in budgetary execution and efforts to effectively and transparently manage expenditure within available resources. Re-emergence of arrears resulting from delays in PFM reforms will add to debt distress.	Accelerate implementation of PFM reform programs, strengthen commitment control, maintain DRM efforts, and communicate regularly and transparently on the budget execution within available resources.
Fiscal dominance resulting in deficient conduct of monetary policy	High	**High** Inability to keep reserve money growth in line with nominal GDP growth can result in pressure on the exchange rate, the RBM's foreign exchange reserves, and inflation. Conflicting signals on policy intentions can also adversely affect market participants' confidence.	Strengthen RBM independence. Maintain a positive real interest rate. Reinstate a clear and effective monetary operational framework.
Natural disasters related to climate change	High	**High** More frequent natural disasters with severe damages to infrastructure can amplify supply chain disruptions, inflationary pressures, and water and food shortages. They would also reduce medium-term growth prospects.	Build economic resilience, through human capital investment, and addressing deforestation.

Annex II. Fuel Imports and Mass Motorization

Booming fuel imports are a leading cause of Malawi's balance of payments pressures and depletion of official foreign reserves. Economic fundamentals do not explain this boom; it appears rather rooted in misaligned policies.

1. **Fuel consumption has been rising and far exceeds the levels of peer countries**. Malawi's fuel imports grew on average 7.7 percent each year during the past 6 years; from 358 million liters in 2016 to 558 million liters in 2022. This rate of growth exceeds population growth (2.7 percent), urban population growth (4.2 percent) or real GDP growth (3.2 percent) by far. In U.S. dollar terms, fuel imports grew by an estimated 2.7 times from $212 million in 2016 to $571 million in 2022,[2] putting significant pressure on the BOP. Fuel consumption per capita (27.9 liters per capita) also seems to be at the level consumed in much more industrialized countries (e.g., Vietnam) and seems to be much higher than that of neighboring countries.

2. **The public sector plays an increasing role in fuel imports**. Fuel imports in the midst of foreign exchange shortages in 2022 led to a shift in market share towards a public fuel importer:

- Petroleum Importer Limited (PIL) has imported 212 million liters in 2022, an 18 percent reduction from 2021. Since its inception in 2000, PIL, a private sector company jointly owned by four large fuel distributors, used to import nearly all fuel to Malawi.

- On the other hand, National Oil Company of Malawi (NOCMA), a state-owned company recorded a substantial increase in fuel imports in 2022. NOCMA's imports grew from 209 million liters in 2021 to 301 million liters in 2022. NOCMA started importing in 2012 after the acute shortages of fuel to build oil reserves for the country. It now has a 55 percent market share.

3. **Fuel prices are set by a regulator and are held at a very low level**. Fuel pricing is regulated by Malawi Energy regulatory Authority (MERA).

- Fuel prices are determined by a formula that uses the official exchange rate, bulk import prices, and a mark-up. Normally, the price of fuel would be adjusted on a monthly basis, but the last adjustment occurred in the second half of 2022.

- The current petrol price is MK1746 per liter ($1.58 per liter at official exchange rate at end-September 2023) is higher than Tanzania ($1.282 per liter), Mozambique ($1.350 per liter) or Zambia ($1.402 per liter) but lower than Zimbabwe ($1.650 per liter) or highly taxed countries such as Germany ($2.016 per liter) or UK ($1.913 per liter). However, at the informal market exchange rate the price in Malawi would be around $1 per liter, one of the lowest in the world,

[2] The U.S. dollar value equivalent is calculated using Malawi Energy Regulatory Authority (MERA)'s fuel import volume, landing costs, and the period average exchange rate. These values are different from fuel imports reported in the RBM's Financial and Economic Review (FER) which are used for the macroeconomic framework (Tables 4a and 4b). The FER reports a much smaller increase from $222 million in 2016 to $239 million in 2022 but the 2022 data are expected to be revised upward.

benefitting drivers who are able to obtain local currency at the black market (including commercial drivers from neighboring countries).

4. Financing fuel imports is becoming increasingly difficult as Malawi's external position has deteriorated.

- *International banks stopped confirming letters of credit (LC) since the end of 2022*. Private sector fuel importers (mainly PIL) rely on LC from local banks promising payment once an exporter ships fuel. Oil suppliers/exporters typically require that local banks' LCs be confirmed by an international reputable bank. Most local banks cannot get LCs confirmed since the end of 2022 unless the full value of imports is deposited upfront.

- *Supplier credit lines have been exhausted*. PIL is enjoying an open credit line of $20 million (on a rolling, monthly basis) with one of Malawi's main oil suppliers. The binding constraint, however, has been the availability of foreign exchange to service the credit line. PIL has not been able to purchase US$20 million per month to service the credit line and the supplier requires upfront payment for all further supplies.

- *RBM has been selling foreign exchange*. Meeting the demand for foreign exchange for fuel imports contributes largely to RBM's struggle to accumulate foreign exchange reserves.

5. Rapid motorization seems to have been driving the rising fuel demand. Japanese secondhand (or used) car imports more than doubled from 2,948 cars in 2016 and 7,368 cars in 2022. There may have been both push and pull factors resulting in this rapid growth:

- Prices in Malawi are comparatively low, reflecting lower taxation levels. Like in much of the region, Malawi's car supply is mainly sourced as secondhand imports from wealthier left-hand drive countries, primarily Japan but also Australia, Singapore, and Thailand. A few companies provide competitive services that allow African customers to select a vehicle online and have it shipped, imported, and registered in their country. The transparency of these companies' business model allows a comparison between secondhand car prices in the region; price differentials are due only to differences in transport costs and local taxation (including VAT, excise, duties, and related fees). Despite the higher transport costs to Malawi (requiring transit shipment through Tanzania), Malawi's car import prices are consistently the lowest.

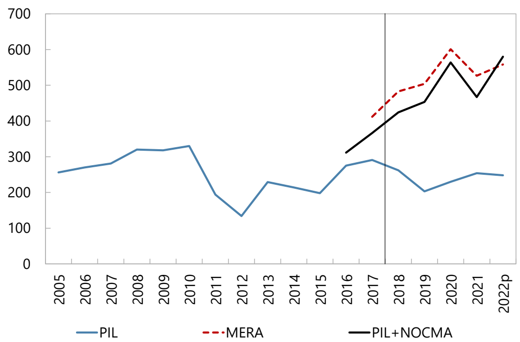
- Japanese secondhand car exports grew rapidly since 2001. They plummeted during the global financial crisis in 2008-09, saw a dent during the China stock market turbulence in 2016, and another dent during the pandemic in 2020-21, implying that they are sensitive to world economic conditions. There may have been a shift in the export destination from elsewhere towards the African market which became much more accessible via online sales and settlements via mobile phones.

6. The high level of vehicle imports constitutes a drain of scarce foreign exchange earnings but also causes elevated demand for fuel (and political pressures for low and stable fuel prices). Mass motorization and the resulting fuel demand constitute a macro-critical risk factor. Furthermore, the relative under-taxation of vehicles and fuel imply a sizeable loss of potential revenue. To address it, the following policy actions may be considered: (i) closing VAT loopholes and ensuring all residents pay the full tax on vehicle imports; (ii) raising import taxes on vehicles to (at least) the regional average; (iii) updating the fuel price formula, including by applying a market-based exchange rate; and (iv) raising fuel taxes.

Table 1. Malawi: Fuel Imports and Mass Motorization, 2005–22

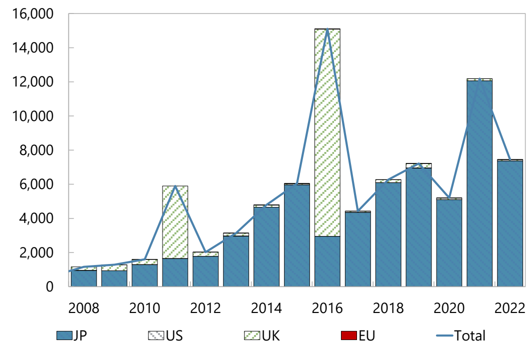
Malawi's fuel imports grew on average 7.7 percent from 358 million liters in 2016 and 588 million liters in 2022.

Fuel Imports, 2005-22
(Million liters)



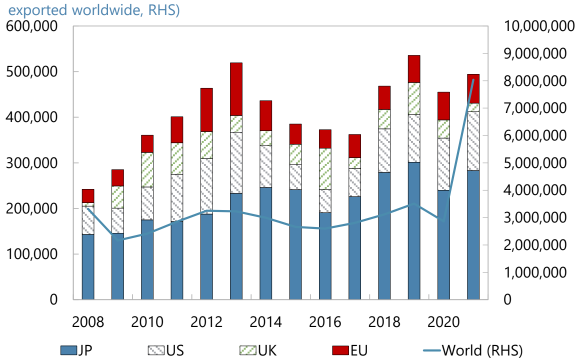
Stock of used motor vehicles tripled from 28 thousand in 2015 to 86 thousand in 2022.

Used Car Exports to Malawi, 2008-22
(Total number of used vehicles exported by country)



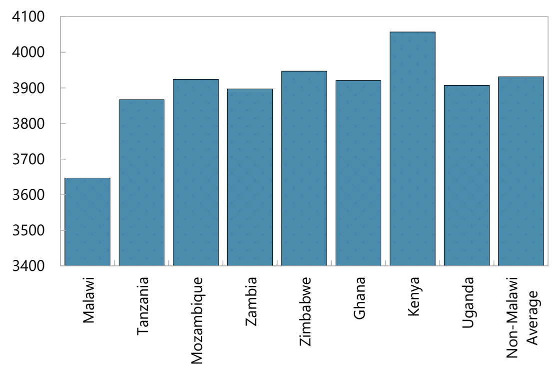
... partly due to a shift in the export destination from elsewhere towards Africa (a push factor)...

Used Car Exports to Select SSA Countries, 2008-21
(Total number of used cars exported by region, LHS; Total number of used cars exported worldwide, RHS)



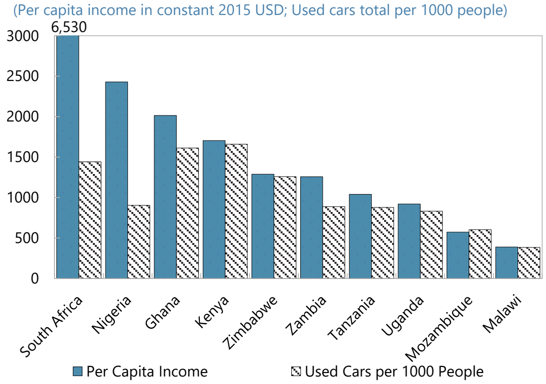
...and partly due to lower prices in Malawi (a pull factor).

Toyota Sienta DICE Price Comparison, 2023
(Prices in USD, inclusive of all taxes)



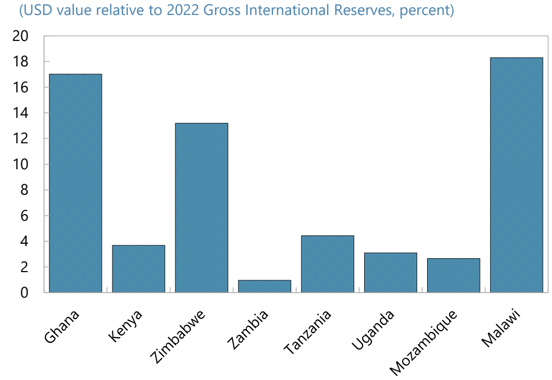
The stock of used cars in Malawi seems broadly in line with peers once adjusted for income differentials...

Stock of Used Cars, 2021
(Per capita income in constant 2015 USD; Used cars total per 1000 people)



... but the stock of used cars (in US$) relative to gross international reserves is the highest among peers.

Stock of Used Cars, 2021
(USD value relative to 2022 Gross International Reserves, percent)



Sources: BeForward; Japan Used Motor Vehicle (JUMV); United States Department of Commerce; Eurostat; UK Trade Info, HM Revenue and Customs; World Bank WDI; IMF WEO; and IMF staff calculations.

Annex III. External Sector Assessment

Overall Assessment: *The external position of Malawi in 2022 was weaker than the level implied by fundamentals and desirable policies. The reported current account (CA) deficit narrowed significantly in 2022, reflecting a reduction in consumption in response to shortages of foreign exchange and an increase in informal imports. But Malawi has continued to struggle to accumulate foreign exchange reserves and periodic shortages of key imports have persisted through the first half of 2023. Despite limiting its uptake of new non-concessional external debt, Malawi continues to face a significant debt service burden on its existing stock of external debt.*

Potential Policy Responses: *Addressing Malawi's external sector imbalances requires significant macroeconomic and other policy adjustments. This includes efforts to develop a diversified and competitive export sector and to reduce the misalignment of the exchange rate. In the longer term, the authorities' strong commitment to a coherent package of policies can restore confidence in Malawi and lead to non-debt-creating grants and Foreign Direct Investment (FDI). These policies include fiscal consolidation, monetary tightening, financial supervision strengthening, and improving governance issues and reducing corruption. Significant improvement in data compilation and reporting is also essential.*

Current Account

Background. The CA deficit narrowed to 3.2 percent of GDP in 2022 from 14.1 percent in 2021. This reduction reflected both a significant squeeze on the consumption of goods purchased abroad—as evidenced by widespread shortages of fuel, fertilizer and other items—and a substantial increase in the share of informal imports in the context of stigma associated with transacting away from the official exchange rate. The role for increased informal imports is corroborated by discussions with the authorities and sizeable discrepancies between the official imports data and other cross-checks. Therefore further revisions to the imports data are expected. In the medium term, the CA deficit is expected to stabilize around 7 percent of GDP (some way below its five-year historical average of 16 percent), reflecting greater availability of foreign exchange and a re-formalization of goods trade in the context of a more stable macroeconomic environment.

Assessment. The EBA-Lite 3.0 CA model suggests that Malawi's external sector position is weaker than the level implied by medium-term fundamentals and desirable policies, after attempting to correct for the temporary distortions to the import data described above.[1] Based on the CA model, the cyclically-adjusted CA deficit after this adjustment and COVID-19 (0.1pp) and natural disaster (-0.1pp) adjustors stood at 9.4 percent of GDP in 2022. This points to a gap of 2.7 percent of GDP compared to the cyclically-adjusted CA norm of -6.6 percent of GDP. Of this gap, 0.5pp can be explained by quantifiable deviations from desirable policies.

Malawi: EBA-lite Model Results, 2022		
	CA model 1/	**REER model**
	(in percent of GDP)	
CA-Actual	**-3.2**	
Cyclical contributions (from model) (-)	0.2	
COVID-19 adjustors (-) 2/	0.1	
Additional temporary/statistical factors (-) 3/	6.0	
Natural disasters and conflicts (-)	-0.1	
Adjusted CA	**-9.4**	
CA Norm (from model) 4/	**-6.6**	
CA Gap	**-2.7**	**0.3**
o/w Relative policy gap	-0.5	
Elasticity	-0.1	
REER Gap (in percent)	**22.3**	**-2.1**

1/ Based on the EBA-lite 3.0 methodology.

2/ Additional cyclical adjustment to account for the temporary impact of the pandemic on tourism (0.1 percent of GDP).

3/ Additional statistical adjustment to correct for distortions introduced by the assumed temporary increase in the share of informal goods trade in 2022.

4/ Cyclically adjusted, including multilateral consistency adjustments.

Real Exchange Rate

Background. The real effective exchange rate (REER) depreciated by 5 percent in 2022, given that the depreciation of the nominal exchange rate was offset somewhat by an increase in relative domestic prices. The spread between the official exchange rate and the market (forex bureau) and other parallel rates widened significantly in 2022 and has remained elevated through the first half of 2023. Notwithstanding efforts to let the official rate depreciate (including via regular auctions) and tentative signs of macroeconomic stabilization, the further increase in the spread is likely to reflect increased uncertainty in the face of continued foreign exchange shortages, as well as speculative activity.

Assessment. The EBA-Lite CA model suggests that the REER is overvalued—by 22.3 percent—relative to the level implied by fundamentals and desirable policy settings. This is less than the spread between the official rate and the bureau rate, suggesting the rate consistent with fundamentals may lie between the two. But as above the difficulties associated with interpreting the 2022 data present the same caveats to this assessment, which should be considered more uncertain than in previous years. The REER model of the gap suggests the exchange rate is closer to fair value, illustrating this uncertainty.

Capital and Financial Accounts: Flows and Policy Measures
Background. Malawi benefits from large capital inflows, consisting mainly of project loans and off-budget support from international donors, to help finance persistent current account deficits. The capital account, balance declined slightly to 6.2 percent of GDP in 2022 (versus an average of 8.8 percent in the preceding five years) but is projected to recover in 2023 and remain relatively stable through the medium term. The capital account comprises mostly on and off-budget grants (transfers) for fixed capital formation. The financial account balance is more volatile, comprising largely of other investment flows, with the caveat that data quality is considered poor. FDI remains small (0.3 percent of GDP in 2022) and is projected to grow only slowly. The authorities continue to impose a surrender requirement on exports that is considered an outflow Capital Flow Management measure (CFM). **Assessment.** Under the PMB, Malawi has reduced its reliance on new non-concessional external debt and an ECF arrangement is expected to catalyze further significant donor support. The use of the surrender requirement can be considered justified given the crisis conditions that Malawi has faced in the recent period. But the authorities should aim to normalize these controls as conditions improve. Data quality can also be improved.
FX Intervention and Reserves Level
Background. Unsustainable macroeconomic policies have seen pressure on the exchange rate and a drain of foreign currency out of Malawi. Gross reserves reached an extremely low level in 2022, amounting to less than 1 percent of GDP. This situation has stabilized in 2023, largely reflecting the RBM's capacity to retain foreign currency associated with project-related and other flows, with outright purchases of foreign currency (including via the surrender requirement) still insufficient to offset sales to fund strategic imports and other expenses. The RBM has maintained a generally stable official exchange rate but has not had the resources to prevent the emergence of significantly weaker parallel rates. The exchange rate regime could be characterized as 'de jure' floating exchange regime but 'de facto' stabilized. **Assessment.** The reserve adequacy model for credit constrained economies suggests that Malawi should maintain reserves equal to at least 3.9 months of import cover to provide adequate insurance against external shocks. This is notably higher than the 0.8 months of import cover provided by Malawi's gross reserves in 2022. Rebuilding external buffers will require a determined effort by the central bank, as well as the successful completion of Malawi's external debt restructuring strategy. A more sustainable and equitable exchange rate regime would also attract more foreign exchange into the country, as well as reducing distortions and incentives for corruption and smuggling.

Annex IV. Capacity Development Strategy for FY2023/24

1. The Fund continues to provide TA and training to support the authorities' reforms and help to build capacity, coordinating closely with TA from other development partners.

- PFM TA to the **Ministry of Finance and Economic Affairs** has focused on reforms in the critical areas of bank reconciliation, payment efficiency, in-year and year-end financial reporting, budgeting, expenditure control, cash management, SOE oversight, public investment management, implementation of the new IFMIS and management of fiscal risks. While some progress has been made, there is a need for the authorities to ramp up implementation of the new IFMIS, cash management, commitment controls, automatic reconciliation with the government's bank statements, and fiscal reporting and to improve the quality, analysis, use and publication of available information.

- TA to the **Reserve Bank of Malawi** has focused on financial sector supervision and Forecasting and Policy Analysis System (FPAS) TA on forecasting and inflation and monetary policy analysis to support modernizing its monetary policy framework. Going forward, TA should be tailored to deepen interbank foreign exchange market and improve central bank monetary operations to better manage money growth. TA to strengthen the stress testing framework of the RBM should also continue.

- TA will support a **governance** diagnostic to identify governance weaknesses and corruption vulnerabilities.

- Lastly, on statistics, TA has focused on supporting the authorities' progress towards improving the quality and regular reporting of data on national accounts, BOP, government finance and monetary and financial statistics as well as developing export and import price indexes. Additional efforts to refine Malawi's external sector data are needed. Staff efforts to encourage greater transparency in relation to strategic imports and to reconcile the varying sources of fuel imports data have resulted in some progress. But more work is needed as a failure to capture a growing share of trade activity has made interpretation of Malawi's balance of payments position increasingly challenging.

2. Going forward, the CD strategy and priorities for Malawi need to continue supporting the authorities' objectives outlined in Malawi 2063. The priorities are summarized below:

TA Priorities	Objectives
Public Finance Management	- Step up implementation of the new IFMIS as an enabler for key PFM reforms in fiscal reporting, budget preparation, expenditure control, bank reconciliation, cash management, payment efficiency and accountability.

TA Priorities	Objectives
	- Strengthen the management of fiscal risks and the oversight of state-owned enterprises. - Improve public investment management systems
Tax Policy and Revenue Administration	- Enhance domestic resource mobilization including through broadening the tax base to include informal sector and rolling out the new Integrated Tax Administration System (ITAS) and supporting the fine-tuning and implementation of the mining tax policy regime. - Review and redesign customs clearing controls and procedures, improve VAT compliance and promote integrity within MRA.
Banks supervision and regulation	- Strengthen the stress testing framework of the Reserve Bank of Malawi
Monetary policy operations	- Enhance the effectiveness of open market operations.
Governance	- Undergo a governance diagnostic to identify governance weaknesses and corruption vulnerabilities. - Develop an action plan with specific deliverables and deadlines following the diagnostic.
Statistics	- Continue improving compilation and dissemination of statistics and developing staff capacity, with a focus on the national accounts, the consumer price index, producer price index, export and import price indexes, fuel imports, BOP, International Investment Position, Government Finance Statistics, public sector debt statistics, and monetary statistics. - The National Statistics Office (NSO) to publish the revised GDP series by production and by expenditure for the base year 2017. - Strengthen public sector debt statistics.

Appendix I. Letter of Intent

November 8, 2023

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

Dear Madame Kristalina Georgieva,

Malawi has made tangible progress in its macroeconomic adjustment and reform implementation, despite a challenging domestic and external environment. We successfully completed macroeconomic adjustment agenda under our Staff Monitored Program with Board Involvement (PMB) approved in November 2022. Under the PMB, the government implemented significant fiscal consolidation by reining in on expenditure, containing government borrowing, and slowing the expansion of monetary base. The Reserve Bank of Malawi (RBM) has taken appropriate policy steps to contain pressures on inflation and on the exchange rate. We have made progress in our debt restructuring strategy. Going forward, we continue to pursue good faith negotiations with commercial creditors and are in arrears on commercial debt while these discussions continue. We are also making tangible progress in securing financing assurances from all our official bilateral creditors. Indeed, performance under the Second Review of the PMB based on end-June 2023 targets were much improved relative to the first review; 5 out of 6 quantitative targets (QTs) were met.

Despite the progress achieved, challenges remain. The increasing frequency and intensity of climate-related shocks are negatively affecting our economic growth prospects. Barely a year since the two cyclones in early 2022, we were hit by Cyclone Freddy in March 2023 resulting in a significant death toll, the highest in the history of cyclones in Malawi and the destruction of critical infrastructure. In addition, from late 2022 to early 2023, Malawi experienced its worst outbreak of cholera in decades, forcing the closure of schools and businesses. Consequently, growth outlook is weaker than initially projected and our economy continues to face protracted balance of payments challenges. The foreign exchange reserves of the RBM remain under pressure while inflation has persisted, standing at 28.6 percent (y-o-y) at end-August 2023. The challenging economic conditions and erosion of purchasing power have negatively affected Malawians, more so the most vulnerable households, already facing a high risk of food insecurity.

Going forward beyond the 12-month PMB, we would like to request a 4-year Extended Credit Facility (ECF)-supported arrangement. In line with our long-term vision to create an inclusively wealthy nation under Malawi 2063, and its First 10-Year Implementation Plan (MIP-1, 2021-2030), we are of the view that the ECF-supported arrangement will support our aspiration to graduating into a lower middle-income economy and achieving most of the Sustainable Development Goals by 2030. We are requesting the approval of a four-year ECF-supported arrangement in the total amount equivalent to SDR 131.86 million for the period November 2023-October 2027. The ECF-supported arrangement will support our macroeconomic and structural reform program. The government is also requesting the immediate disbursement of the first tranche, totaling SDR 26.372 million (19 percent of quota).

The attached Memorandum of Economic and Financial Policies (MEFP) describes recent developments in the Malawian economy and articulates specific policy objectives under the proposed ECF-supported arrangement. It reflects the understandings reached with IMF Staff during the August 29 – September 20 Mission. Our policy objectives are to restore a stable and sustainable macroeconomic position consistent with strong and durable poverty reduction and growth. We will continue to focus on measures to enhance fiscal discipline, maintain price stability and financial soundness, rebuild external buffers, and restore debt sustainability. These reforms will be implemented alongside efforts to address longstanding governance weakness and corruption, including in relation to public procurement. Given our limited fiscal space, we will prioritize expenditure to ensure adequate support to the vulnerable by safeguarding Government's contribution to social safety net programs such as the Social Cash Transfer Program (SCTP), and to protect investment in infrastructure. We are confident that these policies will support the ongoing macroeconomic adjustment program and catalyze grant financing.

The implementation of our program will be monitored through quantitative performance criteria and indicative targets, as described in the attached Technical Memorandum of Understanding (TMU). There will be seven reviews under the ECF-supported arrangement, scheduled to be completed on a semi-annual basis until July 2027. The reviews will assess program implementation progress and reach understandings on additional measures needed to achieve the program objectives.

We are confident that through the implementation of measures and policies described in the attached MEFP, we will attain the objectives of the ECF-supported arrangement. That said, we stand ready to take additional measures that may be needed over and above those articulated in the MEFP in consultation with IMF staff in accordance with the Fund's policy. We also assure you that we will submit all program monitoring information outlined in the attached Technical Memorandum of Understanding (TMU) on a regular and timely basis and will also pro-actively share any other information that may be necessary to evaluate progress made under the ECF-supported program. We intend to make public the contents of the IMF staff report, including this letter, the attached MEFP, the TMU, the informational annex, and the Debt Sustainability Analysis (DSA) carried out by IMF and World Bank staff. As such, we authorize the IMF to publish these documents accordingly.

Yours sincerely,

/s/	/s/
Honorable Simplex Chithyola	Dr. Wilson T. Banda
Minister of Finance and Economic Affairs	Governor of the Reserve Bank of Malawi

Attachments:

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

Attachment I. Memorandum of Economic and Financial Policies

November 8, 2023

INTRODUCTION

1. **The Government of Malawi is implementing a wide-ranging and ambitious macroeconomic and structural reform program in line with the Malawi 2063.** The overarching goal of the Government's efforts is to rebalance the economy to accelerate sustainable and inclusive growth and increase resilience with the aspiration of building an inclusively wealthy and self-reliant industrialized upper-middle-income country. This is in the context of growing threats from economic shocks and natural disasters related to climate change. Our medium-term strategy outlined in the Malawi 2063 First 10 Year Implementation Plan (MIP-1) aims at transforming Malawi into a middle-income economy by 2030 and ensuring the achievement of the 2030 Agenda for Sustainable Development. In this context, Government remains deeply committed to implementing its reform agenda, which is fully aligned with our objectives under this ECF-supported program.

2. **Malawi's already vulnerable macroeconomic foundation has been further damaged by a sequence of external shocks in recent years, necessitating accelerated implementation of reforms to restore macroeconomic stability and support economic recovery.** His Excellency the President Dr. Lazarus McCarthy Chakwera assumed office as President of the Republic of Malawi on 28th June, 2020. At the time, the country was in the midst of the COVID-19 pandemic which hit Malawi's already unstable macroeconomic conditions with significant balance of payment imbalances, debt challenges and an over-valued exchange rate. Over the past years, a combination of weather-related events, health triggered crises and the impact of the Russia-Ukraine war on inflation have put further pressure on the balance of payments and fiscal position of Malawi. The supply chain challenges that emerged from the Russia-Ukraine crisis also led to constrained access to key agricultural inputs, further increasing food insecurity for the population. These developments triggered an ongoing balance of payments crisis while Malawi is in debt distress and external debt has been assessed as unsustainable according to the IMF and World Bank Debt Sustainability Framework for Low-Income Countries (LIC-DSF). Recently, the devastating impact of Cyclone Freddy, resulting in an enormous death toll and destruction of critical infrastructure, put additional pressure on the country's fiscal and external position. This asks for a combination of emergency response to support those impacted by the crisis, while accelerating the debt restructuring process with external creditors.

3. **Performance under the Second Review of the PMB based on end-June 2023 targets was satisfactory, reflecting an improvement from the first review** (Tables 1 and 2). All but one end-June quantitative targets were met. The quantitative target (ceiling) on the stock of monetary base was not met despite RBM's efforts to mop up liquidity through its open market operations. In addition, commercial banks deposit holdings at the RBM increased following an upward adjustment in Liquidity Reserve Ratio (LRR) effected in April 2023. While raising LRR is aimed at

Table 1. Malawi: Quantitative and Indicative Targets[1] Under the PMB, 2022–23

	Target type [2]	2022				2023								
		End-Dec.				End-Mar.				End-June				End-Sept
			Adjusted				Adjusted				Adjusted			
		QT	QT	Est.	Status	IT	IT	Est.	Status	QT	QT	Est.	Status	IT
I. Monetary targets (billions of kwacha)														
Monetary base (ceiling on stock) (upper bound)[3]	QT	590.2				607.6		578.5		633.3		0.09		685.6
Monetary base (ceiling on stock)[3]		573.0		570.9	met	589.9		561.7	met	614.9		690.0	not met	665.6
Monetary base (ceiling on stock) (lower bound)[3]		555.8				572.2		544.8		596.4				645.6
II. Fiscal targets (billions of kwacha)														
Domestic revenue (floor)[6]	IT	1,202.7		1,230.6	met	1,603.5		1,658.5	met	418.1		488.6	met	834.6
Domestic primary fiscal balance (floor)[4,6]	QT	-17.1	-36.2	-198.8	not met	-70.0		-304.4	not met	-7.4		43.7	met	-83.0
RBM financing of central government (ceiling)[6,7]	QT	0.0	160	215.9	not met	0	160	212.2	not met	0	209	21.5	met	0
New domestic arrears (ceiling)[6]	IT	0.0		n.a.	n.a.	0		148.3	not met	0		n.a.		0
Social spending (floor)[6,8]	IT	503.7		610.4	met	669.3		868.1	met	203.2		208.6	met	409.8
III. External sector targets (US$ millions, unless otherwise indicated)														
Change in net international reserves of the RBM (floor)[5]	QT	141.3	122.7	116.0	not met	7.0	-23.8	-16.3	met	87.9		120.2	met	150.4
Accumulation of external payments arrears (ceiling)[6,9]	QT	0		0	met	0		0	met	0		0.0	met	0
Contracting or guaranteeing of nonconcessional external debt (ceiling)[6,9,10]	QT	0		50	not met	0		50	not met	0		0.0	met	0
Contracting or guaranteeing of concessional external debt (ceiling)[6]	IT	15		284	not met	30		284	not met	0		0.0	met	0
Memorandum items:														
Program exchange rate (kwacha per US$)		1,026.4		1,026.4		1,026.4				1,026.4				1,026.4

Source: IMF staff projections.

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

[2] "QT" means Quantitative Target and "IT" means Indicative Target. The QT test date for the 1st Review is end-December 2022. Test dates for future reviews will be end-June 2023. End-March and end-September 2023 targets are ITs.

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

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

[5] Targets are subject to an adjustor for (i) debt service and fees and (ii) general budget support, as specified in the TMU. Foreign currency drains related to undrawn Letters of Credit with TDB are included for end-December 2022 estimate.

[6] Defined in nominal terms as a cumulative flow, starting from the beginning of the fiscal year. Note that targets for end-December 2022 and end-March 2023 were set from the beginning of the program.

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

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

[9] Evaluated on a continuous basis.

[10] For program purposes, a limited exception on NCB may be allowed only in the exceptional circumstance that it is used to wind down maturing swaps and for debt management operation that improves the overall debt profile.

Table 2. Malawi: Structural Benchmarks Under the Staff Monitored Program		
Actions	**Timing / Status**	**Objectives**
Fiscal Reforms		
Roll out full functionalities of IFMIS to all MDAs. The full functionalities will include: (i) capturing all existing contracts / commitments in IFMIS, (ii) issuance of quarterly spending limits and monthly payment funding, (iii) requiring all financial transactions to be entered through IFMIS at the commitment.	End-March 2023 **Not Met** **Moved to a PA for the ECF arrangement**	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption. Ensure new IFMIS delivers on accountability and efficiency in the execution of PFM reforms.
Submit the audited fiscal report of FY2021/22 to IMF staff.	End-December 2022 **Met**	Foster accountability and monitoring.
Notify the FY2022/23Q3 quarter allotment to the pilot MDAs that is in line with the macroeconomic framework and allow MDAs to commit up to this amount through IFMIS.	End-December 2022 **Met**	Demonstrate capacity to monitor and control commitments.
Publish the quarterly audited IFMIS-generated comprehensive monthly fiscal reports.	Continuous, starting in FY2023/24 **This SB was replaced with the next SB for the second review.**	Foster fiscal transparency and monitoring. Improve the in-year comprehensive monthly fiscal reports.
Publish the monthly IFMIS-generated comprehensive fiscal reports	Continuous, starting FY2023/24 **Not met; Implemented with a delay; started publishing on October 30.**	Foster fiscal transparency and monitoring. Improve the in-year comprehensive monthly fiscal reports.
Complete verification of arrears of national budget entities from July 1, 2020 to March 31, 2022 certified by the Auditor General, including compensations and utilities.	End-December 2022 **Met**	Foster financial discipline

Table 2. Malawi: Structural Benchmarks Under the Staff Monitored Program (concluded)		
Actions	**Timing / Status**	**Objectives**
Approval by the Cabinet of an arrears clearance and prevention strategy for national budget entities that has been prepared in consultation with staff.	End-February 2023. Not met; staff have provided feedback; added to the SB Table for the ECF arrangement.	Foster financial discipline.
Monetary and Financial Sector Reforms		
Pre-announcement of forex purchases to allow for a period of market-price formation	End-November 2022 **Not met; Replaced to PA**	Deepen the interbank FX market, improve market functioning, efficiency in intermediation with improved liquidity.
Monetary and Financial Sector Reforms		
Prepare, in consultation with Fund staff, and amend the RBM Act as recommended by the 2021 safeguards assessment; and submit amendments to public consultation first then to the Parliament.	End-October 2023 **In progress; Moved to a SB for the ECF arrangement.**	Strengthen RBM governance.
Establish an executive Asset Liability Management Committee (ALCO) in accordance with recommendations of the 2021 Safeguards Assessment Report; and fully operationalize the ALCO.	End-March 2023 **Not Met. Implemented with a delay.**	Strengthen oversight of foreign reserve assets.
Governance		
Follow-up action report on the COVID-19 spending audit report and EDF's audit report. Publish a follow-up report related to the COVID-19 spending audit report, detailing the corrective actions and measures to pursue and respond to audit findings, including the follow-up of alleged misappropriation of funds as well as the coverage of a second audit findings.	End-October 2023 **Moved to a prior action for the ECF arrangement.**	Strengthen governance and data transparency.

containing growth in broad money supply, it has adverse implication on meeting the monetary base targets.

4. **This Memorandum presents the economic and financial policies that the Government will implement under the ECF-supported arrangement.** The Government's overarching objective is to restore macroeconomic stability to build the foundation for sustainable and inclusive growth as envisaged in Malawi 2063. In the near term, BoP pressure is elevated calling for a steadfast implementation of ambitious reform efforts to help improve the lives of the Malawian people.

5. **We are committed to deliver on the objectives and targets agreed to under this ECF-supported program.** To achieve this, we will take the necessary steps to: 1) deliver on the agreed program targets, including through the prior actions; and 2) make tangible and expedited progress on the debt restructuring process to fully restore debt sustainability in line with the parameters that underpinned the ECF request. Our FY2023/24 budget is aligned with the macroeconomic adjustment path required for stabilizing the economy, underpinned by a combination of enhanced domestic revenue mobilization and expenditure rationalization, to reduce the pressure on domestic borrowing and public debt. We are committed to implement the FY2023/24 budget as passed and to submit the FY2024/25 budget in line with the macroeconomic framework. We have also developed a Contingency Plan to address any challenge to the baseline fiscal path. The Reserve Bank of Malawi remains committed to tightening the monetary policy stance to help contain inflationary pressures. We will continue stepping up our efforts to address governance weaknesses and reduce vulnerabilities to corruption, including through enhancing transparency, accountability, and digitization of public financial management (PFM), enhancing autonomy and governance of the RBM, and strengthening of its foreign exchange reserves position and management.

RECENT ECONOMIC DEVELOPMENTS

6. **Malawi's economic recovery remains on course.** Real GDP growth is now projected at 1.6 percent in 2023, from 1.7 percent at the time of the first PMB review, reflecting continued shortages of foreign exchange, and tighter monetary policy, offset somewhat by stronger-than-originally expected tobacco exports. Inflation is now expected to average 30.3 percent in 2023, up from 24.8 percent projected at the time of the first review. The Reserve Bank has taken decisive action by increasing the policy rate by another 200 basis points in July 2023, bringing it to 24 percent, but inflation has remained elevated. Food prices decelerated more slowly during the 2023 harvest season than expected, even as non-food inflation began to slow down.

7. **The Government has undertaken important corrective actions and macroeconomic adjustment is now taking place.** The authorities have demonstrably stepped-up program ownership heading into the second review, proactively engaging with staff and sharing data. Revenue seems to be broadly coming in on target, and expenditure has been contained. Money growth is flattening out relative to a year ago, and foreign exchange is beginning to return to the system.

8. Performance under the Staff Monitored Program has strengthened. End-June Quantitative Targets (QTs) and Indicative Targets (ITs) have largely been met: five out of six end-June and continuous QTs, and all three end-June ITs, were met. Seven out of 10 Structural Benchmarks (SBs) were not met, but some progress has been made. The monetary target was not met because the RBM was not able to mop up sufficient liquidity through open market operations.

9. Fiscal stance is tightening. The fiscal overall balance reached MWK1.5 trillion (11.7 percent of GDP) in FY2022/23. The fiscal outturn so far is on track to contain the overall deficit for FY2023/24 and FY2024/25 at MWK1.8 trillion (a decline to 10.7 percent of GDP and a further decline to 8.1 percent of GDP, respectively).

10. Gross official reserves remain low and pressure on the exchange rate is high. The current account deficit narrowed significantly to 3.2 percent of GDP in 2022 from 14 percent of GDP in 2021 partly due to a large devaluation and import compression. Despite a large reduction in the current account deficit, reserve accumulation was limited, in part due to sizeable external debt service. Foreign exchange market liquidity remains significantly tight, with demand outpacing supply and limited foreign exchange prioritized to support strategic imports. As a result, preliminary data shows that readily available gross international reserves have remained low, at $156.1 million in end-September 2023, only a small accumulation from $120 million at end-2022. The Reserve Bank has restarted purchases of foreign exchange via regular auctions to facilitate price discovery. But despite some depreciation of the official exchange rate, the spread between the US$/Kwacha bureau and the official rate has further widened to over 50 percent, in part reflecting speculative behaviors on the cash FX market.

11. The banking sector is broadly stable, well capitalized but has high exposure to the public sector. The banking sector meets the minimum regulatory requirements for capital adequacy and the liquidity ratios. However, since the Covid-19 pandemic, industry-wide non-performing loans generally remained above the recommended limit of 5.0 percent, and stood at 7.0 percent in July 2023, up from 4.7 percent in July 2022. The high exposure to government securities is being monitored.

12. Risk to food security is high and increased on account of climate-induced shocks and lingering spillovers from the war in Ukraine. Vulnerability to natural disasters has aggravated food insecurity by further depressing food production, and other exported agricultural products which provided sources of foreign exchange to purchase other necessary food imports.
The destruction of crops caused by Cyclone Freddy has added to the already high pressure on food security.

OUTLOOK

13. Growth is expected to recover as the macroeconomic situation stabilizes. The macroeconomic framework envisages growth picking up gradually and inflation slowing, predicated on a return to fiscal sustainability and the completion of the debt restructuring process in the very near future, which would help mobilize much-needed grant financing. Growth is projected to improve to 1.6 percent in 2023, underpinned by gradual macroeconomic stabilization and recovery across sectors, reaching 4.5 percent in the medium-term by incorporating gains from ongoing reforms and investments. The current account deficit is expected to widen this year, to 7.6 percent, with imports still artificially compressed due to a lack of FX availability, before settling around 7.4 percent in the medium term.

14. Acknowledging substantial risks and the urgency of reforms, we are committed to implement bold macroeconomic adjustment and reforms outlined in this MEFP to lead the Malawian economy to a favorable medium-term outlook. We will take the necessary steps as part of the ECF-supported arrangement to help anchor our macroeconomic policies to address macroeconomic sustainability. In this regard, we will implement bold policies and reforms, accompanied by strategies to restore debt sustainability. Furthermore, we will continue to advance structural reforms to support sustainable and inclusive growth and restore debt sustainability, with a view to improve lives of the Malawian people.

15. We are cognizant that in the short term, the impact of economic adjustment will be difficult, but this is necessary to address the current situation and set the foundation for sustainable and inclusive growth.

- We expect that growth will recover from 0.8 percent in 2022 to 1.6 percent in 2023 as confidence in our policies and economic stability is restored. Specifically, we will pursue prudent fiscal policies and ensure that non-concessional external financing will be replaced by grants, other non-debt creating flows and adjustments under the proposed reform program. Medium-term growth is projected to settle around 4.6 percent, supported by greater macroeconomic stability and implementation of structural reforms.

- Average year-on-year inflation is expected at 30.3 percent in 2023 and projected to decline thereafter towards about 6.5 percent in the medium term, supported by well anchored monetary and fiscal policy stance, taking into account the movements of the currency and passthrough to inflation as the RBM builds up foreign reserves and winds down currency swap operations.

- We will aim to accumulate gross reserves to reach $394 million by December 2023. Gross reserves are projected to recover to over 4 months of imports in the medium term. With external and fiscal policy adjustments, current account deficits are projected to stabilize over time. The reserve accumulation path assumes that the external financing gap will be filled with non-debt creating flows, either debt relief or grants, and concessional loans.

16. Risks to the outlook are significant. Without sufficient external buffers, BOP pressures may further intensify. Further weather-related shocks could also disrupt economic activity. In addition, the war in Ukraine could compound risks to the outlook due to supply chain disruptions and the surge in fuel, food and fertilizer prices resulting in additional financing needs and increasing risks to food security.

ECONOMIC AND FINANCIAL POLICIES FOR THE PROGRAM PERIOD

17. Economic and financial policies for the program period will be anchored by the Malawi 2063 and its First 10 Year Implementation Plan (MIP-1). Our program objectives include, (i) restoring macroeconomic stability, (ii) enhancing fiscal discipline, (iii) maintaining price stability and financial soundness, (iv) rebuilding external buffers, (v) restoring debt sustainability and closing the financing gap, and (vi) addressing weaknesses in governance. The remainder of this MEFP outlines in detail the specific policies we have adopted or intend to adopt to achieve our program goals.

A. Fiscal Policy

18. Our fiscal policy stance will aim to regain fiscal discipline and restore macroeconomic stability. This will be supported by measures to enhance revenue collection, manage expenditures and improve transparency and monitoring of budget execution.

19. The FY2023/24 budget and the draft FY2024/25 in preparation are in line with the program macroeconomic framework. The budget aligns spending to revenue projections so that net domestic financing is contained. The budget is anchored on a realistic revenue estimate and a rationalization of expenditure, while protecting essential spending, to achieve a fiscal adjustment of about 1.9 percentage points (ppt) of GDP in FY2023/24. The envisaged reduction of the domestic primary deficit is 0.8 ppt of GDP in FY2023/24. Preliminary data suggest that our domestic primary fiscal balance is roughly on track to contain the overall deficit for FY2023/24 and FY2024/25 at MWK1.8 and MWK1.7 trillion (a decline to 11 percent of GDP and a further decline to 8 percent of GDP, respectively). We have developed a Contingency Plan to close the financing gap in case the baseline fiscal path faces implementation challenges (PA).

20. Our fiscal objective is to reach a debt stabilizing primary fiscal balance as soon as possible. The size of the envisaged fiscal adjustment is about 1.7 ppt of GDP per year (in terms of domestic primary balance), or a cumulative of 6.7 ppt over the four years from FY2023/24. Excluding RBM recapitalization, the size of the adjustment would be about 1.3 ppt per year over four years. During FY2023/24, our fiscal consolidation efforts are focused on (i) stepping up implementation of our Domestic Revenue Mobilization Strategy (DRMS) in a timely manner; (ii) rationalizing and prioritizing expenditures; (iii) introducing and implementing sound commitment control measures; and (iv) implementing well targeted measures to support low-income households. Going forward, we are committed to implementing the tax policy and revenue measures already committed under the PMB (Text Table 1).

Text Table 1. Malawi: Fiscal Adjustment, 2023/24–2026/27
(Percent of GDP)

	FY2022/23	FY2023/24		FY2024/25	FY2025/26	FY2026/27	Adjustment over the 4 years		
		First Review	Current				Overall	First year	Annual Average
September 2023									
Domestic Revenue	13.3	14.3	14.0	15.8	16.1	15.7	2.4	0.7	0.6
Domestic Primary Expenditure	17.1	17.1	17.0	14.8	13.7	12.8	-4.3	-0.1	-1.1
Overall Balance	-11.7	-10.5	-10.8	-8.1	-7.1	-5.7	5.9	0.9	1.5
Domestic Primary Fiscal balance	-3.8	-2.8	-3.0	1.0	2.4	2.9	6.7	0.8	1.7
Domestic Primary Fiscal Balance excl. RBM Recapitalization	-2.4	-1.1	-0.6	1.2	2.3	3.0	**5.4**	1.8	1.3
Total Size of Measures			**1.9**	**1.6**	**1.5**	**0.9**	**5.9**	1.9	
Revenue Measures			0.5	1.0	1.1	0.6	3.2	0.5	
Tax Policy Measures			0.4	0.9	0.9	0.4	2.6	0.4	
VAT Base Broadening			0.2	0.5	0.5	0.1	1.3	0.2	
Other Tax Measures			0.2	0.4	0.4	0.3	1.3	0.2	
CIT Base Broadening									
PIT Reform									
Excise and Carbon Tax									
Tax Administration Measures			0.1	0.1	0.2	0.2	0.6	0.1	
Expenditure Measures			-1.4	-0.6	-0.4	-0.3	-2.7	-1.4	
Wage Bill			-0.3	-0.3	-0.3	-0.2			
AIP			-0.6	-0.3					
General Goods and Services			-0.5	-0.2	-0.1	-0.1			
Social Protection				0.2					

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

21. We announce quarterly allotments aligned with the macro-framework and the outturns for revenue, grants and expenditure and allow Ministries, Departments and Agencies (MDAs) to commit up to this amount through IFMIS. MDA payments are limited to monthly cash releases, aligned with allotments, to demonstrate our commitment to stronger expenditure control reforms, reducing the risk of accumulating new payment arrears. The extension of this practice to all MDAs was done through announcement in the FY2023-24 Budget Policy Statement and is now being executed. We are committed to improve information set and toolkits as well as communication channels to MDAs so that decisions on quarterly allotments are aligned with MDAs' intended timing of purchase / expense orders and projected availability of resources and funding needs. We will also define calendar for issuing allotments and funding releases to institutionalize the new allotment process.

22. Our revenue mobilization efforts will be driven by the timely implementation of revenue measures announced in the DRMS and FY2022/23 and FY2023/24 Budget Policy Statements. We launched the DRMS in December 2021 with the objective to increase revenue by 5 percent of GDP in the five years of implementation. To step up implementation, we have incorporated the DRMS in Malawi Revenue Authority's (MRA) strategic plan and formulated a DRMS Monitoring Committee comprising MoFEA, MRA, Accountant General, Immigration Department, Malawi Police Service and Registrar General in FY2022/23. We are committed to ensure timely reporting to the Committee and holding regular meetings of the Committee to review the report to enhance efficiency and the effectiveness of the implementation of the DRMS. The following measures are being implemented as part of the DRMS:

- **Advance income tax:** we introduced the advance income tax (AIT) in May 2022 at the rate of 3 percent on commercial imports, raising additional revenue amounting to MWK6 billion. In FY2023/24, we increased the AIT rate to 10 percent, and extended it to non-compliant exporters without a tax clearance certificate.

- **Electronic tax stamps:** we are in the process of introducing the requirement for affixing or printing of electronic tax stamps on alcohol (spirits, whiskey, malt beer, opaque beer), energy drinks, flavored water, carbonated soft drinks, opaque non-alcoholic drinks and cigarettes. We expect this to be operational in FY2024/25.

- **New stamp duties:** new stamp duties will apply to various instruments, including motor vehicles, in FY2023/24. We introduced an electronic stamp duty system in 2023 and extended the regime to include various instruments, including motor vehicles, transfer of property and shares.

- **Taxes for small businesses**: we have introduced presumptive tax for small businesses whose annual turnover is less than MWK12.5 million. To ensure that the presumptive tax system is effective, we are rolling out the Block Management System (BMS) in all commercial centers. We have rolled out the system in Blantyre, Mzuzu, Limbe and Lilongwe. We plan to roll out the system to all major cities by December 2024.

- **Tax Incentives**: the FY2022/23 budget announced establishment of Special Economic Zones, to help catalyze the much-needed foreign investment in Malawi. As far as tax incentives are concerned, we are reviewing the system with a view to streamline the incentives. The recommendations of the report will be incorporated in the new Taxation Act, Value Added Tax Act, and Customs and Excise Act that are currently under review, and will be submitted to the Parliament with the FY2024/25 budget. We will ensure that streamlining tax incentives will not contradict SBs committed under the program.

- **Bank Supernormal Profits Tax** we introduced an additional income tax of 10 percent for bank profits above MWK10 billion. Thus, bank profits below MWK10 billion will continue to be taxed at 30 percent, while profits above MWK10 billion will be taxed at 40 percent. This is a temporary measure that will be reviewed in the next fiscal year.

- **Value Added Tax:**

  - We have introduced standard rate VAT on the following products: exercise books with hard covers; rye flour; other cereal flour; groats and meal of wheat, groats and meal of other cereals; rolled or flaked grains of oats or other cereals; other worked grains of oats or other cereal; cereal, germ, whole rolled flaked or ground; roasted malt; and malt roasted of barley, oats, rye, sorghum or millets. We will repeal the VAT relief for current and former politicians, senior public officials, judges and other similar privileged individuals and groups (SB), and ensure that every supply of motor vehicle is standard rated for VAT purposes (SB).

We will eliminate VAT exemptions and zero-rating for business inputs (SB) and repeal the VAT relief for building materials by July 2024 (SB).

- In addition, the rolling out of the VAT module in the Msonkho Online, our Integrated Tax Administration System (ITAS), has enhanced business intelligence sharing and data analysis which has led to the identification of i) discrepancies between Output VAT on filed tax returns by suppliers against Input VAT by buyers which exaggerates the VAT refunds, ii) non-reporting of Output VAT sales in the Msonkho Online in order to suppress VAT revenue to the government, iii) non-registered taxpayers charging VAT thereby making fraudulent VAT claims and iv) re-assessment of corporate income tax and overall VAT refunds. The MRA is engaging the concerned taxpayers to address these anomalies and consequently reclaiming the illegitimate VAT refunds and collecting the evaded tax revenue.

- **Increase the withholding tax on contractors from 3 percent to 10 percent:** as one way of increasing tax compliance in the construction industry, we have increased the withholding tax rate for the industry from 3% to 10%.

- **Collect rental income tax from residential houses:** realizing that there are more Malawians who have several residential rental houses but are not paying taxes, we have embarked on a project to register all houses in cities and towns and start enforcing the payment of rental income tax.

23. To strengthen tax administration, we launched Msonkho online, our Integrated Tax Administration System, in December 2022. Currently, not all modules that are used by taxpayers such as registration, payment of taxes and filing of tax returns, are operational. We plan to operationalize the outstanding modules by end-March 2024 (SB). We will implement the Tax Administration Act and establish the Revenue Appeal Tribunal by December 2023. We will publish MRA's corporate strategic plan and annual reports to enhance transparency.

24. To improve non-tax revenues, we have implemented measures, including ensuring that SOEs comply with the PFM Act by opening a holding account with the RBM; ensuring that MDAs remit non-tax revenue collection to MG1 account through their departmental receipts' accounts, and increasing some fees and charges to ensure that they reflect, where possible, full cost recovery. More increases to fees and charges are planned, as well as additional measures, including automating the payment systems and business processes of the MDAs; and enforcing the dividend and surplus policy.

25. The government continues to improve the national payment system by enabling the interoperability across bank payment channels such as Point of Sales (POSs), debit and credit cards, customer accounts, and mobile network operators' wallets through a national switch. This switch will be the backbone of the national electronic payments (e-payments) gateway. An international firm that developed the switch has been re-engaged to provide an e-payments solution for the gateway and is currently working on the operationalization of technical and functional specifications for the installation of the required infrastructure and software. The E- government department is ensuring that the systems of the major non-tax revenue MDAs are technology-ready to be connected when the gateway rolls out in March 2024. Among other benefits, financial transactions will be centralized, enhancing efficiency and transparency in government revenue collection, accountability and reconciliation. Digitization of payments will reduce revenue leakages, resulting in improvement of non-tax revenue contribution to the overall domestic revenue.

26. Expenditure prioritization is more critical than ever given the need to support the vulnerable and invest in infrastructure. We will endeavor to improve efficiency of public spending and to reduce non-critical spending.

- **Continue to rationalize the Affordable Input Program (AIP).** We have implemented the first phase of reform to the fertilizer and seed subsidy program, AIP by having a National Integrated Social Safety Net Program using the Unified Beneficiary Register to reduce duplication of access hence bringing in efficiency in beneficiary targeting. We have taken necessary measures to prevent cost overrun in the AIP from escalating fertilizer prices and Kwacha depreciation including through increment to farmer contribution while capping the Government Subsidy and fast-tracking beneficiary reform. We are committed to implementing our plan to phase out the AIP. Furthermore, we have moved farmers at the lowest end of the income spectrum to social protection programs and those at the higher end of the spectrum to commercial agriculture programs, supported by development partners.

- **Rationalize the wage bill.** The Personnel Audit was carried out in 2021, which provided a number of recommendations, and the Government of Malawi is committed to manage its wage bill by flushing out ghost workers, freezing on new hiring into the public service, except in critical areas such as health and education sectors, strengthening approval processes to payroll and pension changes within the existing Human Resource Management Information System (HRMIS).

- **To safeguard social protection and to protect the vulnerable, we have established a floor on social spending as an indicative target (IT) under the program.** This will comprise of Government contribution to health and basic and secondary education spending, as well as a number of social safety net spending, including the Social Cash Transfer Program (SCTP) and AIP.

27. We have stepped up measures to enhance the oversight of State-Owned Enterprises (SOEs). Weak oversight and financial reporting are a challenge to adequate monitoring and management of risks to the budget and public debt from the SOEs. In this regard, we will keep close track of government guaranteed debt of SOEs. We have undertaken detailed reporting to the Parliament for FY2021/22 for high-risk SOEs, including Blantyre Water Board, ESCOM, ADMARC, NOCMA and EGENCO. On a quarterly basis, we will monitor the management accounts of the relevant SOEs. In compliance with the new PFM Act, we will continue to prepare an annual consolidated report of all SOEs.

28. Implementation of the new IFMIS, institutionalizing reporting and controls are key for execution of the budget and commitment control. We will exploit the new IFMIS, which started in July 2021, to build upon recent progress and enable future Public Finance Management (PFM) reforms, including the interim Electronic Funds Transfer (EFT) for government payments, to improve our budget preparation, cash management, commitment control, banking arrangements, accountability, and payment efficiency. As of end-August 2023, all MDAs but two are included in IFMIS (PA). The success of the fiscal adjustment program relies heavily on comprehensive and timely reporting, and sound commitment controls. Our measures are as follows:

- **Domestic Arrears:** We have completed the verification of arrears of the national budget entities from 1st July 2017 to 30th March, 2022. We are in discussion with the Auditor General on the stock of the unverified arrears to agree on how these will be treated and in addition, on the stock of arrears that have been inspected but not verified. We are committed to implementing our Arrears Clearance and Prevention Strategy, which will be submitted to Cabinet by end-December 2023 and approved by end-March 2024 (SB).

  We are committed to settle the arrears within the limits of the fiscal framework and available resources. We have started clearing the stock of arrears by paying amounts below MWK100 million through the regular budget and issuing zero coupon promissory notes for amounts above MWK100 million. In order to improve our institutional framework for managing arrears, we will: i) assign the responsibility of monitoring in-year overdue payments to the Accountant General Department; ii) ensure that expenditures are properly accounted for and converted into debt when issuing promissory notes to settle large payment arrears; iii) develop and maintain an up-to-date database on arrears by December 2023; and iv) establish by March 2024 a Guiding Framework for issuance of promissory notes, with limits within the budgetary framework and reporting requirements. We are committed to avoid further accumulation of arrears through implementation of quarterly allotment, enhancement of commitment controls and implementation of contract management module within IFMIS. To curb arrears on utilities we are promoting the installation of prepaid meters for all MDAs and rehabilitating water reticulations systems in key public institutions to reduce water wastage.

- **Contract Management module of IFMIS-** starting mid November 2022, we implemented quarterly commitment limits (backed by monthly payment fundings) and rolled out the IFMIS contract management module starting with two MDAs, including the Ministries of Health and Transport. We will increase the pilot MDAs by 10 in January 2024 and keep increasing the MDAs in phases as we get in FY2024/25. We will finalize the roll out to the remaining MDAs by end-FY2024/25. Applying the lessons learned from the pilot exercise and rolling out these functions to all MDAs will form our cornerstones for firm commitment control and management of multi-annual contracts. Implementation will include i) capturing all existing contracts/commitments in IFMIS, ii) issuance of quarterly spending limits and monthly payment funding, iii) requiring all financial transactions to be entered through IFMIS at the commitment (contract signing/purchase order issuance) stage.

- **Expand the coverage of transactions recorded in IFMIS** to include items that in the past have transacted outside of IFMIS from April, 2023, including actuals of all revenue, domestic debt issuance receipts and all debt servicing payments, transfers to local councils, non IFMIS MDAs, and advances to embassies. We will instruct MDAs to capture in IFMIS, project expenditure financed by development partners (Development Part 1) and will agree on appropriate codes for MRA tax refunds and banking arrangements for budget support grants and loans. To achieve full institutional coverage of the national budget for FY24-25, we will configure, test, and accept by March 2024 the solution for the Malawi Defence Force (MDF) and State Residences to transact in SAP-IFMIS. We will also complete the rollout of the revenue module to all major revenue collecting agencies. We envisage rolling out the functionalities to all MDAs during the course of FY2024/25. These include the revenue, project systems, asset management and recognition, and contract management modules.

- **Bank account reconciliation:** We have reviewed the bank account structure used for public debt to ensure compliance with the new PFM Act, facilitate the recording of transactions and prevent payments through unfunded bank accounts. We will step up our efforts to reconcile within IFMIS the MG1 bank statement by finalizing the configuration and supply of electronic bank statements in the specified format, with the support of IMF TA. By end-FY2023/24, we will: i) upload to IFMIS all MG1 payments and receipts that were transacted outside IFMIS since July 2021; ii) develop suitable business processes and banking arrangements to prevent future direct deposits to or payments from MG1; iii) establish reconciliation of current transactions while reducing the SAP-IFMIS backlog and accounting for the balance migrated from the EPICOR-IFMIS. To ensure successful delivery of this the RBM is also being requested to furnish the electronic bank statement to MoFEA by 31st October 2023.

- **Enhance commitment controls:** since July 2023, all but two MDAs are operating under our new framework for commitment controls. To better manage commitments and cash-flows, we will provide detailed guidance and deliver trainings to MDAs on the new framework, and capture information in their procurement plans to inform quarterly allotments. By end-FY2023/24, we will establish direct lines of contact with key MDAs to receive information on their near-term cash needs to better inform cash flow forecasts. We are drafting our new Treasury Instructions and will include provisions to institutionalize the new budget execution process, thereby strengthening our commitment controls framework. We will also closely monitor the implementation of the framework through regular reports to ensure that commitments are aligned to available resources.

- **Cash management and debt issuance:** to strengthen our cash management and debt issuance, we will strictly adhere to the budget execution process stipulated in the flow chart shown in the MEFP at the time of PMB approval in November 2022.

- **Electronic Funds Transfer (EFT):** Expenditure continues to be exclusively done through EFT for government payments across all MDAs. The Government will cease to act as a participating bank in the interbank payment system in Automatic Transfer System (ATS) when the RBM's Flexcube upgrade will be finalized by 31st March 2024.

- **Consolidated fiscal reports**: We are expanding the IFMIS coverage to include all national government cash inflows and outflows, including all MG1 and public debt issuance and servicing transactions, and we are working to record all missing data from July 2021 to now by March 2024. Auto-reconciliation of government's bank statements has started, enabling us to commence compiling IFMIS-generated monthly fiscal reports. So far, we have compiled the domestic budget execution data for FY2023/24. Going forward, we will continue to improve the in-year comprehensive monthly fiscal reports. We will start publishing the unaudited IFMIS-generated comprehensive fiscal reports on the MOFEA website starting in FY2023/24 (the "Dashboard" Text Tables 2 and 3) to enhance transparency and accountability of the budget execution (SB). From FY2024/25, these reports will be backed by reconciled bank statements submitted within three weeks from the end of each month. We will improve the recording of capital expenditure by closing data gaps regarding project expenditures financed by development partners.

- **PFM Act:** We passed the new PFM Act in March 2022 to align the legal framework with ongoing PFM reforms. We are drafting the Regulations and Treasury Instructions to support the implementation of the new Act. Prior to their promulgation, we have shared the drafts with the IMF and other development partners inviting feedback. The Regulations and Treasury Instructions will be finalized by October 2023 and June 2024, respectively.

Text Table 2. Malawi: Fiscal Dashboard, Expenditure Breakdown by Code

(In billions of MWK, YTD as of September 30, 2023)

Code	Description	Appropriation (FY 23/24 Budget)	Quarterly Allotment[3/]	IFMIS Commitments	IFMIS Outturns[1/]
	Revenue	**2554**	**1275**		**1377**
	Tax Revenue	2128	987		992
	Grants	312	211		244
	Other Revenue	114	77		141
	Total Expenditure	**3779**	**1974**	**1680**	**1584**
21	Compensation of Employees	917	456	450	448
22	Use of Goods & Services	548	344	382	348
24	Interest	915	400	414	414
26	Grants	303	132	191	179
27	Social Benefits	249	141	177	140
28	Other Expense	16	16	9	8
31	Non Financial Assets	831	486	56	47
	Overall Balance	**-1225**	**-699**		**-208**
	Domestic Financing[2/]	1103	411		243
	Net Borrowing from Reserve Bank				238
	Net Borrowing from Commercial Banks				-17
	Net Borrowing from Non-Bank Sector				22
	Unreconciled Financing	121	288		-36

[1/] Revenue outturns are taken from Quarterly Fiscal Tables, data are through Q2 2023

[2/] Domestic Financing outturns are taken from change in net domestic borrowing at cost value relative to start of fiscal year.

[3/] Quarterly allotments are the sum of Q1 2023 and Q2 2023 Allotments

Text Table 3. Malawi: Fiscal Dashboard, Expenditure Breakdown by Vote

(In billions of MWK, YTD as of September 30, 2023)

Code	Description	IFMIS Budget	IFMIS Commitments (Quarterly Allotments)	IFMIS Outturns
	Total Expenditure	**3341**	**1680**	**1584**
010	The Presidency	0	0	0
020	Miscellaneous & Other Statutor	33	24	21
030	Pension & Gratuities	163	116	102
040	Public Debt Charges	915	414	414
050	State Residences	16	12	12
060	National Audit Office	2	2	1
070	The Judiciary	19	15	15
080-082	National Assembly and Related Offices	36	21	18
090-097	Office of the President and Related Offices	242	19	17
100-101	Ministry of Defense and Malawi Defense Force	155	104	103
120-121	Ministry of Local Government and Local Gov. Finance	359	87	72
130	Ministry of Lands	33	24	24
180	Ministry of Youth and Sports	8	5	5
190	Ministry of Agriculture	285	150	120
210	Ministry of Irrigation and Water Development	7	5	5
240	Office of the Vice President	1	2	2
250	Ministry of Education, Science, and Technology	171	70	68
260	Ministry of Foreign Affairs	38	21	21
270-279	Ministry of Finance and Related Offices	230	122	117
310	Ministry of Health	191	73	66
320	Ministry of Gender, Children, Disability, and Social Welfare	9	4	4
330	Ministry of Information	8	8	7
340-344	Ministry of Homeland Security and Related Offices	195	92	86
350-354	Ministry of Justice and Related Offices	6	3	3
360	Ministry of Tourism, Wildlife & Culture	2	3	3
370	Ministry of Labour	9	4	4
390	Ministry of Trade and Industry	5	3	2
400	Ministry of Transport & Public Work	31	14	13
430	Malawi Human Rights Commission	1	1	1
460	Malawi Electoral Commission	48	35	28
470	Ministry of Forestry & Natural Resources	9	6	6
480	Ministry of Mining	3	2	1
490	Ministry of Energy	9	6	1
510	Anti Corruption Bureau	7	4	3
520	Legal Aid Bureau	2	1	1
550	Office of the Ombusdsman	1	1	1
560	Law Commission	1	0	0
601-928	District Councils	89	209	215
	Miscellaneous Categories	0	0	1

B. Maintaining Price Stability and Financial Soundness

29. Monetary policy will be tightened forcefully and proactively as needed to contain inflationary pressures. Our monetary program will remain anchored on containing reserve money growth. Our measures will include:

- Maintaining a tight monetary policy stance by setting the monetary policy rate to ensure positive real interest rates to tame inflation.

- Containing the RBM's net claims on Government in line with program targets, through greater use of repurchase agreements for Open Market Operations (OMOs) and the introduction of less favorable terms for the RBM's rediscounting facility.

- Strengthening the RBM's capacity to manage excess liquidity, including through changes in reserve requirements, the sale of securities, and the use of OMOs.

30. Financial sector stability will continue to be safeguarded. The further increase in the exposure of the banking sector to the public sector and hikes in the interest rates may pose potential risks to the stability of the financial sector. We will therefore remain vigilant to these risks and continue to strengthen financial sector oversight. To promote financial stability, we will continue to:

- Monitor the banking system's exposure to the government through securities, and

- Reassess loan and collateral quality needs of commercial banks.

C. Rebuilding External Buffers

31. Our external policies will support a continued rebuild of our foreign exchange reserves, alongside policy actions to facilitate a market-determined exchange rate. In June 2023, the RBM restarted purchases of foreign exchange via monthly auction to encourage price discovery. We will be taking actions to ease these pressures and allow for a durable rebuild of our external buffers. To achieve these objectives, we will take the following actions:

- We will allow for a greater flexibility in the exchange rate to substantially reduce foreign exchange shortages.

- We will increase the effectiveness and transparency of the FX operations going forward (PA).

- We will continue to rebuild our foreign exchange reserves to a level that would provide adequate insurance against external shocks. This will be achieved by implementing the agreed path of reserves accumulation to reach at least 3.9 months of import cover in the medium term. The RBM will purchase foreign exchange as necessary to deliver this path, while at the same time limiting its sales of foreign exchange and thus becoming, on average, a net purchaser. Moreover, we will monitor short-term foreign currency drains to ensure our external buffers are sustainably maintained.

- We will monitor and mitigate FX swap rollover risks and continue to lower our swap costs by winding down FX swaps with non-residents—in accordance with our plan to reduce the open swap position in the medium term.

- We will ensure that coordination between the government and the RBM will support our external sector policy goals. In particular, the government's adherence to the agreed fiscal program will support a well-functioning FX market and allow importers and exporters to plan with greater certainty.

- We are carrying on with efforts to enhance foreign exchange earnings through promotion of the Agriculture, Tourism and Mining (ATM) sectors, in line with the MIP-1. In agriculture, the Government is concentrating on operationalization of mega-farms to increase exports and promote import substitution. The Government is also promoting infrastructure related to tourism growth and has also stepped up our tourism marketing to attract more international tourists. Furthermore, we will continue exploring the opportunities in the mining sector and accelerating the process of concluding Mining Development Agreements.

- We are also implementing measures to contain demand for fuel and motor vehicle imports. For example, we will gazette the specific tax regime on secondhand motor vehicles (PA), will repeal preferential treatment for motor vehicles and VAT relief for privileged individuals and groups (SB), and reinforced the implementation of the automatic price adjustment mechanism that aligns local fuel prices to international fuel prices. Some other measures such as (i) raising import duty and excise tax on motor vehicles to raise the price of motor vehicles to (at least) the regional average and (ii) raising fuel taxes will be implemented as soon as possible but no later than the passage of the FY2024/25 budget.

32. We maintain four multiple currency practices (MCP) and three exchange restrictions subject to approval under Article VIII. We request approval for these measures as they are temporary and maintained mostly for balance of payments reasons. They are nondiscriminatory and do not give us an unfair competitive advantage. We are committed to eliminating these measures during this ECF-supported program as soon as our balance of payments conditions permit (SB). Our efforts to eliminate our balance of payments problems and strengthen our tax administration system will facilitate the elimination of these measures. We will not impose or intensify existing restrictions on payments and transfers for current international transactions or adopt new or modify MCPs.

D. Restoring Debt Sustainability and Closing the Financing Gap

33. Malawi's overall and external public debt is assessed to be in debt distress. This mainly reflects legacy debts that we inherited, driven by unsustainable fiscal and external policies. Restoring public debt sustainability is our top priority to support macroeconomic stability and to lay the foundation for sustainable and inclusive growth.

34. Our policies will focus on restoring debt sustainability by concluding the restructuring of our external debt, containing new borrowing, and improving debt management. We have developed a debt restructuring strategy which serves as our cornerstone for restoring debt sustainability. Our debt strategy is designed to achieve debt sustainability and to close the financing gaps. The strategy relies on the following pillars to overcome current external debt challenges, including solvency and liquidity concerns:

- Bringing external public debt back to a moderate risk of debt distress in the medium term through a combination of policy adjustment and the necessary debt treatment. The debt strategy targets all external DSA solvency and liquidity ratios to cross their respective thresholds under the baseline in the next five years. This means (i) the baseline of the present value of debt-to-GDP ratio to reach below 30%, (ii) the present value of debt-to-exports ratio below 140%, (iii) the external debt service-to-exports ratio below 10%, and (iv) the external debt-to-revenue ratio below 14% in the medium-term.

- We have followed best practices in sovereign debt restructuring, including taking into consideration inter-creditor equity and comparability of treatment of all official bilateral creditors. We have engaged with private creditors in good faith, by engaging in an early dialogue with creditors, sharing relevant information with all creditors on a timely basis and providing creditors with an early opportunity to give input on the design of restructuring strategies. We are committed to continue working with all creditors to achieve a debt treatment consistent with program parameters and recognizing that servicing debt on the original terms would not be consistent with debt sustainability.

- We are seeking from the largest bilateral creditors, China and India, specific and credible assurances that are in line with program parameters. We will continue working with all creditors with a goal to achieve a suitable debt treatment consistent with program parameters and commit to resolving debt to all official bilateral creditors on comparable terms.

- Mobilization of non-debt creating flows to ensure the external and fiscal financing gaps are closed over the medium term, including through the debt treatment and the mobilization of external grant support from development partners.

35. We continue to pursue good faith negotiations with commercial and official bilateral creditors and are in arrears on commercial debt while these discussions continue. We commit that our commercial debt will be repaid or restructured only on terms that are consistent with the parameters of the ECF-supported arrangement. While we continue our best efforts to successfully complete our restructuring negotiations, we have provided IMF staff with a timeline along which we intend to complete the restructuring process and which will form part of the assessment at the next financing assurances review. We understand that as long as arrears are outstanding, an approval of this arrangement and each Fund disbursement under this arrangement is subject to a financing assurances review in which the Board considers, inter alia, whether adequate safeguards remain in place for further use of Fund's resources and whether Malawi's adjustment efforts are undermined by developments in creditor-debtor relations.

36. We are committed to pursue public finances consistent with debt sustainability and implement measures to strengthen debt management, monitoring recording and reporting. To ensure our debt remains on a sustainable path, we will implement measures articulated below:

- To enhance public debt management, we have updated and published our Medium-Term Debt Strategy (MTDS) to take into account on-budget externally and domestically financed projects either contracted or expected as reflected in the macro-fiscal framework. The MTDS also reflects the ceiling on new non-concessional external debt, contracted or guaranteed, that applies to Malawi as required by the Fund's Debt Limit Policy.

- We will adopt best practices in terms of data reporting and transparency, as well as fulfil our reporting duty to the Fund during the Staff's program review or upon request. In particular, we reiterate our commitment to continue to integrate public debt data into IFMIS. To further enhance transparency around Malawi's debt data, we are continuing to publish regular reports on outstanding debt figures on our official websites. Finally, we are dedicated to building capacity around debt management and financing, and to seeking technical assistance from the IMF and other partners.

- To further support debt sustainability, we will undertake a fiscal adjustment while limiting the impact on economic growth and protecting vulnerable populations through our revenue mobilization efforts.

- Finally, to rebuild our external buffers over the medium term and improve liquidity, we will continue to implement our National Export Strategy. In addition, we aim to reduce Malawi's dependance on agricultural exports, thereby building resilience to climate shocks while supporting economic growth over the medium term.

E. Tackling Governance Challenges Structural Reforms

37. Fiscal transparency, strengthening RBM's autonomy, governance arrangements, and reserve management remain the cornerstones of our program. In this regard:

- We will continue to develop and refine timely, accurate and reliable fiscal data, and make it readily available to the public on the MoFEA website.

- The RBM Board established an Asset Liability Management Committee (ALCO) in accordance with recommendations of the 2021 Safeguards Assessment Report.

- We have developed a revised framework for management of foreign reserves in accordance with recommendations of the 2021 Safeguards Assessment Report and shall ensure its endorsement by the Board.

- Discussions with Fund staff on the prepared draft amendments to the RBM Act are in progress. Once finalized, we will submit the amendments to parliament as recommended in the 2021 Safeguards Assessment Report (SB).

- To strengthen accuracy of RBM's program monitoring data, we (i) instituted a policy to have our external auditors verify NIR data within 10 weeks after each test date and will ensure timely submission of the audited NIR results; and (ii) will continue to submit monetary data through standard reporting forms to the Fund on a regular basis.

38. The misappropriation of COVID-19 public funds is a stark reminder of the urgent need to address longstanding governance weaknesses. We will publish a follow-up report related to the COVID-19 spending audit report, detailing the corrective actions and measures to pursue and respond to audit findings, including the follow-up of alleged misappropriation of funds as well as the coverage of a second audit findings (PA). To avoid recurrence of the misappropriation of Government resources, all payments across Government MDAs are, since 2021, exclusively being done through Electronic Funds Transfer (EFT). Payment of allowances is linked to employment number and one bank account number. In addition, Government has operationalized the Financial Crimes Court to fast-track prosecution of financial related crimes and removed the requirement by the Anti-Corruption Bureau (ACB) to obtain consent from the Director of Public Prosecution to effect arrests for suspected corruption cases. The PPDA Act is undergoing review to provide for declaration of beneficial ownership in the bidding process and to address the anti-competitive practices by bidders in the procurement process. The review will provide for a requirement for Procuring and Disposal Entities (PDEs) to scrutinize highly priced bids in relation to indicative prices of the PPDA. In addition, the ACB has signed Memorandum of Understanding with selected MDAs to facilitate data and information sharing for combating corruption. ACB is enhancing anti-corruption initiatives by setting up of satellite offices. It further intends to undertake lifestyle audit and is formulating Whistle Blowers Protection Bill.

39. Governance weaknesses at the Export Development Fund (EDF) pose a risk to the government in terms of contingent liabilities. EDF is a wholly owned subsidiary of RBM but the Government is working on modalities to merge EDF with Malawi Agricultural and Industrial Investment Corporation, PLC (MAIIC) (SB). We will publish a follow-up action report on EDF's audit recommendations. We closed the Commodity Market Making Unit which was one of the key sources of the credit losses (SB). We strengthened deal origination by decoupling origination from credit risk assessment, established a peer review committee, and introduced a fully-fledged treasury function to ensure effective and efficient liquidity management. We also established an enterprise-wide risk management function, including the recruitment of an expert to mitigate operations risks that may result in the Fund being defrauded of financial resources. We strengthened the governance and risk management framework by developing various policies and procedures including Liquidity and Funds Management Policy, Counterparty Guidelines, Risk Management Policy, Risk Appetite Policy, Pricing Guidelines, and Environmental and Social Policy. We expanded the Board, diversifying its skillset and established various working internal committees. We introduced a balanced scorecard system to strengthen accountability and alignment of every function towards the delivery of the Funds strategic objectives.

40. We have renewed our commitment that public procurement is conducted transparently and in full accordance with proper procedures and the PFM Act. We will continue maintaining a repository of contracts and will make available to Fund staff a full repository of contracts that would give rise to actual or contingent external debt liabilities of the government and the RBM. We are committed to following the appropriate public procurement procedures and adhering to the limits on contracting and guaranteeing nonconcessional and concessional external debt set forth in the ECF-supported program. We have requested a governance diagnostic technical assistance from Fund staff to identify any weaknesses in regulation, legislation, and compliance. We will undergo the diagnostic over the next 9-12 months, will follow up on the recommendations (SB).

41. Broader governance agenda. Mindful of the obvious fact that corruption harms society, undermines national economic development, and threatens democracy, the Government adopted a strategy to combat corruption. His Excellency President Lazarus McCarthy Chakwera, from the outset of his administration, set out the 'golden thread of conditions' with the objective to ensure that the Malawi economy is put on a path to economic recovery and strives. Among the conditions, the rule of law, the presence of law enforcement institutions, and the absence of corruption stood out. The Government's strategic response to corruption includes four components used to combat serious and organized crime. These include: (a) prosecuting and disrupting people engaged in corruption (Pursue); (b) preventing people from engaging in corruption (Prevent); (c) increasing protection against corruption (Protect); and (d) reducing the impact of corruption where it takes place (Prepare). The plan will be reviewed on a regular basis, as part of the Government's commitment to open partnership with all key stakeholders in combating the scourge. To facilitate implementation of the strategy, the Office of the Director of Public Asset Declarations (ODPOD) will digitize asset declarations for easy access and transparency. This will include the establishment of an interface system between ODPOD and Anti-Corruption Bureau (ACB) to facilitate lifestyle audits by September 2023. We will strengthen collaboration among the Financial Intelligence Agency (FIA), the Director of Public Prosecutions (Asset Forfeiture Unit) and ACB in tracing assets belonging to suspects for freezing and subsequent confiscation by September 2023.

F. Enhancing Transparency and Accountability of Strategic Imports

42. The Government will ensure publication of strategic imports data on a timely manner. More specifically, the National Statistics Office (NSO) will be empowered by the Ministry of Finance and Economic Affairs to work closely with all institutions that collect data on fuel (such as MERA), fertilizers for the AIP (Ministry of Agriculture), and pharmaceuticals (Central Medical Store Trust) to ensure that monthly Trade Bulletin provides reconciled data on imports of these strategic commodities. Furthermore, the NSO will be reflecting the data of these strategic commodities on separate line within their monthly Trade Bulletin for close monitoring purposes (SB).

PROGRAM MONITORING, PRIOR ACTIONS AND STRUCTURAL BENCHMARKS UNDER THE ECF

43. The macroeconomic policies under the ECF-supported arrangement will be complemented by a strong structural program, which will increase the efficiency and effectiveness of our economic policies. The performance criteria (PCs) and indicative targets (ITs) under the ECF-supported arrangement are outlined in Table 3. The Prior Actions (Table 4) signal our commitment to a strong reform agenda, while the Structural Benchmarks (Table 5) will anchor our structural reform agenda during the course of the program.

Table 3. Malawi: Performance Criteria and Indicative Targets[1] Under the ECF Arrangement, 2023–24

	Target type [2]	2023	2024		
		End-Dec	End-Mar	End-June	End-Sept
		Proposed Targets			
		IT	PC	IT	PC
I. Monetary targets (billions of kwacha)					
Monetary base (ceiling on stock) (upper bound)[3]		958.7	1,010.2	1,023.1	1,060.3
Monetary base (ceiling on stock)[3]	PC	930.8	980.8	993.3	1,029.4
Monetary base (ceiling on stock) (lower bound)[3]		902.9	951.4	963.5	998.5
II. Fiscal targets (billions of kwacha)					
Domestic revenue (floor)[6]	IT	1,621.0	2,223.0	747.0	1,494.0
Domestic primary fiscal balance (floor)[4,6]	PC	-155.7	-94.1	95.5	57.0
RBM financing of central government (ceiling)[6,7]	IT	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0	0	0	0
Social spending (floor)[6,8]	IT	686.7	910.8	290.0	582.8
III. External sector targets (US$ millions, unless otherwise indicated)					
Change in net international reserves of the RBM (floor)[5]	PC	253.0	68.7	183.3	221.8
Accumulation of external payments arrears (ceiling)[6,9]	PC	0	0	0	0
Contracting or guaranteeing of nonconcessional external debt (ceiling)[6,9,10]	PC	0	0	0	0
Contracting or guaranteeing of concessional external debt (ceiling)[6]	IT	70	70	0	0
Memorandum items:					
Program exchange rate (kwacha per US$)					

Source: IMF staff projections.

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

[2] "PC" means Performance Criteria and "IT" means Indicative Target. The PC test date for the 1st Review is end-March 2024. The test dates for the future review will be in end-September 2024. End-December 2023 and end-June 2024 targets are ITs.

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

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

[5] Targets are subject to an adjustor for (i) debt service and fees and (ii) general budget support, as specified in the TMU. Defined as cumulative flow, starting from the beginning of the calendar year.

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

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

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

[9] Evaluated on a continuous basis.

[10] For program purposes, a limited exception on NCB may be allowed only in the exceptional circumstance that it is used to wind down maturing swaps and for debt management operation that improves the overall debt profile.

Table 4. Malawi: Prior Actions Under the ECF Arrangement		
Actions	**Objective**	**Status**
External Sector Reforms		
• RBM to announce, via public circular, changes to its FX operations, to include: (i) increasing the frequency of purchase operations to at least on a fortnightly basis and removing any implicit or explicit constraints on access, allotment or prices submitted; (ii) allowing FX intermediaries to trade at freely negotiated rates with their clients and between themselves; and (iii) if the RBM were to conduct FX sales, sales should be done via auction (in line with the recommendations of "The Review of the Fund's policy on Multiple Currency Practices—Proposals for Reform", paragraph 15).	• To increase transparency, broaden participation and facilitate greater flexibility in the official exchange rate, and to reduce economic distortions and opportunities for corruption.	• Draft received on October 13.
• Submit to IMF staff audits of NIR from end-December 2022, end-March, and end-June 2023.	• Foster transparency and monitoring of foreign exchange reserves. • Improve data quality.	• Draft audit reports received on October 21. • Finalized reports submitted on October 27.
Fiscal Reforms		
• Roll out core functionalities of IFMIS to key MDAs with mandatory use. The core functionalities will include: (i) capturing all existing contracts / commitments in IFMIS, (ii) issuance of quarterly spending limits and monthly payment funding, (iii) requiring all	• Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption.	• **Met**

Table 4. Malawi: Prior Actions Under the ECF Arrangement (concluded)		
Actions	**Objective**	**Status**
Fiscal Reforms		
funding, (iii) requiring all financial transactions to be entered through IFMIS at the commitment.	• Ensure new IFMIS delivers on accountability and efficiency in the execution of PFM reforms.	• **Met**
• Prepare a contingency plan to close the financing gap in case the baseline fiscal path faces implementation challenges.	• Minimize fiscal risks associated with shortages in domestic revenue and financing.	• Submitted on October 30.
• Implement the specific tax on second-hand motor vehicles.	• Enhance revenue and improve tax and customs compliance culture. • Enhance revenue and improve transparency in duty rates of secondhand cars, as well as contain secondhand car imports.	• Gazette received on October 28.
Governance Reforms		
• Follow-up action report on the COVID-19 spending audit report and EDF's audit report. Publish a follow-up report related to the COVID-19 spending audit report, detailing the corrective actions and measures to pursue and respond to audit findings, including the follow-up of alleged misappropriation of funds as well as the coverage of a second audit findings.	• Strengthen governance and data transparency.	• Published on October 27.

Table 5. Malawi: Structural Benchmarks Under the ECF Arrangement

Actions	Timing	Objectives
Fiscal Reforms		
• Publish the monthly unaudited IFMIS-generated comprehensive fiscal reports on the MOFEA website, within 5 days after end of each month starting end-October 2023.	• Continuous, starting in FY2023/24	• Foster fiscal transparency and monitoring. • Improve the in-year comprehensive monthly fiscal reports.
• Repeal the preferential treatment for motor vehicle and VAT relief for current and former politicians, senior public officials, judges and other similar privileged individuals and groups.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.
• Ensure that every supply of a motor vehicle is standard rated for VAT purposes.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.
• Comprehensively eliminate VAT exemptions and zero-ratings for business inputs. • The sectors under these Customs Procedures Codes will be subjected to subsequent SBs: CPC 402 for (pharmaceutical and fertilizer manufacturing), 405 (health), 406 (education) 445 (priority industry and Government to Government Agreements). • “business” input means all goods imported by businesses specifically for their operations.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.

Table 5. Malawi: Structural Benchmarks Under the ECF Arrangement (continued)		
Actions	**Timing**	**Objectives**
Fiscal Reforms		
• Repeal VAT relief for building materials such that all supplies of building materials, construction services and commercial property are standard rated. • The following sectors will be subject to subsequent SBs: Education, Health, Priority sector and where there is an Agreement between Malawi Government and other Governments or bona fide institutions.	• July 2024	• Enhance revenue and improve tax and customs compliance culture.
• Full launch of the Integrated Tax Administration System (ITAS).	• End-March 2024	• Enhance revenue and improve tax and customs compliance culture
• Approval by the Cabinet of an arrears clearance and prevention strategy for national budget entities that has been prepared in consultation with Fund staff.	• End-March 2024	• Foster financial discipline.
• Publish a performance report outlining the status of project execution and spending for all projects, with a total estimated cost of at least MWK 25 billion in the Public Sector Investment Program (PSIP) on the MOFEA website, within 6 months after the fiscal year.	• Annually, starting in 2025	• Improve public investment management. • Support Malawi 2063

Table 5. Malawi: Structural Benchmarks Under the ECF Arrangement		
Actions	**Timing**	**Objectives**
Monetary and Financial Sector Reforms		
• Prepare, in consultation with Fund staff, draft amendments to the RBM Act as recommended by the 2021 Safeguards Assessment report and submit those amendments to public consultation	• End-December 2023	• Strengthen RBM governance.
• Submit the RBM Act amendments to Parliament	• End-March 2024	• Strengthen RBM governance.
External Sector Reforms		
• Progressively remove the four multiple currency practices and three exchange restrictions measures identified by Fund staff	• Gradually, starting 2024	• Strengthen the functioning of a market-determined exchange rate.
Governance Reforms		
• MOFEA and RBM jointly design and implement a credible, comprehensive, and cost-effective resolution plan to address challenges identified in the audit of the EDF.	• End June 2024	• Strengthen governance and transparency.
• Improve transparency and management of EDF via improved organizational arrangements and action on audit findings	• End June 2024	• Strengthen governance and transparency.
• NSO to start including reconciled data on imports of strategic commodities in the monthly Trade Bulletin	• End-December 2023	• Develop greater transparency in relation to strategic imports and to reconcile the varying sources of fuel imports data.

Table 5. Malawi: Structural Benchmarks Under the ECF Arrangement (concluded)

Actions	Timing	Objectives
Governance Reforms		
• Develop an action plan with specific deliverables and deadlines following the governance diagnostic TA.	• September 2024	• Strengthen governance and transparency.
Climate		
• Submit to Parliament the Disaster Risk Management (DRM) regulations and related policies to address gaps in disaster risk management. • (i) Building policy • (ii) Gazette Disaster Risk Management Regulations	• December 2024 • December 2023 • June 2024	• To guide developments in the area of disaster preparedness, risk reduction, and response and recovery buildings.

Attachment II. Technical Memorandum of Understanding

November 8, 2023

INTRODUCTION

1. **This memorandum sets out the understandings between the Malawian Authorities and the International Monetary Fund (IMF) regarding the definitions of the structural benchmarks (SBs), performance criteria (PCs), and indicative targets (ITs) for the Extended Credit Facility (ECF) as described in the Memorandum of Economic and Financial Policies (MEFP) for the period November 2023 through November 2024, and sets out the data reporting requirements.** It also describes the methods to be used to assess the program performance and the information requirements to ensure adequate monitoring of the targets. The authorities will inform the Fund before modifying measures contained in this memorandum, or adopting new measures that would deviate from the goals of the program, and provide the Fund with the necessary information for program monitoring.

COVERAGE

2. **The government is defined as the budgetary central government of Malawi, extra-budgetary units of the central government, and transfers to local government.** It excludes public nonfinancial corporations, public financial corporations, operations of local councils and social security funds. The budgetary central government is defined as central government entities with budgets controlled by the Ministry of Finance and Economic Affairs (MOFEA).

3. **The coverage of the financial sector includes the Reserve Bank of Malawi (RBM) and other depository corporations (ODC).** Monetary aggregates under the program are based on the central bank survey, other depository corporations survey, and depository corporations survey, in accordance with the Monetary and Financial Statistics (MFS) Manual and Compilation User Guide (2016).

PROGRAM EXCHANGE RATES

4. **For the purpose of evaluating the PCs and ITs, all foreign currency-related assets, liabilities, and flows will be evaluated at "program exchange rates" as defined below, with the exception of items affecting government fiscal balances, which will be measured at the current RBM exchange rates. The program exchange rates are those that prevailed on end-September 2023.** Accordingly, the exchange rates for the purposes of the program are shown in Table 1.

Table 1. Malawi: Cross Rates for Nominal Exchange Rate and Gold Price for the 2023–27 ECF

	30-Sep-23
Gold bullion LBM[1] US$/troy ounce	1915.43
SDR to US$ exchange rate	0.76
Australian $ to US$ exchange rate	1.55
Canadian $ to US$ exchange rate	1.35
Euro to US$ exchange rate	0.94
Kuwaiti dinar to US$ exchange rate	0.31
Malawian kwacha to US$ exchange rate	1115.78
Saudi Arabian riyal to US$ exchange rate	3.75
South African rand to US$ exchange rate	18.86
Sterling UK to US$ exchange rate	0.82
Swiss Franc to US$ exchange rate	0.91
UAE dirham to US$ exchange rate	3.67
Yen to US$ exchange rate	149.44
Yuan to US$ exchange rate	7.30

Sources: IMF; and Reserve Bank of Malawi

[1] LBM connotes London Bullion Market

PERFORMANCE CRITERIA AND INDICATIVE TARGETS

5. **Performance Criteria are established for March 31, 2024 and September 30, 2024; and Indicative Targets are established for December 31, 2023 and June 30, 2024 with respect to:**

- Monetary base (ceiling);
- Domestic revenue (floor)
- Domestic primary balance of the government (floor);
- RBM financing of the central government (ceiling);
- New domestic arrears (ceiling);
- Social spending (floor);
- Cumulative change in net international reserves (NIR) of the RBM since the beginning of the calendar year (floor);
- Accumulation of external payments arrears (ceiling);
- Contracting or guaranteeing of non-concessional external debt (ceiling); and
- Contracting or guaranteeing of concessional external borrowing (ceiling).

DEFINITIONS

Targets for Monetary Aggregates

Ceiling on the Stock of Monetary Base

6. A ceiling applies to the upper bound of a monetary base band (set +/-3 percent) around the monetary base target.

7. Definition. The monetary base is defined as currency in circulation, ODCs' deposit holdings at the RBM, and those deposits of money-holding sectors at the RBM that are also included in broad money as defined in the Monetary and Financial Statistics (MFS) Manual and User Guide (2016).

Targets for Fiscal Sector

Floor on Domestic Revenue

8. A floor applies to the cumulative flow of domestic revenue since the beginning of the fiscal year.

9. Definition of domestic revenue: The program domestic revenue is tax and nontax revenue, or other revenue as defined in Government Financial Statistics Manual (GSFM) 2014 Chapter 5, recorded on a cash basis. External loans and grants are excluded. One-off revenues (e.g. transfers from extra-budgetary funds, proceeds from the sale of financial assets, revenue from privatizations or from the granting or renewal of licenses) are not considered domestic revenue for the purposes of this domestic revenue floor. RBM dividends used to repay promissory notes associated with recapitalization of RBM are excluded from the calculation of domestic revenue.

Floor on Domestic Primary Fiscal Balance

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

11. Definition of the domestic primary fiscal balance. Domestic primary fiscal balance is defined (i) domestic revenue less (ii) the sum of recurrent budget expenditure (net of domestic and foreign interest payments), and domestically-financed budget development expenditure. Those flows related to recapitalization of the RBM are excluded from the calculation of domestic primary fiscal balance.

12. Definition of net foreign borrowing of the government: Net foreign borrowing is defined as the sum of project and program loan disbursements from official creditors (both multi- and bilateral creditors), holdings of government securities by non-residents, and commercial borrowing from non-residents, minus amortization due.

13. Definition of general budget support: General budget support includes all grants and foreign financing not directly linked to externally financed projects. Excluded from this definition are external project financing to fund particular activities, BOP support from the IMF as defined in the Memorandum of Understanding between the MOFEA and RBM, and donor inflows (in Kwacha) from the foreign currency-denominated donor pool accounts for the Joint Funds (e.g. health, education, and agriculture), held in financial institutions.

Ceiling on RBM Financing of the Government

14. Definition of RBM financing of the government. RBM financing of the government is defined as gross borrowing from the RBM by the government (including ways and means advances, loans, holdings of local registered stocks, government securities at cost value, and promissory notes). Those flows related to recapitalization of the RBM are excluded from the calculation of RBM financing of the government.

15. Adjustors:

- For cash management purposes, the ceiling on RBM financing of the central government for December, June, and September is subject to an upward adjustment of up to 10 percent of the average inflation-adjusted (by the GDP deflator) annual domestic revenue of the government for the past three fiscal years.

- Reflecting the current illiquidity in the secondary market for government securities, the ceiling on RBM financing of the central government for the remainder of FY2023/24 is subject to an additional upward adjustment calculated such that the total adjustor is equal to the maximum of (i) 10 percent of the average inflation-adjusted (by the GDP deflator) annual domestic revenue of the government for the past three fiscal years; or (ii) an adjustor to reflect holdings of illiquid securities, as defined below:

(MWK billions)	CY2023Q4 FY23/24Q3	CY2024Q1 FY23/24Q4	CY2024Q2 FY24/25Q1	CY2024Q3 FY24/25Q2
10 percent of revenue	209	0	263	263
Illiquid securities	250	300	0	0
Total adjustor	250	300	263	263

Ceiling on New Domestic Arrears

16. Definition of domestic arrears: Arrears as defined in PFM Act (2022) means all unpaid bills, inclusive of contractual and statutory obligations, after the end of financial year. For the purpose of this TMU, payments on wages and salaries, and transfers are deemed to be in arrears when they remain unpaid for more than 30 days beyond their due date. Domestic interest payments are in arrears when the payment is not made on the due date. Payments for goods and services and compensations are deemed to be in arrears if, following receipt of the goods or services or claims for compensations, they have not been paid by the end of the fiscal year, or – if a grace period has been agreed – within the contractually agreed grace period. For the purpose of the monthly reporting, the outstanding purchase orders, payables, and cash expenses on goods and services will be reported. New pensions arrears are deemed to exist if the stock of pension increases by the end of the fiscal year. For the purpose of the monthly reporting, outstanding pension payments in the last quarter due will be reported.

Floor on Social Spending

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

Targets for External Sector

18. Definition of net international reserves (NIR) of the RBM: The Net International Reserve (NIR) of the RBM is defined as reserves assets (RA) of the RBM minus foreign currency drains (FCD) of the RBM. The values of all foreign assets and FCD will be converted into U.S. dollars at each test date using the program cross exchange rates listed in Table 1. Cumulative change in NIR on each test date is calculated relative to the start of the calendar year: that is, the change is calculated between the stock of the NIR on the test date and that of the end-date of the previous calendar year.

19. Definition of reserve assets of the RBM. are defined by the International Reserves and Foreign Currency Liquidity Guidelines for a Data Template as external assets immediately available and controlled by RBM "for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency's exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing)" (BPM6, paragraph 6.64). Reserve assets include the following: (i) monetary gold holdings of the RBM; (ii) holdings of SDRs; (iii) the reserve position in the IMF; (iv) foreign convertible currency holdings; (v) foreign currency denominated deposits held in foreign central banks, the Bank for International Settlements, and other banks; (vi) loans to foreign banks redeemable upon demand; (vii) foreign securities; and (viii) other unpledged convertible liquid claims on nonresidents.

20. Foreign currency drains (FCD) of the RBM are defined as the sum of the following:

- outstanding medium and short-term liabilities of the RBM (including as an agent of the government), to the IMF (excluding SDR allocations); and

- all foreign currency liabilities of the RBM and the RBM as an agent of the government to come due within the next 12 months (4 quarters). These liabilities include (a) all foreign currency debt service falling due in the next 12 months (4 quarters), except to creditors to which the RBM and the RBM as an agent of the government is in arrears and/or servicing via other means, in line with the debt restructuring strategy, and (b) swaps outstanding with remaining maturity of less than one year.

21. Adjustors Applied to change in NIR Program Floor:

- **Adjustment clause on NIR- general budget support**: The program floor on change in NIR will be adjusted upward by the full amount by which the foreign currency-denominated inflows from the budget support exceed the program baseline (see Table below). In the event of a shortfall in budget support inflows, the downward adjustment of the change in NIR floor by the full amount by which the foreign currency-denominated inflows from the budget support falls short of the program baseline. They will be recorded in the original currency of payment and then converted to U.S. dollars using the above defined program cross exchange rates.

(USD Millions)	CY2023Q4	CY2024Q1	CY2024Q2	CY2024Q3
General budget support	80	55		
Multi Donor Trust Fund[1]	6	0		

[1] The Multi Donor Trust Fund (MDTF) is used for social projects such as social cash transfer programs. The fund is primarily mobilized in Malawi Kwacha, thus the foreign exchange component is projected to contribute in building up official reserves.

Ceiling on Accumulation of External Payment Arrears

22. Definition of external payment arrears: External payment arrears consist of debt service obligations (principal and interest) of the government or the RBM to nonresidents that have not been paid at the time they are due, or if a grace period has lapsed, as specified in contractual agreements. External debt that is to be subject to rescheduling or restructuring in line with the debt restructuring strategy is exempted from being included as external payment arrears, on the condition that the government continues to make a good faith effort to reach a collaborative agreement with creditors. This quantitative target will be monitored on a continuous basis.

Ceiling on Contracting or Guaranteeing Non-Concessional and Concessional External Debt

23. Definition of public and publicly guaranteed debt: The definition of debt, for program purposes, is consistent with paragraph 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to IMF Executive Board Decision No. 16919-(20/103), adopted in October 2020, as below, and also includes contracted or guaranteed commitments for which value has not been received. For program purposes, the term "debt" is understood to mean a current, that is, not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. For program purposes, a debt is considered contracted when all conditions for its entrance into effect have been met, including approval by the National Assembly. Contracting of credit lines with no predetermined disbursement schedules or with multiple disbursements will be also considered as contracting of debt. Debt can take several forms; the primary ones being as follows:

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

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

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

Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

24. Definition of concessional and non-concessional external debt. Short-, medium-, and long-term debt is considered concessional if it includes a grant element of at least 35 percent[1] and non-concessional if otherwise. The grant element is defined as the difference between the nominal value of the loan (or contractually-agreed package of loans) and its present value, expressed as a percentage of the nominal value of the loan (or package). The present value of the debt at the date on which it is contracted is calculated as the discounted sum of all future debt service payments at the time of the contracting of the debt.[2] The discount rate used for this purpose is 5 percent per annum. The ceiling on concessional and non-concessional debt applies to the contracting and guaranteeing of debt with nonresidents by the government, the RBM, and state-owned enterprises,

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

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

unless an explicit selective exclusion is made. This performance criterion is monitored on a continuous basis. The ceiling applies to debt and commitments contracted or guaranteed for which value has not been received. The ceiling is measured cumulatively from the beginning of the fiscal year.

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

26. Medium- and long-term debt: Outstanding stock of debt with an original maturity of more than one year.

27. Excluded from the limit on non-concessional external debt is the use of IMF resources.

28. Swaps in debt service: In line with definition of debt (Para.5), debt service payments should include swaps based on the net change in the position.

29. Foreign exchange swaps: contracting or renewing foreign currency swaps with non resident banks beyond the program amount would be subject to the ceiling of non-concessional external debt since they pose fiscal risks.

REPORTING REQUIREMENTS

30. For the purpose of program monitoring, the Government of Malawi will provide the data listed in Table 2 below. For all bi-weekly submissions, data should be reported with a lag of one week. For all monthly and quarterly submissions, data should be reported within 3 weeks. For data submissions requiring audit, data is reported within 10 weeks. Annual data will be provided within six months after the end of the year.

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

32. The authorities will furnish an official communication to the IMF describing program quantitative performance, structural benchmarks, and indicative targets within 8 weeks of a test date.

Table 2. Malawi: Summary of Reporting Requirements				
	Frequency of Data[1]	**Frequency of Reporting**[1]	**Frequency of Publication**[1]	**Agency**
Exchange Rates, Spread between exchange bureau midrate and the official exchange midrate	D	2W	D	RBM
Volume of transactions in the interbank money market and Lombard Facility, including banking system liquidity	D	2W	M	RBM
Foreign Exchange Cashflow (including Reserve Assets, Sources and Uses of foreign currency) (Telex Table 14)	D	2W	M	RBM
RBM intervention and ADB's Sales and Purchases of FX	D	2W	M	RBM
Foreign Exchange Swaps	continuous	2W	M	RBM
Reserve/base money, FMO transactions, and RBM conversion of ways and means account to government securities	M	M	M	RBM
Monetary and Financial Statistics Standard Report Forms (1SR, 1SG, 2SR, 2SG, 3SG, 5SR in Telex Table 1)	M	M	M	RBM
Consumer Price Index and monthly statistical bulletin (Telex Table 5)	M	M	M	RBM
Detailed issue and maturity profile for all government securities (Telex Table 6 & 7)	M	M	M	RBM
Central government domestic borrowing (Holdings of local registered stocks, treasury bills, treasury notes and other government securities) (Telex Table 8, 13, 20)	M	M	M	RBM
RBM financing of the central government	M	M	M	RBM
Government Project Funds through the RBM (Telex Table 9)	M	M	M	RBM
Interest rates [2] (Telex Table 12)	M	M	M	RBM
RBM foreign exchange cash flow and intervention (Telex Table 14, 27)	M	M	M	RBM
ADBs FCDA Balances (Telex Table 15)	M	M	M	RBM
Banking System Liquidity (Required and Excess Reserves) (Telex Table 16)	M	M	M	RBM

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

	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Agency
RBM Holding of Treasury Bills and Conversion of Ways and Means Advances (Telex Table 17)	M	M	M	RBM
Reserve Assets of the Monetary Authorities (as defined in Chapter 1 of International Reserves and Foreign Currency Liquidity: Guidelines For A Data Template)[3] (Telex Table 19)	M	M	M	RBM
Foreign Currency Drains of the Monetary Authorities (as defined in Chapter 3 of International Reserves and Foreign Currency Liquidity Guidelines For A Data Template)[3,4] (Telex Table 19)	M	M	…	RBM
Government securities auction results (Telex Table 20)	M	M	M	RBM
Bank statements of the Ministry of Health Swap account, agricultural Swap account, NAC account held at RBM (Table 24, 25, 26)	M	M	…	RBM
Sectoral Allocation of Private Sector Credit (Telex Table 28)	M	M	M	RBM
RBM Foreign Exchange Deposits (Telex Table 32)	M	M	M	RBM
Financial soundness indicators by banks (Telex Table 34)	M	M	…	RBM
Forex Bureau Trade Volume (Telex Table 35)	M	M	M	RBM
Balance of payments	A	A	A	RBM / NSO
New external loans contracted or guaranteed by the government and disbursement schedule [5]	Continuous	Continuous	Continuous	MOFEA
Revenue collected by MRA, by major revenue line	D	2W	M	MOFEA
Accumulation of new domestic government arrears[6]	M	M	M	MOFEA
Strategic Imports (value, volume, and prices)	M	M	M	MOFEA
Fiscal table (GFS based), including revenue, grants, expenditure, balance, and composition of financing of the central government[5, 7]	M	M	…	MOFEA
In-year comprehensive monthly fiscal reports	M	M	Q	MOFEA

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

	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Agency
Exports and imports of goods and subcomponents (to be added to Telex tables submissions)	M	M	Q	MOFEA
On and off-budget project reports	Q	Q	Q	MOFEA
Stocks of public sector and public-guaranteed debt[5, 8]	Q	Q	Q	MOFEA
Quarterly external debt service (actual and projections)	Q	Q	…	MOFEA
Debt service payments on domestic debt (outturn and projections)	M	Q	Q	MOFEA
Report on IMF program performance	Q	Q	…	MOFEA
Quarterly report on clearance of government domestic arrears	Q	Q	…	AG
Exports and imports of services, and subcomponents.	A	A	A	MOFEA
Annual financial reports of the 5 high-risk parastatals[9]	A	A	…	MOFEA
Consolidated financial statements and audit opinion	A	A	A	AG
Consolidated budget execution reports	M	M	A	AG
GDP, by activity and expenditure, at constant and current prices	A	A	A	MOFEA

[1] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Semi-annually (SA); Irregular (I).
[2] Both market-based and officially-determined, including discount rates, money market rates, interbank money market rate, rates on treasury bills, notes, and bonds.
[3] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[4] Includes a memorandum section which includes Net International Reserves based as defined in this TMU.
[5] Detailed information on the amounts, currencies, terms and conditions, including debt contracted or guaranteed by the RBM or any other agency on behalf of the central government.
[6] In accordance with the definition of arrears in the TMU Paragraph 17.
[7] Foreign and domestic banks, and domestic nonbank financing.
[8] Includes borrowing of 8 major parastatals: Agriculture Development and Marketing Corporation (ADMARC), Electric Supply Company of Malawi (ESCOM), Electricity Generation Company of Malawi (EGENCO), Malawi Housing Corporation, National Oil Company of Malawi (NOCMA), Northern Regional Water Board, Lilongwe Water Board, and Blantyre Water Board (BWB).
[9] ADMARC, BWB, ESCOM, EGENCO, and NOCMA.

INTERNATIONAL MONETARY FUND

MALAWI

November 8, 2023

SECOND REVIEW UNDER THE STAFF-MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT AND REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

Approved By
Costas Christou and Bjoern Rother (both IMF) and Manuela Francisco and Hassan Zaman (both IDA)

Prepared by the International Monetary Fund and the International Development Association[1]

Malawi: Joint Bank-Fund Debt Sustainability Analysis[2]	
Risk of external debt distress	*In Debt Distress*
Overall risk of debt distress	*In Debt Distress*
Granularity in the risk rating	*Unsustainable*
Application of judgment	*No*

Malawi's external and overall public debt is assessed as "in distress"—unchanged from the previous Debt Sustainability Analysis (DSA) in July 2023. This DSA presents an analysis of Malawi's debt outlook prior to the implementation of the authorities' planned debt restructuring.

Under the baseline scenario, the Present Value (PV) of PPG external debt-to-GDP ratio remains below the threshold throughout the horizon. However, breaches are observed in the PV of debt-to-exports, debt service-to-exports, and debt service-to-revenue ratios over the medium term—with significant external debt servicing needs (around 60 percent of exports in 2023) falling due in the near term. The debt service-to-exports ratio remains in breach beyond the medium-term horizon. The PV of Malawi's overall public debt-to-GDP was around 67 percent in 2022 and remains significantly above the threshold through the medium term. Malawi's debt is currently unsustainable. Timely and complete implementation of the authorities' debt restructuring strategy would be necessary for the external debt burden to be considered sustainable on a forward-looking basis.

[1] The current DSA follows the revised Debt Sustainability Framework (DSF) for LICs and Guidance Note (2017) in effect as of July 1, 2018.

[2] Malawi's Composite Indicator (CI) is based on the latest published vintage (2021 Country Policy and Institutional Assessment, CPIA) and the IMF's April 2023 World Economic Outlook. The CI remains 'weak' with a CI score of 2.42.

PUBLIC DEBT COVERAGE

1. **The DSA covers central government debt, central government guaranteed debt, and central bank debt contracted on behalf of the government** (Text Table 1). Public debt used for this DSA is public and publicly guaranteed (PPG) external (as defined on a residency basis) and public domestic debt, covering debt contracted and guaranteed by the central government and the Reserve Bank of Malawi (RBM). Due to data limitations, it does not include debt held by state and local governments, other elements in the general government (such as the social security fund and extra budgetary funds), or nonguaranteed state-owned enterprise (SOE) debt. [3,4]

Text Table 1. Malawi: Coverage of Public Sector Debt, 2022

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

1	The country's coverage of public debt	The central government, central bank			
		Default		Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0	percent of GDP	3.3	2 percent for limited coverage, 1.3 percent for government guaranteed debt.
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2	percent of GDP	2.0	
4	PPP	35	percent of PPP stock	0.0	
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5	percent of GDP	5.0	
	Total (2+3+4+5) (in percent of GDP)			10.3	

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

BACKGROUND AND RECENT DEVELOPMENTS

2. **This DSA is being conducted in the context of the second review of the Staff-Monitored Program with Executive Board Involvement (PMB) and request for an arrangement under the Extended Credit Facility (ECF).** The last Low-Income Country (LIC) DSA using the LIC-Debt Sustainability Framework (DSF) was considered by the Executive Board in July 2023 as part of the first review of the PMB.[5]

[3] The contingent liabilities shock from SOE debt is kept at the default value of 2 percent to reflect risks associated with nonguaranteed SOE debt, currently excluded from the analysis due to data availability constraints. There are no current public-private partnerships reported that subject the authorities to contingent liabilities.

[4] The government has recognized the importance of increasing debt coverage and requested the World Bank to support in creating a contingent liability framework under the FY24 SDFP PPAs.

[5] The last joint DSA can be found in IMF Country Report No. 23/299, July 2023.

Malawi is subject to International Development Association (IDA)'s Sustainable Development Finance Policy (SDFP) and the IMF's Debt Limit Policy (DLP), which both impose a zero non-concessional debt ceiling.

3. **Malawi continues to face a challenging macroeconomic outlook.** Real GDP growth is projected to recover to a below-trend 1.6 percent in 2023, as Malawi has continued to face protracted balance of payments challenges, including shortages of foreign exchange, and a hit to agriculture output as a result of Cyclone Freddy. Inflation remains elevated, at 27.8 percent in September, driven in large part by food inflation, at 36.8 percent, even as global price pressures ease and money growth levels off. The Reserve Bank of Malawi (RBM) raised interest rates by a further 200 basis points, to 24 percent, in August. But inflation is projected to remain well above target this year and next, at 30.3 percent and 27.9 percent, on average, respectively.

4. **Strong efforts to meet fiscal targets under the PMB have been evident, with government spending in FY 23/24 so far largely consistent with the budget envelope.** This reflects a marked turn-around in performance from the first review, when fiscal targets were missed. Fiscal consolidation has been supported by strong public financial management (PFM) reforms, including the continued rollout of the Integrated Financial Management Information System (IFMIS) and the announcement of quarterly allotments aligned with the agreed macroeconomic framework. But Malawi continues to run a significant domestic primary deficit, estimated to be 3 percent of GDP in FY 23/24, and faces a heavy domestic debt service burden, 5 percent of GDP in FY 23/24. Central bank financing was contained over the first half of 2023 but remains elevated.

5. **Meanwhile, external strains—including shortages of foreign exchange, difficulties in securing trade credit, and continued pressure on the spread between official and bureau exchange rates—have persisted.** Import activity remained below 2021 levels over the first half of the year, with Malawi continuing to experience shortages of fuel, cement, fertilizer and essential medical supplies. However, exports are expected to benefit from a significant increase in tobacco sales, on the back of improved weather and higher prices. The official exchange rate has depreciated by around 15 percent since the first review, with the RBM restarting regular auctions in an effort to move towards a market-clearing rate. This has not yet had the effect of narrowing the spread between the official rate and the bureau rate, which now stands at over 50 percent.

6. **The RBM has made limited progress in rebuilding its official reserves—preliminary data show that gross reserves stood at [US$156 million] as of end-September 2023.** Strong project-related inflows and the proceeds from export earnings have supported reserves accumulation, but the RBM has continued to face selling pressure to meet the country's strategic import needs. Gross reserves are projected to grow from here and to reach the level of import coverage considered to provide adequate insurance against external shocks (3.9 months of import cover) in 2025.

7. **Public debt has increased significantly in recent years driven by structural fiscal deficits and rising interest costs**. The stock of public and public-guaranteed debt reached 75.7 percent of GDP in 2022, driven by both external and domestic debt. Conversion of short-term swaps into medium-term commercial debt further contributed to pushing external debt into distress. The government's recourse to high-cost domestic borrowing to finance fiscal deficits has pushed domestic debt upwards, reaching 40.8 percent

of GDP in 2022. Rising interest costs have not only increased the fiscal burden (absorbing 36.8 percent of domestic revenue in FY2022/23) but have also strained liquidity on the domestic market.

8. The authorities continue to make progress on their external debt restructuring strategy, which staff assesses to represent a challenging but credible path to external debt sustainability. Malawi is seeking comparable treatment from all official bilateral creditors, and, in the judgement of staff, continues to pursue good faith negotiations with its commercial creditors. Malawi is in arrears on commercial debt while these discussions continue, which has helped to ease near-term liquidity pressures. Staff expects that Malawi's debt to Saudi Arabia, Kuwait, UAE and the two Paris Club creditors will be treated on comparable terms with its largest bilateral creditors.

Box 1. Malawi: October 2022 Debt Restructuring Strategy

The authorities continue to pursue an external debt restructuring strategy that serves as the cornerstone of their efforts to restore debt sustainability. This follows a decade in which Malawi's external debt (as a share of GDP) has increased by over 80 percent, leading to an unsustainable debt burden and servicing costs. In May 2022, they hired legal and financial advisors to support a credible process for restructuring based on adequate creditor engagement to ensure the approach taken delivers the necessary contributions in a sustainable manner. The authorities approached all external creditors early in the process.

The debt restructuring strategy is designed to achieve debt sustainability and to close the financing gaps. The strategy relies on the following pillars to overcome current external debt challenges, including solvency and liquidity concerns:

- Bringing external public debt back to a moderate risk of debt distress in the medium term through a combination of policy adjustment and the necessary debt treatment. The debt strategy is designed to ensure all external DSA solvency and liquidity ratios move below their respective thresholds under the baseline over the medium term. As such, the present value of debt-to-GDP ratio falls below 30 percent, the present value of debt-to-exports ratio falls below 140 percent, the debt service-to-exports ratio falls below 10 percent, and the debt-to-revenue ratio falls below 14 percent in the medium term (see chart panel below).

- Mobilization of non-debt-creating flows to ensure that external and fiscal financing gaps are closed over the program period, including through the debt treatment and the mobilization of external grant support from development partners.

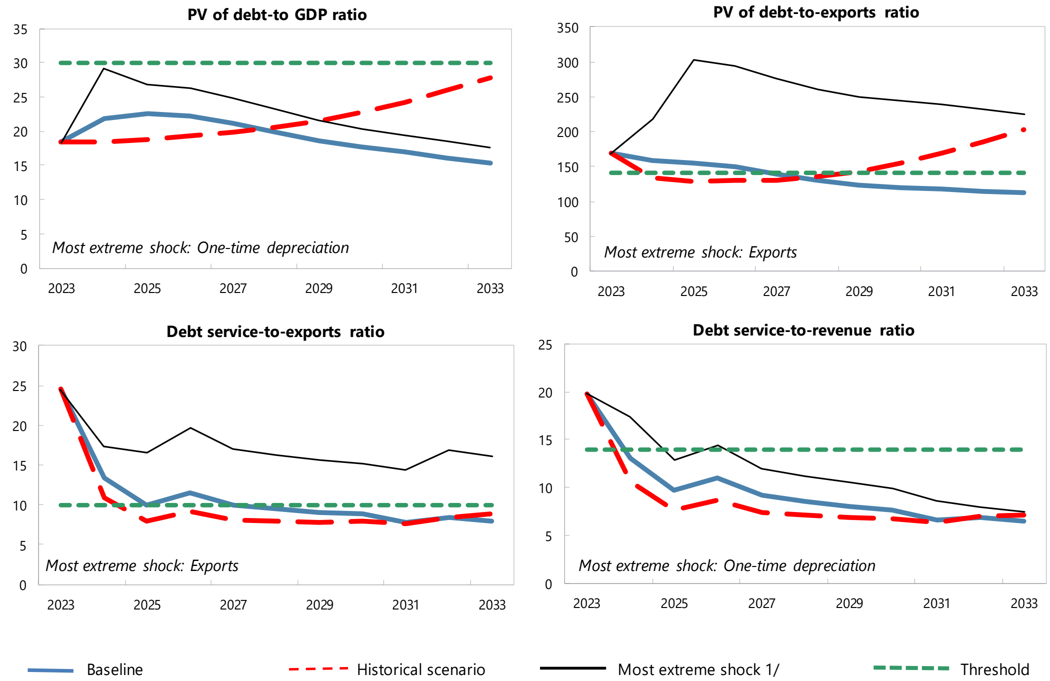
- The proposed debt treatment would result in a reduction in the NPV of Malawi's external debt of US$592 million. This would be achieved via significant maturity extension and reprofiling of scheduled payments to provide important near-term liquidity relief and to bring Malawi's external debt servicing costs in the medium term to a sustainable level.

The authorities are negotiating with commercial and official bilateral creditors and have reached agreement to reduce their debt service needs in the interim. Malawi is now in arrears (totaling US$418 million as of end-September 2023) on commercial debt. Subject to a judgement that Fund support was essential for the successful implementation of Malawi's adjustment program, and that Malawi was pursuing appropriate policies and making a good faith effort to reach a collaborative agreement with its private creditors, this would allow the Fund's Lending into Arrears (LIA) policy to apply.

Box 1. Malawi: October 2022 Debt Restructuring Strategy (concluded)

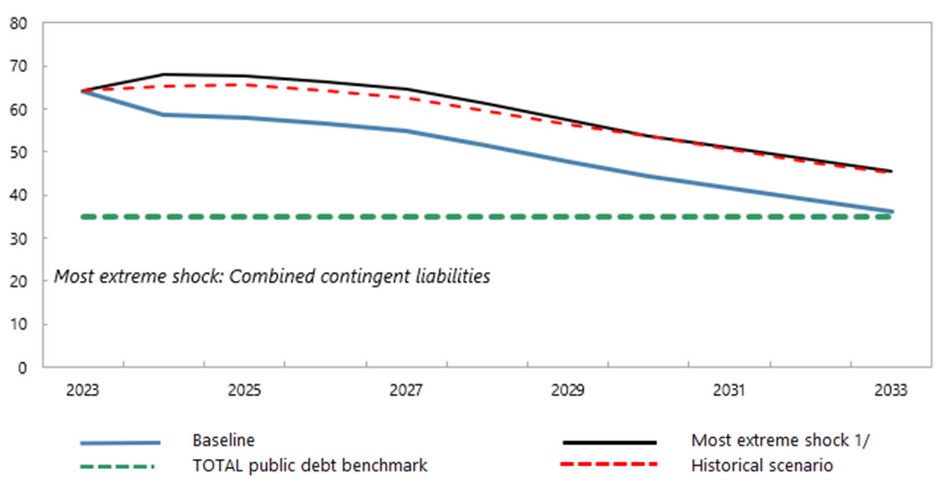
Malawi has received financing assurances from its largest official bilateral creditors and continues to negotiate with its commercial creditors. The timeline to complete this process remains uncertain and the risk of further delays is high, which would have the potential to jeopardize program performance.

Public and Publicly Guaranteed External Debt Under Post-Debt Restructuring Scenario, 2023–33



Overall Public Debt Under Post-Debt Restructuring Scenario, 2023–33

PV of Debt-to-GDP Ratio



[1] The most extreme stress test is the test that yields the highest ratio in or before 2033.

Text Table 2. Malawi. Decomposition of Public Debt and Debt Service by Creditor, 2022[1]

	Debt Stock (end of period)		
	2022		
	(In Million US$)	*(Percent total debt)*	*(Percent GDP)*
Total	8,699	100	76
External	4,006	46	35
Multilateral creditors[2]	2,558	29	22
IMF	437	5	4
World Bank	1,317	15	11
AfDB	431	5	4
Other Multilaterals	372	4	3
o/w: IFAD	106	1	1
OFID	76	1	1
Bilateral Creditors	418	5	4
Paris Club	4	0	0
o/w: Spain	3	0	0
Belgium	1	0	0
Non-Paris Club	414	5	4
o/w: EXIM China	222	3	2
EXIM India	114	1	1
Saudi Arabia	29	0	0
Local debt with non-residents	87	1	1
Commercial creditors	890	10	8
o/w: AFREXIM	495	6	4
TDB	395	5	3
FX Swaps with non-residents	53	1	0
Domestic	4,693	54	41
Held by residents, total	4,555	52	40
FX Swaps with resident	139	2	1
Memo items:			
Collateralized debt[3]	503	6	4
o/w: Related			
o/w: Unrelated		0	0
Contingent liabilities	53	1	0
o/w: Public guarantees		0	0
o/w: Other explicit contingent liabilities[4]			
Nominal GDP	12,535		

1/As reported by country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA.
2/Multilateral creditors are defined here as institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears)
3/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and
4/Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

UNDERLYING ASSUMPTIONS

9. **Financing assumptions rest on the implementation of a strict reform program by the authorities while debt restructuring negotiations are ongoing.** Under the ECF, the authorities have committed to a macroeconomic adjustment and reform program to restore macroeconomic stability and promote durable and inclusive growth. Decisive actions to secure financing and debt sustainability assurances are envisaged in the authorities' debt restructuring strategy (Box 1), which includes the

replacement of non-concessional external financing by non-debt-creating flows (including grants and debt relief).[6]

10. The key macroeconomic assumptions are broadly unchanged relative to the DSA that accompanied the PMB first review (the July 2023 DSA hereafter). The baseline scenario presented here is in line with the macroeconomic adjustment path envisaged under the PMB and is intended to represent a pre-debt restructuring scenario (Text Table 3). Changes to the underlying assumptions relative to the July 2023 DSA are as follows:

- **Growth** in 2023 is a little weaker, reflecting continued shortages of foreign exchange, and tighter monetary policy, offset somewhat by stronger tobacco exports. Real GDP growth is now projected to be 1.6 percent in 2023, down from 1.7 percent projected at the time of the first review, before recovering to 4.6 percent in the medium term. This is underpinned by gradual macroeconomic stabilization, including an easing of shortages of foreign exchange and related external pressures, and a recovery across all sectors, including the resumption of electricity generation at the Kapichira hydropower plant, which will support the manufacturing and services sectors, governance reforms in the energy sector, and various measures to promote agriculture commercialization. The long-term growth assumptions incorporate the expected impact of future weather-related shocks, given Malawi's vulnerability to climate change.

- The near-term outlook for **inflation** has worsened, despite some easing in global price pressures. CPI inflation is projected to reach 30.3 percent on average in 2023, up from 24.8 percent as expected at the time of the first review, reflecting renewed pressure on the exchange rate and food prices. In the medium term, inflation falls back to around 6.5 percent as external shocks fade and money growth is brought under control. This will require concerted effort from monetary and fiscal policy, including further tightening as needed to control additional inflationary pressures. In the medium term, **broad money** is assumed to grow in line with nominal GDP.

- The baseline scenario includes a challenging **fiscal adjustment**. It aims to, at a minimum, stabilize public debt by the end of medium term—i.e. to reduce the primary deficit, estimated at 6.8 percent of GDP in FY22/23, to sustainably reach the debt-stabilizing primary deficit by 2028 at the latest. Accordingly, the size of adjustment of the **domestic primary balance** is about 1.7 percentage points of GDP per year (excluding RBM capitalization, the size of the adjustment is about 1.3 ppt per year over four years)—which is within the norm of fiscal adjustments for fragile states and is consistent with policy adjustments identified in recent Technical Assistance on domestic revenue mobilization. The adjustment on expenditure will focus on further scaling back the Affordable Input Programme (fertilizer subsidies) by improving targeting and efficiency, and reallocation of spending towards building a foundation for growth and boosting human and physical capital, including improvements in the social safety net and agricultural productivity. This is supported by the introduction of new revenue measures as well as improvements in tax administration. New measures include operationalizing a specific tax on secondhand cars, repealing VAT relief on motor vehicles for

[6] Consistent with the LIC DSF Guidance Note, grants are only included in the DSA if they are firmly committed or, if they don't change the risk of debt distress rating, where they are considered highly likely.

current and former politicians, senior public officials, judges, and other similarly privileged individuals and groups, ensuring that every supply of a motor vehicle is standard rated for VAT purposes, and comprehensively eliminating other VAT exemptions on business inputs and building materials. The full launch of the Integrated Tax Administration System (ITAS) will enhance revenue collection and improve tax and customs compliance culture.

- The baseline scenario assumes that the RBM takes further decisive steps to rebuild **gross official reserves,** which increase to a level better able to withstand external shocks (assessed to be at least 3.9 months of imports cover) as soon as possible but no later than by the end of the medium term. This will require the central bank to limit sales of foreign exchange to the market and to maintain a consistent pace of net purchases and retention of other inflows.

Text Table 3. Malawi: Underlying DSA Assumptions, 2019–43

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	Avg. 2029-43
					(year-on-year percent change)						
Real GDP Growth											
Current	5.4	0.9	4.6	0.8	1.6	3.3	3.8	4.3	4.5	4.6	4.6
Previous	5.4	0.9	4.6	0.8	1.7	3.3	3.8	4.3	4.5	4.6	4.6
					(Percent of GDP)						
Primary Balance[1/]											
Current	-1.9	-2.7	-3.6	-5.0	-6.8	-5.4	-1.1	0.4	1.7	3.0	...
Previous	-1.9	-2.7	-3.6	-5.0	-6.8	-4.9	-1.6	1.2	1.5	2.1	...
Total Public Debt[1/]											
Current	45.3	54.8	61.5	75.7	82.1	75.4	74.5	72.2	69.5	65.0	35.0
Previous	45.3	54.8	64.0	76.6	74.6	74.5	73.8	72.6	71.0	68.9	52.7
Current Account Deficit											
Current	12.6	13.8	14.1	3.2	7.6	8.5	9.9	9.0	8.2	7.4	5.5
Previous	12.6	13.6	14.1	3.8	7.9	9.0	8.6	7.6	6.3	5.9	3.7
FDI											
Current	1.0	0.8	0.8	0.3	0.4	0.5	0.8	0.8	0.9	1.0	1.3
Previous	1.0	0.8	0.8	0.3	0.4	0.5	0.8	0.8	0.9	1.0	1.3

Sources: Malawian authorities and IMF staff calculations and projections.
[1/] Fiscal Data refers to fiscal year; e.g. 2021 = FY2020/21

- The **current account deficit** is projected to widen in the coming years as import growth recovers (and informal imports reduce), before improving gradually over the medium term. Exports continue to grow over the medium term (and to diversify somewhat beyond tobacco), but Malawi is assumed to remain reliant on large current transfers. The current account deficit reaches 7.4 percent of GDP in 2028, roughly in line with the sustainable level according to Staff's External Sector Assessment. The projected external sector adjustment will be supported by efforts to boost exports, including measures to promote agricultural productivity, diversification and commercialization through improved support to smallholder farmers and increased investment in large anchor farms, the further growth of tourism, and expanded mining activity.

- The total **external financing gap** (from 2023 to 2027) is projected to sum to around US$1.6 billion (roughly 9 percent of 2022 GDP). The assumed financing mix and terms for the government are in line with Malawi's Medium-Term Debt Management Strategy (MTDS), as in the July 2023 DSA. The financing mix now includes prospective disbursement under the ECF arrangement over 2023-27, which is different from the July 2023 DSA. Existing non-concessional external financing is wound down over time, with prospective concessional budget support grants and loans assumed to come in CY2023 Q4. In the medium term the external debt stock is smaller as a share of GDP and largely composed of financing from multilateral creditors. No debt treatment is assumed in the baseline scenario; instead, net domestic financing is assumed to fill the residual gap on market terms.

- Domestic financing costs are currently elevated, given tight monetary policy and high uncertainty, which increases the risk of fiscal slippage and crowding out of private investment. Interest costs are assumed to decrease gradually over the medium term (to around 14 percent on average) as policy normalizes and the economic outlook stabilizes. Issuance is across the curve, with 70 percent issued at a maturity of three years or less. Domestic financing (excluding that required to cover the residual external financing gap in the pre-restructuring scenario) is expected to average 13 percent GDP from 2023 to 2028 before declining gradually over time.

REALISM OF THE BASELINE ASSUMPTIONS

11. **The realism tools suggest that the baseline scenario is not significantly out of line with Malawi's historical experience and cross-country experiences** (Figures 3 and 4). The projected trajectory of nominal external and overall public debt as a share of GDP is very similar to that in the July 2023 DSA, but is lower than that in the November 2022 DSA in the medium term and beyond. The growth of external debt is slightly lower over the next five years than in the preceding five years, partly reflecting the improvement in the current account balance. Overall public debt is projected to grow by notably less, given the assumed fiscal adjustment.

12. **The pace of adjustment in the primary balance in the next three years is ambitious and falls within the top quartile of historical data on LIC adjustment programs** (Figure 4). The GDP growth projection is also stronger than implied by the estimated fiscal impulse alone, given staff expects some catch-up growth as Malawi recovers from the impact of Cyclone Freddy and other supply shocks, as well as the positive catalytic effects of the assumed reform path. These results highlight the challenging nature of the adjustment path and support the assessment in the Staff Report that the balance of risks is tilted to the downside.

COUNTRY CLASSIFICATION AND MODEL SIGNAL

13. **Malawi's debt-carrying capacity based on the Composite Indicator (CI) is assessed as weak** (Text Table 4). The CI is determined by the World Bank's 2021 Country Policy and Institutional Assessment (CPIA), the IMF's April 2023 World Economic Outlook, and other variables informed by the macroeconomic framework, including real GDP growth, import coverage of reserves, remittances as a percent of GDP,

and global growth. It is broadly unchanged from the July 2023 DSA. The four external debt burden thresholds and the total public debt benchmark are determined by this classification of the debt carrying capacity (Text Table 5).

Text Table 4. Malawi: Composite Index

Debt Carrying Capacity	Weak

Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintage
Weak	Weak 2.42	Weak 2.27	Weak 2.34

Calculation of the CI Index:

Components	Coefficients (A)	10-year average values (B)	CI Score components (A*B) = (C)	Contribution of components
CPIA	0.385	3.147	1.21	50%
Real growth rate (in percent)	2.719	3.432	0.09	4%
Import coverage of reserves (in percent)	4.052	21.568	0.87	36%
Import coverage of reserves^2 (in percent)	-3.990	4.652	-0.19	-8%
Remittances (in percent)	2.022	2.223	0.04	2%
World economic growth (in percent)	13.520	2.856	0.39	16%
CI Score			2.42	100%
CI rating			Weak	

Text Table 5. Malawi: Debt Carrying Capacity and Thresholds

EXTERNAL debt burden thresholds	Weak	Medium	Strong
PV of debt in % of			
Exports	140	180	240
GDP	30	40	55
Debt service in % of			
Exports	10	15	21
Revenue	14	18	23

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

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

SCENARIO STRESS TESTS

14. Standard scenario stress tests and a contingent liability stress test are conducted (Text Table 1, and Tables 3 and 4). The latter features a one-off increase of 11 percentage points in the debt-to-GDP ratio in the second year of the projection, designed to capture the combined impact of limited public debt coverage, contingent liabilities associated with SOEs, and the risk of potential future recapitalization of the banking sector.

15. A second tailored scenario featuring a commodity price shock is also conducted (Tables 3 and 4). Given that tobacco accounts for nearly half of Malawi's total goods exports, the DSA stress tests the debt outlook against a prolonged decline in commodity prices. The shock is calibrated to simulate a decline in prices in the second year of the projection to the lower end of the 68 percent confidence interval in the IMF's commodity price forecasts, which is then assumed to unwind over a period of six years.

EXTERNAL DSA

16. Malawi's external public debt is assessed to be in debt distress, reflecting the country's ongoing debt restructuring negotiations. Under the baseline scenario, the PV of PPG external debt-to-GDP ratio remains below the threshold. But there are significant and sustained breaches of the other solvency and liquidity indicators (Figure 1). The PV of debt-to-exports, debt service-to-exports, and debt service-to-revenue ratios are currently above their respective thresholds and remain so for a prolonged period—through 2030 in the case of debt-service-to-exports. The debt service burden (which includes repayment of arrears in the pre-restructuring scenario) is exceptionally high in the near-term, reaching 58 percent of exports and 47 percent of revenue in 2023.

17. Malawi's external debt is currently unsustainable. If the debt restructuring strategy were to be executed successfully, alongside implementation of the envisioned macroeconomic adjustment, it would be considered sustainable on a forward-looking basis. A successful debt treatment of commercial and official bilateral debt in line with the authorities' strategy (as set out in Box 1) would significantly reduce near-term debt service and bring the relevant solvency and liquidity indicators below their respective thresholds by 2028 or sooner. This would bring Malawi back to moderate risk of external debt distress over the medium term.

18. The stress scenarios highlight that Malawi's capacity to service its debt is particularly sensitive to the outlook for exports and the exchange rate. Malawi's exports are highly concentrated and vulnerable to weather and climate-related shocks, while the exchange rate could also be buffeted by domestic and external shocks. Mitigating the former risk somewhat is the fact that Malawi has typically received steady and predictable aid flows in foreign currency (not accounted for in the calculation of the DSA's liquidity indicators).

PUBLIC DSA

19. Malawi's overall public debt is assessed to be in distress, given the ongoing external debt restructuring negotiations. Under the baseline scenario, the PV of overall public debt reaches 69 percent of GDP in 2023, significantly above the threshold of 35 percent. This indicator declines somewhat over the medium term but remains in breach. Overall public debt service peaks in 2025 at 121 percent of revenues and remains high in the medium term. Successful implementation of the government's external debt restructuring strategy would significantly reduce the PV and servicing costs of overall public debt, although both would remain elevated, albeit decreasing, in the medium term. The overall risk of public debt distress would remain high in this scenario, with the PV of public debt at around 52 percent of GDP in 2028 (Box 1), while debt service-to-revenue would remain below 100 percent and decline gradually over time.

RISK RATING AND VULNERABILITIES

20. Malawi is currently in debt distress and absent restructuring the debt burden is assessed to be unsustainable, given the vulnerabilities associated with the significant and sustained breaches of the DSA's solvency and liquidity indicators. Conditional on the successful completion of the government's debt restructuring strategy, its external debt would be considered sustainable on a forward-looking basis.

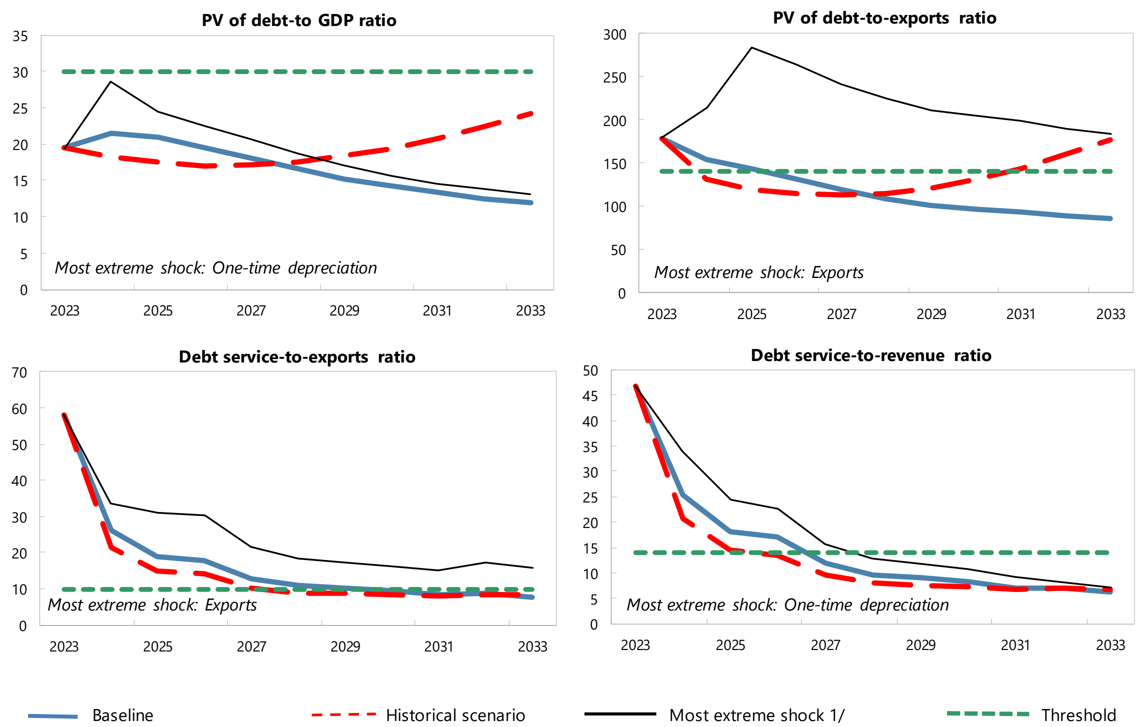
21. This assessment is subject to significant uncertainty and risks are skewed to the downside. Most notably, further delays to the completion of Malawi's debt restructuring strategy will make it increasingly difficult to close the government's financing gaps. Likewise, there is limited scope for any slippage on the ambitious fiscal adjustment, and associated implementation of PFM measures and other reforms, envisioned as part of the ECF—especially given the risk of additional spending pressures related to the general election in May 2025 and downside risks to the growth outlook. Elevated domestic financing costs and the associated debt service burden leave little room for maneuver. Malawi is also vulnerable to a range of external shocks and will remain so if the authorities fail to take decisive action to rebuild external buffers.

22. Mitigating factors include the authorities' strong commitment to macroeconomic adjustment, including corrective actions taken to complete the first review of the PMB. Expedited and comprehensive implementation of necessary policy actions has the potential to catalyze a positive feedback loop: as the outlook improves, resilience is strengthened, and confidence is boosted. Further upside risks include successful efforts to pursue export diversification, including sooner-than-expected development of mining projects (not yet included in the macro framework), which would enhance Malawi's capacity to meet future debt servicing needs.

AUTHORITIES' VIEWS

23. The authorities are in broad agreement with the WB's and IMF's staff assessments. They remain determined to restore macroeconomic stability and deliver strong and durable poverty reduction and growth. This will require decisive efforts to enhance fiscal discipline, maintain price stability and financial soundness, rebuild external buffers, and restore debt sustainability. Successful and timely completion of the authorities' external debt restructuring strategy is vital to achieving these goals. They are committed to shifting Malawi's growth model from a consumption-driven to a production-driven one and from a government-led to a private-sector-led one in line with the core principles of Malawi 2063.

Figure 1. Malawi: Indicators of Public and Publicly Guaranteed External Debt Under Baseline (Pre-Debt Restructuring) Scenarios, 2023–33



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	Yes	
Natural disaster	n.a.	n.a.
Commodity price	No	No
Market financing	n.a.	n.a.

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

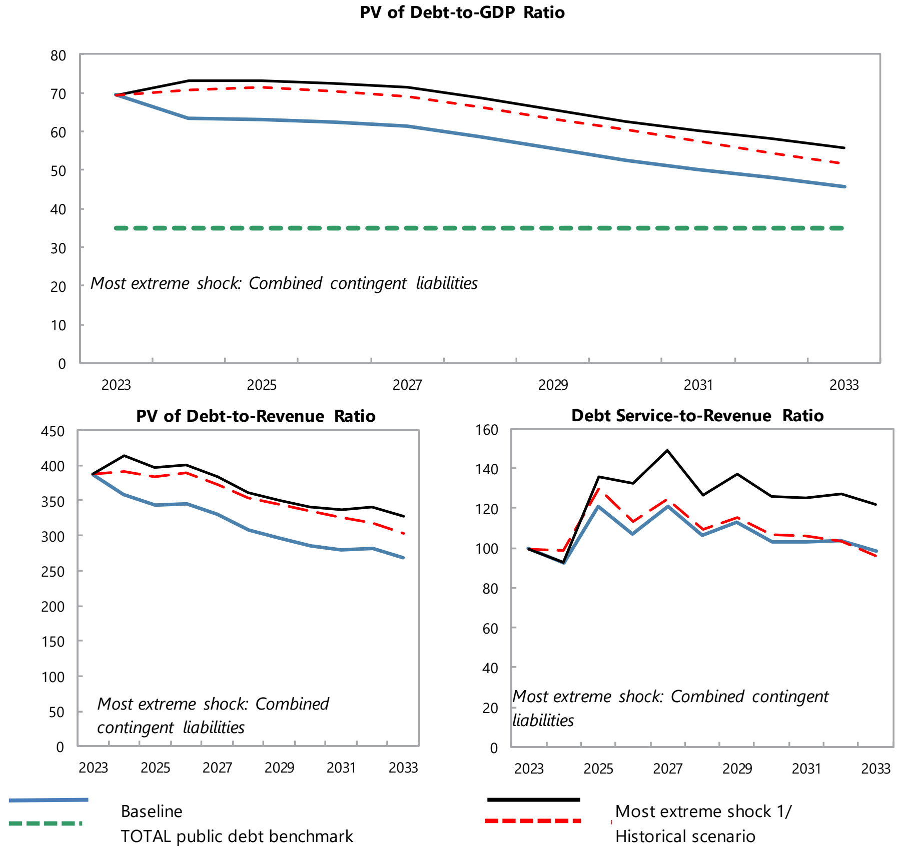
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	0.8%	0.8%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	34	34
Avg. grace period	6	6

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

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 2. Malawi: Indicators of Public Debt Under Baseline Scenarios, 2023–33



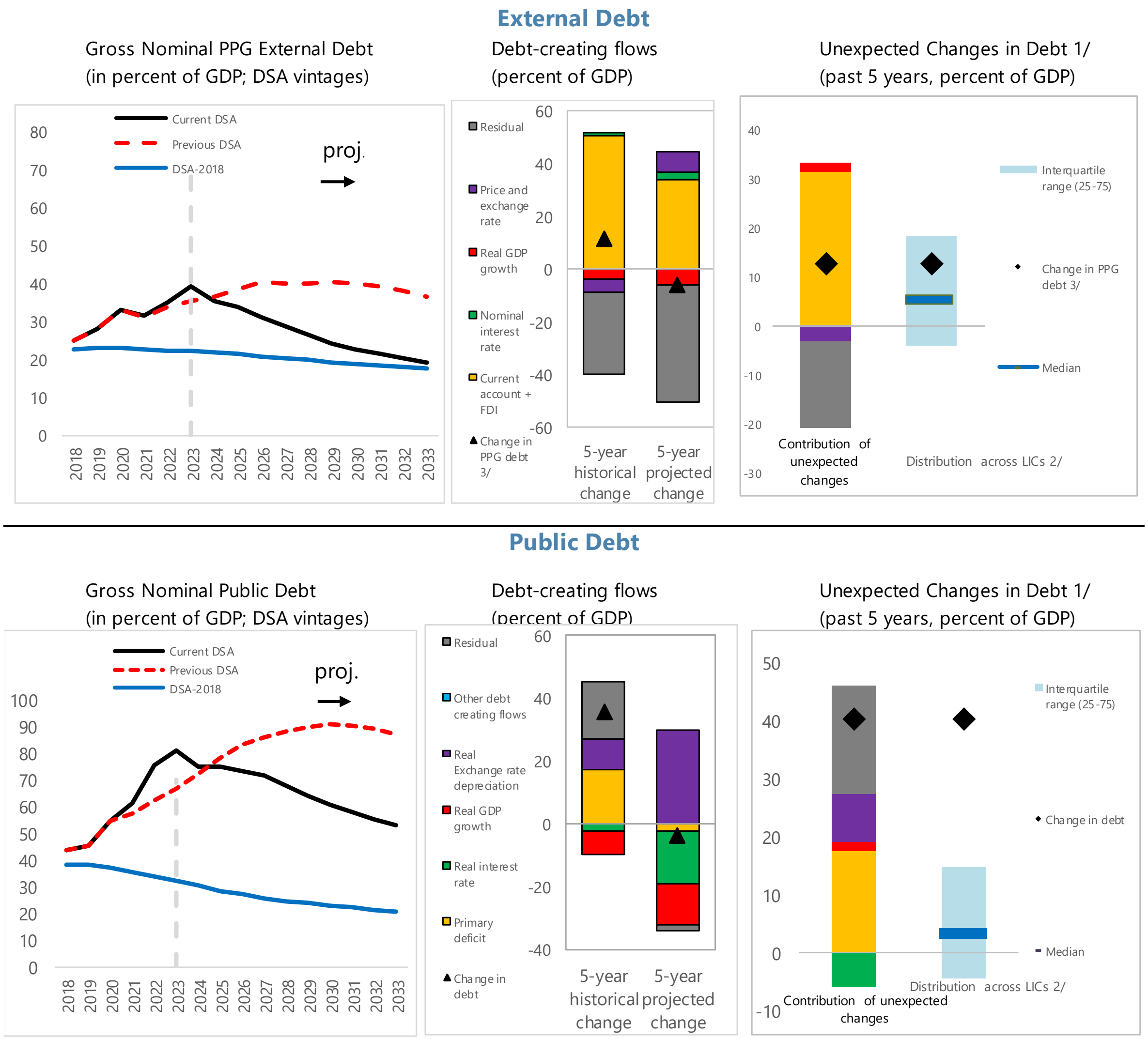
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	8%	8%
Domestic medium and long-term	78%	78%
Domestic short-term	14%	14%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	0.8%	0.8%
Avg. maturity (incl. grace period)	34	34
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	6.9%	6.9%
Avg. maturity (incl. grace period)	3	3
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	2.8%	2.8%

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

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Malawi: Drivers of Debt Dynamics (comparison to November 2022 DSA)

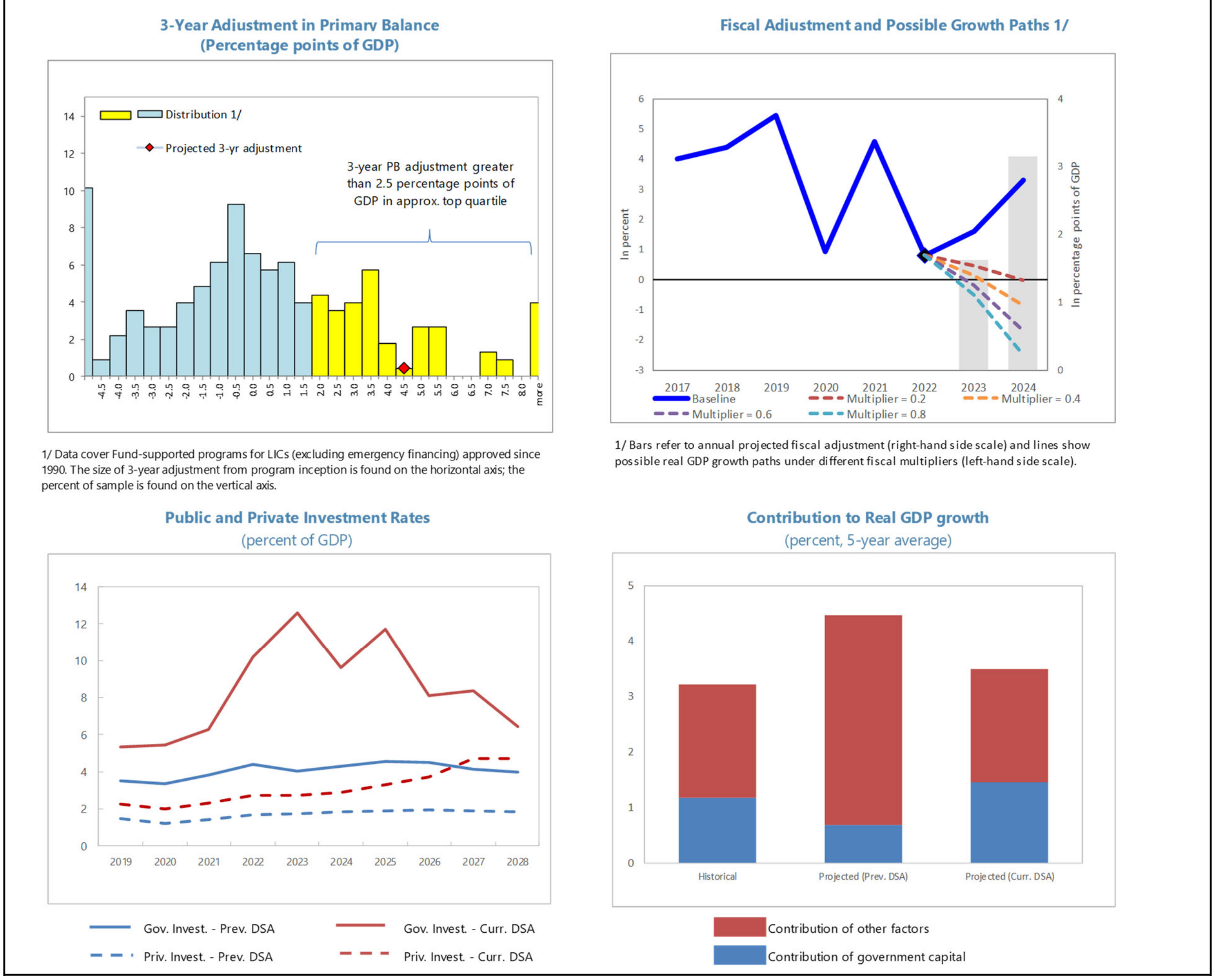


1/ Difference between anticipated and actual contributions on debt ratios.

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

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

Figure 4. Malawi: Realism Tools (comparisons to November 2022 DSA)



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

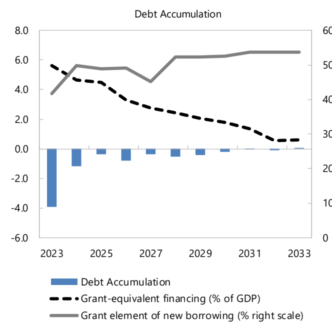
1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

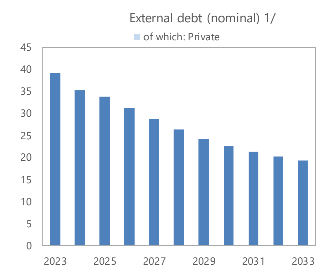
Table 1. Malawi: External Debt Sustainability Framework, Baseline Scenario, 2020–43

(Percent of GDP, Unless Otherwise Indicated)

	Actual			Projections												Average 8/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2043	Historical	Projections
External debt (nominal) 1/	32.9	31.5	34.8	39.3	35.2	33.8	31.2	28.8	26.3	24.2	22.6	21.3	20.2	19.2	12.2	26.3	27.5
of which: public and publicly guaranteed (PPG)	32.9	31.5	34.8	39.3	35.2	33.8	31.2	28.8	26.3	24.2	22.6	21.3	20.2	19.2	12.2	26.3	27.5
Change in external debt	5.1	-1.4	3.3	4.4	-4.1	-1.4	-2.6	-2.4	-2.5	-2.1	-1.6	-1.3	-1.2	-1.0	-1.3		
Identified net debt-creating flows	11.1	11.2	2.7	6.0	5.2	7.6	6.0	5.9	5.2	4.9	4.9	4.5	3.9	3.9	1.4	8.6	5.3
Non-interest current account deficit	13.6	13.8	2.8	5.8	6.6	9.2	7.9	8.0	7.2	6.9	6.9	6.5	6.0	6.0	3.2	10.8	7.0
Deficit in balance of goods and services	17.6	17.2	5.6	9.5	10.2	11.6	11.0	10.3	9.4	9.1	9.2	8.9	8.4	8.5	6.0	14.0	9.6
Exports	8.2	9.6	9.0	10.9	13.8	14.6	14.8	15.2	15.2	15.1	14.7	14.4	14.0	13.7	10.4		
Imports	25.8	26.7	14.6	20.4	24.0	26.3	25.8	25.4	24.7	24.2	23.8	23.3	22.4	22.2	16.5		
Net current transfers (negative = inflow)	-5.6	-4.9	-4.4	-5.2	-5.5	-4.4	-5.0	-4.1	-4.1	-4.1	-4.1	-4.2	-4.2	-4.2	-4.5	-4.8	-4.5
of which: official	-0.4	0.0	-0.6	-1.5	-1.2	-0.1	-0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other current account flows (negative = net inflow)	1.5	1.6	1.6	1.5	1.9	1.9	1.9	1.9	1.9	1.8	1.8	1.8	1.8	1.8	1.6	1.5	1.8
Net FDI (negative = inflow)	-0.8	-0.8	-0.3	-0.4	-0.5	-0.8	-0.8	-0.9	-1.0	-1.1	-1.1	-1.2	-1.3	-1.3	-1.4	-1.4	-1.0
Endogenous debt dynamics 2/	-1.7	-1.8	0.2	0.6	-0.8	-0.8	-1.1	-1.2	-1.0	-0.9	-0.9	-0.8	-0.8	-0.7	-0.5		
Contribution from nominal interest rate	0.2	0.3	0.3	1.2	0.7	0.6	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.1		
Contribution from real GDP growth	-0.2	-1.4	-0.3	-0.5	-1.5	-1.3	-1.4	-1.3	-1.3	-1.1	-1.1	-1.0	-0.9	-0.9	-0.6		
Contribution from price and exchange rate changes	-1.7	-0.7	0.1	...	...	...	...	...	...	...	...	...	...	...	...		
Residual 3/	-6.0	-12.6	0.6	-1.6	-9.3	-9.0	-8.6	-8.3	-7.6	-6.9	-6.5	-5.8	-5.1	-4.9	-2.7	-7.0	-6.7
of which: exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators																	
PV of PPG external debt-to-GDP ratio	...	...	24.3	19.5	21.4	20.9	19.5	18.1	16.6	15.2	14.2	13.4	12.5	11.9	7.4		
PV of PPG external debt-to-exports ratio	...	...	269.9	178.8	154.8	142.8	131.3	118.8	108.9	101.0	96.5	92.8	89.2	86.4	71.0		
PPG debt service-to-exports ratio	7.2	6.8	11.9	58.1	26.1	18.8	18.0	12.8	10.8	10.1	9.5	8.3	8.6	7.8	5.4		
PPG debt service-to-revenue ratio	4.6	4.9	7.8	46.9	25.4	18.2	17.1	11.9	9.7	9.0	8.2	7.0	7.1	6.2	13.9		
Gross external financing need (Billion of U.S. dollars)	1.6	1.8	0.5	1.5	1.1	1.3	1.1	1.1	1.0	1.0	1.0	1.0	1.0	1.0	0.8		
Key macroeconomic assumptions																	
Real GDP growth (in percent)	0.9	4.6	0.8	1.6	3.3	3.8	4.3	4.5	4.6	4.6	4.6	4.6	4.6	4.6	4.6	3.6	4.1
GDP deflator in US dollar terms (change in percent)	6.4	0.7	-0.3	3.0	-17.1	-3.0	-1.1	1.1	1.1	1.3	1.3	1.1	1.3	1.3	4.5	0.8	-0.9
Effective interest rate (percent) 4/	0.7	1.0	1.1	3.5	1.5	1.6	0.9	0.6	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.9	1.2
Growth of exports of G&S (US dollar terms, in percent)	-19.2	23.4	-5.4	26.6	8.6	6.5	4.7	8.2	5.9	5.0	3.1	3.5	3.3	3.4	3.8	-1.1	7.2
Growth of imports of G&S (US dollar terms, in percent)	0.3	9.2	-44.9	46.0	0.6	10.1	1.4	4.1	2.5	3.7	4.5	3.2	2.0	4.7	3.2	-0.5	7.6
Grant element of new public sector borrowing (in percent)	...	...	...	41.7	49.8	48.8	49.1	45.1	52.4	52.2	52.7	53.7	53.7	53.7	53.7	...	50.3
Government revenues (excluding grants, in percent of GDP)	12.8	13.2	13.8	13.5	14.2	15.1	15.6	16.4	16.9	17.0	17.1	17.1	17.1	17.0	4.0	13.3	16.1
Aid flows (in Billion of US dollars) 5/	0.4	0.4	0.7	0.8	0.6	0.5	0.4	0.4	0.3	0.3	0.3	0.3	0.2	0.2	0.2		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	5.6	4.6	4.5	3.3	2.8	2.4	2.0	1.8	1.4	0.6	0.6	0.4	...	2.7
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	77.7	80.4	77.3	79.3	80.9	89.6	85.4	79.6	74.6	53.7	53.7	53.7	...	75.7
Nominal GDP (Billion of US dollars)	12	12	13	13	11	11	12	12	13	14	15	15	16	17	32		
Nominal dollar GDP growth	7.4	5.3	0.5	4.7	-14.4	0.7	3.2	5.6	5.8	5.9	5.9	5.7	5.9	5.9	9.3	4.5	3.2
Memorandum items:																	
PV of external debt 7/	...	...	24.3	19.5	21.4	20.9	19.5	18.1	16.6	15.2	14.2	13.4	12.5	11.9	7.4		
In percent of exports	...	...	269.9	178.8	154.8	142.8	131.3	118.8	108.9	101.0	96.5	92.8	89.2	86.4	71.0		
Total external debt service-to-exports ratio	7.2	15.2	11.9	58.1	26.1	18.8	18.0	12.8	10.8	10.1	9.5	8.3	8.6	7.8	5.4		
PV of PPG external debt (in Billion of US dollars)			3.0	2.6	2.4	2.4	2.3	2.2	2.2	2.1	2.1	2.1	2.1	2.1	2.4		
(PVt-PVt-1)/GDPt-1 (in percent)				-3.9	-1.2	-0.4	-0.8	-0.4	-0.5	-0.4	-0.2	-0.1	-0.1	0.0	0.1		
Non-interest current account deficit that stabilizes debt ratio	8.5	15.2	-0.5	1.4	10.6	10.6	10.6	10.4	9.7	8.9	8.5	7.8	7.1	6.9	4.5		

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





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g) + Ɛα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ɛ=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

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

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

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

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

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

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

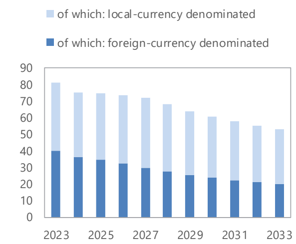
Table 2. Malawi: Public Sector Debt Sustainability Framework, Baseline Scenario, 2020–43

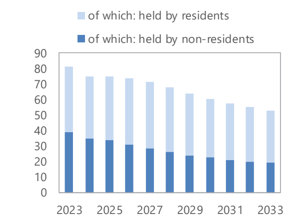
(Percent of GDP, Unless Otherwise Indicated)

	Actual			Projections								Average 6/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Projections
Public sector debt 1/	54.8	61.5	75.7	81.3	75.0	74.8	73.5	71.8	68.0	52.9	24.2	**46.3**	**66.8**
of which: external debt	32.9	31.5	34.8	39.3	35.2	33.8	31.2	28.8	26.3	19.2	12.2	**26.3**	**27.5**
Change in public sector debt	9.5	6.8	14.1	5.6	-6.3	-0.2	-1.3	-1.8	-3.7	-2.4	-1.6		
Identified debt-creating flows	7.1	2.7	7.1	-10.0	-11.9	-3.9	-3.0	-3.3	-4.6	-3.2	-1.4	**2.2**	**-5.1**
Primary deficit	5.0	4.6	4.6	3.0	-0.1	0.1	-2.3	-2.8	-4.3	-2.6	-0.6	**2.5**	**-2.1**
Revenue and grants	14.5	15.0	17.3	18.0	17.7	18.4	18.1	18.6	19.0	17.0	4.0	**15.5**	**18.1**
of which: grants	1.8	1.9	3.6	4.5	3.5	3.2	2.5	2.2	2.1	0.0	0.0		
Primary (noninterest) expenditure	19.5	19.6	22.0	21.0	17.6	18.4	15.8	15.8	14.7	14.4	3.4	**18.0**	**16.0**
Automatic debt dynamics	2.1	-1.9	2.5	-13.0	-11.8	-4.0	-0.7	-0.4	-0.3	-0.6	-0.8		
Contribution from interest rate/growth differential	1.3	-3.3	-4.8	-13.0	-11.8	-4.0	-0.7	-0.4	-0.3	-0.6	-0.8		
of which: contribution from average real interest rate	1.7	-0.9	-4.3	-11.9	-9.2	-1.2	2.4	2.7	2.9	1.8	0.4		
of which: contribution from real GDP growth	-0.4	-2.4	-0.5	-1.2	-2.6	-2.7	-3.1	-3.2	-3.2	-2.4	-1.1		
Contribution from real exchange rate depreciation	0.8	1.3	7.3	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	**0.0**	**0.0**
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	2.4	4.1	7.0	15.7	5.7	3.7	1.7	1.5	0.8	0.8	-0.2	**2.5**	**3.0**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	67.3	69.4	63.5	63.1	62.3	61.5	58.6	45.8	19.3		
PV of public debt-to-revenue and grants ratio	...	...	388.5	386.6	358.5	343.7	345.3	329.9	308.7	268.6	477.7		
Debt service-to-revenue and grants ratio 3/	24.9	18.7	35.9	99.6	92.6	120.8	107.3	120.8	106.3	98.6	160.1		
Gross financing need 4/	8.6	7.4	10.9	20.9	16.3	22.3	17.1	19.7	15.9	14.2	5.8		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	0.9	4.6	0.8	1.6	3.3	3.8	4.3	4.5	4.6	4.6	4.6	**3.6**	**4.1**
Average nominal interest rate on external debt (in percent)	0.7	0.6	1.1	3.8	2.1	1.8	1.0	0.6	0.8	0.8	0.8	**0.9**	**1.3**
Average real interest rate on domestic debt (in percent)	11.5	3.0	0.8	-13.0	-5.1	6.4	11.6	11.2	10.6	8.5	8.7	**8.3**	**6.1**
Real exchange rate depreciation (in percent, + indicates depreciation)	4.0	5.9	25.7	...	...	...	...	...	...	...	...	**12.7**	**...**
Inflation rate (GDP deflator, in percent)	6.3	8.2	17.3	28.4	25.1	13.5	7.6	6.4	5.8	5.7	5.7	**14.8**	**10.5**
Growth of real primary spending (deflated by GDP deflator, in percent)	21.2	5.0	12.9	-3.0	-13.4	8.9	-10.8	4.7	-2.6	4.8	-74.1	**6.3**	**0.4**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-4.5	-2.2	-9.5	-2.6	6.1	0.3	-1.0	-1.1	-0.6	-0.2	1.0	**-5.4**	**0.0**
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

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

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central government, central bank . Definition of external debt is Residency-based.

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

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

4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Malawi: Sensitivity Analysis for Key Indicators of PPG External Debt, 2023–33
(Percent)

	Projections 1/										
	2023	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**	**2033**
PV of debt-to GDP ratio											
Baseline	19	21	21	19	18	17	15	14	13	13	12
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	19	18	17	17	17	18	18	19	21	22	24
B. Bound Tests											
B1. Real GDP growth	19	22	22	21	19	18	16	15	14	13	13
B2. Primary balance	19	22	21	20	19	17	16	15	15	14	13
B3. Exports	19	23	26	25	23	21	20	19	18	17	16
B4. Other flows 3/	19	23	23	22	20	19	17	16	15	14	13
B5. Depreciation	19	29	24	23	21	19	17	16	15	14	13
B6. Combination of B1-B5	19	22	22	20	19	17	16	15	14	13	12
C. Tailored Tests											
C1. Combined contingent liabilities	19	22	21	20	19	18	16	16	15	14	14
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	19	21	21	19	18	17	15	14	13	13	12
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	**179**	**155**	**143**	131	119	109	101	96	93	89	86
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**179**	131	119	115	113	115	121	132	**144**	**159**	**176**
B. Bound Tests											
B1. Real GDP growth	**179**	**155**	**143**	131	119	109	101	96	93	89	86
B2. Primary balance	**179**	**156**	**146**	135	123	114	107	104	101	98	96
B3. Exports	**179**	**215**	**283**	**264**	**242**	**225**	**212**	**205**	**198**	**190**	**184**
B4. Other flows 3/	**179**	**164**	**157**	**145**	132	122	114	110	106	102	98
B5. Depreciation	**179**	**155**	125	113	102	92	84	80	76	73	71
B6. Combination of B1-B5	**179**	**200**	**153**	**195**	**177**	**163**	**152**	**146**	**140**	135	131
C. Tailored Tests											
C1. Combined contingent liabilities	**179**	**158**	**147**	136	125	116	109	106	103	101	99
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	**179**	**155**	**143**	131	119	109	101	96	93	89	86
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	**58.1**	**26.1**	**18.8**	**18.0**	**12.8**	**10.8**	**10.1**	9.5	8	9	8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**58**	**21**	**15**	**14**	**10**	9	9	8	8	9	9
B. Bound Tests											
B1. Real GDP growth	**58**	**26**	**19**	**18**	**13**	**11**	**10**	10	8	9	8
B2. Primary balance	**58**	**26**	**19**	**18**	**13**	**11**	**10**	10	8	9	8
B3. Exports	**58**	**34**	**31**	**30**	**22**	**18**	**17**	**16**	**15**	**17**	**16**
B4. Other flows 3/	**58**	**26**	**19**	**18**	**13**	**11**	**10**	10	9	9	9
B5. Depreciation	**58**	**26**	**19**	**18**	**13**	**11**	10	9	8	7	7
B6. Combination of B1-B5	**58**	**31**	**26**	**25**	**18**	**15**	**14**	**13**	**13**	**13**	**12**
C. Tailored Tests											
C1. Combined contingent liabilities	**58**	**26**	**19**	**18**	**13**	**11**	**10**	10	8	9	8
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	**58**	**26**	**19**	**18**	**13**	**11**	**10**	10	8	9	8
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	**47**	**25**	**18**	**17**	12	10	9	8	7	7	6
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**47**	**21**	**14**	13	10	8	8	7	7	7	7
B. Bound Tests											
B1. Real GDP growth	**47**	**26**	**19**	**18**	13	10	10	9	7	8	7
B2. Primary balance	**47**	**25**	**18**	**17**	12	10	9	8	7	7	6
B3. Exports	**47**	**26**	**19**	**18**	13	10	10	9	8	9	8
B4. Other flows 3/	**47**	**25**	**18**	**17**	12	10	9	8	8	8	7
B5. Depreciation	**47**	**34**	**24**	**23**	**16**	13	12	11	9	8	7
B6. Combination of B1-B5	**47**	**24**	**18**	**17**	12	9	9	8	7	7	6
C. Tailored Tests											
C1. Combined contingent liabilities	**47**	**25**	**18**	**17**	12	10	9	8	7	7	6
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	**47**	**25**	**18**	**17**	12	10	9	8	7	7	6
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	14	14	14	14	14	14	14	14	14	14	14

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

Table 4. Malawi: Sensitivity Analysis for Key Indicators of Public Debt, 2023–33
(Percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
PV of Debt-to-GDP Ratio											
Baseline	**69**	**63**	**63**	**62**	**61**	**59**	**55**	**52**	**50**	**48**	**46**
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**69**	**71**	**71**	**70**	**69**	**66**	**63**	**60**	**57**	**54**	**52**
B. Bound Tests											
B1. Real GDP growth	**69**	**66**	**68**	**68**	**68**	**66**	**64**	**61**	**60**	**58**	**57**
B2. Primary balance	**69**	**68**	**71**	**71**	**70**	**67**	**64**	**61**	**59**	**56**	**54**
B3. Exports	**69**	**65**	**68**	**67**	**66**	**63**	**60**	**57**	**54**	**52**	**49**
B4. Other flows 3/	**69**	**65**	**65**	**64**	**64**	**61**	**57**	**54**	**52**	**50**	**47**
B5. Depreciation	**69**	**64**	**62**	**61**	**59**	**56**	**53**	**49**	**46**	**44**	**41**
B6. Combination of B1-B5	**69**	**65**	**65**	**64**	**63**	**60**	**56**	**53**	**51**	**49**	**47**
C. Tailored Tests											
C1. Combined contingent liabilities	**69**	**73**	**73**	**72**	**72**	**69**	**66**	**63**	**60**	**58**	**56**
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	**69**	**64**	**60**	**56**	**53**	**50**	**46**	**44**	**43**	**41**	**40**
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
TOTAL public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
PV of Debt-to-Revenue Ratio											
Baseline	387	359	344	345	330	309	297	286	280	281	269
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	387	392	384	389	372	354	345	334	325	319	303
B. Bound Tests											
B1. Real GDP growth	387	368	366	373	362	345	338	333	333	342	334
B2. Primary balance	387	381	388	391	375	353	342	332	327	331	318
B3. Exports	387	368	369	371	354	332	320	309	303	304	290
B4. Other flows 3/	387	367	356	357	341	320	308	296	291	292	278
B5. Depreciation	387	364	341	338	320	298	283	269	260	257	242
B6. Combination of B1-B5	387	370	355	354	338	316	303	290	285	287	275
C. Tailored Tests											
C1. Combined contingent liabilities	387	414	398	401	384	362	351	341	336	340	328
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	387	361	330	317	293	268	254	246	242	243	234
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Debt Service-to-Revenue Ratio											
Baseline	100	93	121	107	121	106	113	103	103	103	99
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	100	99	130	113	124	109	115	107	106	104	96
B. Bound Tests											
B1. Real GDP growth	100	95	127	114	131	118	127	119	121	125	122
B2. Primary balance	100	93	127	124	143	126	132	123	122	123	118
B3. Exports	100	93	121	108	121	107	113	103	104	105	100
B4. Other flows 3/	100	93	121	107	121	106	113	103	104	104	99
B5. Depreciation	100	90	117	103	115	101	108	98	97	98	93
B6. Combination of B1-B5	100	91	119	110	127	112	116	106	107	108	103
C. Tailored Tests											
C1. Combined contingent liabilities	100	93	136	133	149	127	137	126	125	127	122
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	100	93	114	97	106	92	97	89	89	89	86
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

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

INTERNATIONAL MONETARY FUND

MALAWI

November 8, 2023

SECOND REVIEW UNDER THE STAFF-MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT AND REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—INFORMATIONAL ANNEX

Prepared By

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

CONTENTS

FUND RELATIONS

(As of October 1, 2023)

Membership Status

Joined: July 19, 1965; Article VIII

General Resources Account:

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

SDR Department:

	SDR Million	%Allocation
Net cumulative allocation	199.40	100.00
Holdings	2.27	1.14

Outstanding Purchases and Loans:

	SDR Million	%Quota
RCF Loans	208.15	149.96
ECF Arrangements	108.49	78.16

Latest Financial Commitments:

Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF	04/30/2018	09/24/2020[1]	105.84	53.85
ECF	07/23/2012	06/29/2017	138.80	138.80
ECF	02/19/2010	07/22/2012	52.05	13.88

Outright Loans:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
RCF	11/21/2022	11/23/2022	69.40	69.40
RCF	10/02/2020	10/06/2020	72.31	72.31
RCF	05/01/2020	05/05/2020	66.44	66.44

[1] Undrawn outright disbursements (RFI and RCF) expire automatically 60 days following the date of commitment, i.e. Board approval date.

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

	2023	2024	2025	2026	2027
Principal	9.79	23.11	33.46	47.84	40.47
Charges/Interest	2.02	8.02	8.02	8.02	8.02
Total	11.81	31.13	41.48	55.86	48.49

Implementation of HIPC Initiative:

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

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

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

Implementation of Multilateral Debt Relief Initiative (MDRI):

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

Debt Relief by Facility (SDR Million)

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

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

Implementation of Catastrophe Containment and Relief (CCR)[1]**:**

Date of Catastrophe	**Board Decision Date**	**Amount Committed** (SDR million)	**Amount Disbursed** (SDR million)
N/A	04/13/2020	7.20	7.20
N/A	10/02/2020	7.20	7.20
N/A	04/01/2021	7.81	7.81
N/A	10/06/2021	6.72	6.72
N/A	12/15/2021	3.91	3.91

[1] As of February 4, 2015, the Post-Catastrophe Debt Relief Trust has been transformed to the Catastrophe Containment and Relief (CCR) Trust.

Safeguards Assessments:

The most recent safeguards assessment was conducted in 2021, in connection with financing under the Rapid Credit Facility approved in 2020. It found significant deterioration of safeguards at the RBM since the 2018 assessment. Governance arrangements at the RBM and the internal control environment are in need of reforms, which should, inter alia, establish the Board as the RBM's main decision-making body responsible for oversight and policy formulation, introduce collegiality in executive management, and strengthen aspects of RBM’s autonomy. Other recommendations related to the need to strengthen the RBM’s foreign reserves management policy, internal audit and financial reporting practices, and the risk management framework. The RBM is making progress in addressing the recommendations and has recently adopted a risk management policy and aligned procedures for market operations with the RBM Act. A revised framework for management of foreign reserves has been prepared and submitted for endorsement by the Board. Staff continues the engagement on the remaining recommendations, including the legal amendments and external audit verification of NIR.

Exchange Arrangements:

In May 2012, the government liberalized the foreign exchange regime, devalued the kwacha by about 33 percent, and adopted a de jure floating exchange rate regime. However, the U.S. dollar exchange rates have shown remarkable stability since October 2016. Accordingly, the de facto exchange rate arrangement is classified as "stabilized". Inflows of foreign exchange and swap arrangements have allowed for increase in international reserves until 2020. The RBM reintroduced in August 2021 a surrender requirement to address foreign exchange shortages which is treated as a temporary measure to address extraordinary circumstances and should be lifted as conditions improve. In May 2022, kwacha was devalued by 25 percent to correct for a large real exchange rate overvaluation.

In September 2023, staff conducted a review of Malawi's exchange system with regard to its compliance with members' obligations under Article VIII, Sections 2(a), 3, and 4 of the IMF's Articles of Agreement. The assessment took stock of important changes to the exchange system since the last assessment (2006). The assessment found that official actions resulted in four multiple currency practices (MCP) subject to Fund jurisdiction. (1) The first MCP stems from a deviation of more than 2 percent between the rate used by FX bureaus for electronic (spot) transactions and the respective rates used by the RBM in spot transactions. (2) The second MCP arises from a deviation of more than 2 percent between some of the accepted bids of the auction and the rates used in all other RBM spot operations conducted on the same day, including other accepted auction bids. [2]
(3) The third MCP stems from the spread between the rate used by the RBM for the tobacco surrender requirement in the days following a recent auction, when the RBM continues to use the lower, pre-auction indicative selling price prevailing on a previous day, and other exchange rates used by the RBM in spot operations. (4) The fourth MCP arises from the spread between the rate used by FX bureaus and the rates used by Authorized Dealer Banks. These MCPs will be assessed under the new MCP policy once it comes into effect on February 1, 2024.

In addition, Malawi maintains three foreign exchange restrictions. (1) The first restriction arises from unavailability and undue delays in accessing FX for current payments and transfers due to the authorities' rationing and limiting exchange rate adjustment. (2) The second restriction relates to a ban on accessing foreign exchange for unrelated current international transactions by customers who fail to comply with advance payment requirements. (3) The third restriction stems from the requirement to provide a tax clearance certificate prior to permitting transfers for certain current transactions.

[2] The auction does not comply with best practices, as the RBM failed to adjudicate one auction and, in another, rejected some bids reflecting market prices, thus failing to purchase the full allocation. As a result, the MCP policy requires the spreads related to the auction to be assessed.

Article IV Consultation:

The Executive Board concluded the last Article IV consultation with Malawi on December 13, 2021.

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

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

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

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

Technical Assistance: (since 2015, as of October 2023)

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
07/23	AFE	RBM	Develop/strengthen insurance companies' regulation and supervision frameworks	Mission/Virtual
07/23	AFE	RBM	Review the developed draft Basel III guidelines and templates	Mission
06/23	FAD	MRA	Provide support to the authorities on using the FAD's Discrete Guarantees and Loans Assessment Tool (DGLAT)	Mission
06/23	FAD	MRA	Review and update the budget calendar and budgeting manual	Mission
05/23	FAD	MRA	Strengthen MRA's risk management capability through data matching and analysis	Mission
04/23	STA	NSO	Assist with developing export and import price indexes (XMPIs)	Mission
01/23	FAD	MRA	VAT rationalization	Mission
12/22	AFE	MRA	Budget baseline costing and performance budgeting	Workshop
11/22	AFE	RBM	Forecasting and Policy Analysis System (FPAS)	Mission
09/22	FAD	MRA	Strengthen the management of MRA's tax arrear's function and improve debt management capacity	Mission
08/22	MCM	RBM	Enhance the RBM's understanding of systematic risk in domestic systematically important banks	Mission
08/22	FAD	MRA	Review the deployment of new Information Tax Administration System (ITAS)	Virtual Mission
07/22	FAD	MRA	Review the Revenue Mobilization Thematic Fund (RMTF) project	Mission
07/22	FAD	MRA	Review MRA's proposed organizational design for the Domestic Tax Division	Virtual Mission
06/22	FAD	MRA	Assess the effectiveness of the tax audit program	Virtual Mission
05/22	AFE	MOF	Strengthen project appraisal and selection techniques	Mission
05/22	FAD	MRA	Tax Administration Diagnostic Assessment Tool training workshop	Virtual Mission

Date of Delivery	Department	Ministry/Agency	Purpose/Topic	Modality
05/22	AFE	MOF	Strengthen the credibility and reliability of the Public Sector Investment Plan document	Mission
04/22	AFE	MRA	Strengthen MRA's investigations capacity and customs administration	Workshop
04/22	AFE	NSO	Designing new IIP and PPI bulletin	Virtual Mission
04/22	MCM	RBM	Basel III framework with a focus on credit, operational and liquidity risk	Virtual Mission
04/22	STA	MOF	Improve the quality of fiscal data for the consolidated general government	Virtual Mission
04/22	STA	NSO	Improve the quality and timeliness of external sector statistics	Virtual Mission
03/22	AFE	RBM	Review the key components of FPAS	Virtual Mission
02/22	FAD	MRA	Strengthen revenue administration	Virtual Mission
11/21	AFE	MOF	Strengthen SOE analysis	Virtual Mission
11/21	FAD	MOF	Supporting implementation of a new ITAS	Virtual Mission
11/21	AFE	MOF	Improving quality of general government fiscal data	Virtual Mission
11/21	AFE	NSO	Compilation of GDP expenditure and production	Virtual Mission
09/21	AFE	NSO	Finalize new weights and update the CPI basket	Virtual Mission
09/21	AFE	MOF	Using tax data for GDP compilation	Virtual Mission
09/21	FAD	MOF	Developing a VAT compliance improvement plan	Virtual Mission
09/21	FAD	MOF	Integrating performance budgeting and IT systems	Virtual Mission
09/21	FAD	MOF	Excise management	Virtual Mission
08/21	AFE	MOF	Strengthening project appraisal and selection	Virtual Mission
07/21	AFE	NSO	Continued compilation of GDP expenditure	Virtual Mission
07/21	FAD	MOF	Audit of high risk sectors for VAT	Virtual Mission
06/21	STA	NSO	CPI Update	Virtual Mission
05/21	MCM	RBM	Principles for financial market infrastructures training	Workshop
05/21	MCM	RBM	Review of oversight framework	Workshop
04/21	STA	RBM	Monetary and financial statistics	Virtual Mission
04/21	FAD	MOF	Strengthen excise management	Virtual Mission
03/21	STA	RBM	External sector statistics	Virtual Mission

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

(As of October 2023)

- World Bank Group
  https://www.worldbank.org/en/country/malawi/overview

- African Development Bank
  https://www.afdb.org/en/countries/southern-africa/malawi

- AFRITAC East
  https://www.eastafritac.org

STATISTICAL ISSUES

As of October 1, 2023

I. Assessment of Data Adequacy for Surveillance and Program Monitoring
General: Data provision has shortcomings that are serious and significantly hamper surveillance. Most affected areas are: national accounts, fiscal, monetary and external sector statistics.
National Accounts: GDP was rebased from 2010 to 2017, with 2017 figures published for GDP by production only. Malawi's nominal GDP for 2017 was revised upwards by 38.4 percent from MK4,635.4 billion (US$6.35 billion) in the 2010 base year to MK6,417.3 billion (US$8.8 billion) in the 2017 base year. Since then, the GDP estimates have been revised further with technical assistance missions to the National Statistics Office (NSO) focusing on compiling GDP by expenditure and resolving several inconsistencies in GDP by production and expenditure. NSO has not yet published the finalized numbers for both production and expenditure.
Price Statistics: The NSO compiles and disseminates a monthly CPI with weights based on expenditure data from the 5th Integrated Household Survey (IHS5), conducted from April 2019 to April 2020. The producer price index (PPI) is based on weights derived from the results of the Census of Economic Activity conducted during 2016-2017. These data are now more than five years old and the weights should be updated. There is also a need to expand index coverage to include other economic activities, to better reflect the current structure of the economy. With support from STA, the NSO is in the process of developing export-import price indexes.
Government Finance Statistics: The authorities compile and disseminate GFS for budgetary central government (BCG), which is aligned with the Government Finance Statistics Manual 2014 (GFSM 2014). Efforts have been in place to expand the coverage to General Government. The authorities have implemented a new Integrated Financial Management Information System (IFMIS) which covers most of the central government transactions. However, data quality problems still remain: • Due primarily to differences in coverage, published data for the BCG show a sizeable statistical discrepancy between above and below the line data. The coverage of government for above the line data is considerably narrower than the information on financing reported by RBM. • While tax revenue data are received in a timely fashion, it is not always possible to reconcile them with deposits in the Malawi Government Account. This is a result of the way taxes are reported, and timing differences between receipt of taxes and cleared funds being available

for the government. The finances and operations of the Malawi Revenue Authority are also unusually opaque. Nontax revenue, including capital revenues collected by line ministries, is not properly accounted for in the fiscal reports prepared by the Ministry of Finance.

- Interest payments are currently reported on a currency basis rather than based on the residency of the holder of the security.

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. The new IFMIS which started in July 2021, has been rolled out to all MDAs except for two by the end of August 2023, and authorities are working to produce comprehensive fiscal reports using the new system. The authorities are currently working with East AFRITAC to modify the chart of accounts and output-based structures so that they could more easily be realigned to the national strategy and be more readily understood.

Annual government finance data for the BCG and Local governments in a GFSM 2014 presentation are reported for publication in the Government Finance Statistics Yearbook (GFSY). However, these data are not disseminated domestically. STA TA missions have encouraged the authorities to compile and report high frequency data for BCG in GFSM 2014 framework and assisted them in compiling data for extrabudgetary units with the objective of expanding coverage to general government.

Monetary and Financial Statistics: The Reserve Bank of Malawi (RBM) is compiling and reporting monetary data to STA using standardized report forms (SRFs). On April and May 2021, STA provided a TA mission to RBM to address outstanding issues in SRF and RBM has moved completely to reporting in SRFs.

External sector statistics (ESS): The NSO compiles annual trade and balance of payment (BOP) data. Previously trade data submission had more than nine months of lag, and the latest available Balance of Payment (BOP) data is for 2021. The international investment position (IIP) data is available up to 2021. The ESS data are compiled annually and more timely and higher frequency data would significantly improve the staff's work on projection and macroeconomic framework of the external sector development. The ESS mission conducted by STA in March 2021 focused on improvements of the coverage, compilation, and timeliness of goods trade data, along with assessment of the BOP and IIP data compilation to follow up a previous TA mission. The mission noted the issues in areas of source data collections as well as physical and human resource capacity. In response to the recommendations of the 2021 TA mission the NSO has increased its ESS compilation unit by at least 2 persons. These new staff can undergo some training in ESS compilation in the forthcoming 2024 TA mission.

As of October 31, 2021, the NSO provided goods trade data up to March 2021. The timeliness of dissemination of the trade data needs to be accelerated to (at least) within two months from

the end of a reference month as the STA mission recommended, especially given that no reliable BOP data is available. The daily exchange rate data, monthly international reserves data as well as the FXI data are regularly reported from the Reserve Bank of Malawi (RBM). The reported international reserves data follow closely the data template on International Reserves and Foreign Currency Liquidity (IRFCL). The RBM started to submit a daily FX cashflow table on a regular basis. Regarding the external debt data, the government of Malawi (GOM) now provides granular breakdowns on top of the end-year stock data. In the current conjuncture of Malawi's extremely vulnerable position to the external sector, reliable and timely ESS reporting is essential for diagnoses of any developments in the external sector. To move forward with improvements, the NSO, RBM and the GOM should coordinate further and take appropriate steps to implement TA recommendations to ensure a regular and more frequent flow of data from this system for trade, BOP and IIP compilation; and the government should allocate sufficient resources for conducting regular surveys.	
II. Data Standards and Quality	
Malawi implemented the e-GDDS and its National Summary Data Page (NSDP) went live on November 15, 2016 (http://cb.malawi.opendataforafrica.org/uwkhibc/national-summary-data-page-nsdp). The authorities are aiming at improving performance against the timeliness benchmarks that they have set under the e-GDDS.	Data ROSC was published on February 17, 2005.

INTERNATIONAL MONETARY FUND

MALAWI

SECOND REVIEW UNDER THE STAFF-MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT AND REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—SUPPLEMENTARY INFORMATION

November 10, 2023

Approved By
Costas Christou (AFR) and Bjoern Rother (SPR)

Prepared by the African Department in consultation with the Strategy, Policy, and Review Department

This supplement provides additional information since the issuance of the Staff Report (EBS/23/114) issued on November 8, 2023. The information does not alter the thrust of the staff appraisal.

This supplement includes a proposed decision approving Malawi's exchange measures as well as a proposed decision approving a four-year arrangement under the Extended Credit Facility as well as the text of such ECF arrangement in an attachment to this Supplement.

FINANCING ASSURANCES

1. As foreseen in the staff report, Staff's assessment is that there are sufficient assurances regarding the debt restructuring needed to restore debt sustainability and generate financing consistent with program parameters.

2. With the provision of the financing assurances from official bilateral creditors, the thrust of the staff appraisal contained in the staff report remains appropriate and staff recommends approval of the arrangement under the Extended Credit Facility.

POLICY DEVELOPMENTS

3. The Reserve Bank of Malawi (RBM) adjusted the exchange rate from the selling rate of MWK 1180.29 to a selling rate of MWK 1700.00 to the US Dollar with effect from November 9, 2023.

4. The RBM met the outstanding prior action of announcing operational changes to the foreign exchange market. The changes announced are: (i) authorized dealer banks (ADBs) are permitted to freely negotiate exchange rates to trade with their clients and amongst themselves, notwithstanding any limitations previously in place. (ii) The Bank will buy and sell FX in a transparent manner through competitive auctions at market determined prices, open to all ADBs in good standing and without restriction on the range or level of the exchange rate that participants can submit. Allotment will be determined according to prices submitted. (iii) Auctions to purchase FX with ADBs will switch from monthly to fortnightly. Sales will take place only as necessary to address disorderly market conditions.

IMPLICATIONS

5. The exchange rate adjustment is in line with staff advice and removes a major economic distortion. RBM would need to maintain its efforts to increase transparency, broaden participation and facilitate price discovery in the official exchange rate.

6. The impact of this change on growth, inflation, and the balance of payments has been factored in the macroeconomic framework and program design to the extent possible.

Statement by Mr. Willie Nakunyada, Executive Director for Malawi, Ms. Abigail Nainda, Senior Advisor to the Executive Director and Mr. Moeti Godfrey Damane, Advisor to the Executive Director

November 15, 2023

Introduction

1. Our Malawian authorities appreciate the productive policy dialogue with staff during the mission on the Second Review of the Staff Monitored Program with Executive Board Involvement (PMB). They also appreciate the candid negotiations with Fund staff on a new four-year Extended Credit Facility (ECF)-supported arrangement. More importantly, they are grateful to all creditors for their cooperation in extending the much-needed financing assurances for debt relief.

2. Malawi has experienced successive and severe shocks that set back the country's growth and development ambitions. Specifically, shocks from the COVID-19 pandemic, the global food crisis, and the devastating effects of recurrent tropical cyclones, have dampened growth performance and amplified macroeconomic imbalances. Despite the challenging domestic and external circumstances, the authorities have established a track record of macroeconomic adjustment and implementation of reforms, with satisfactory performance under the PMB to pave the way for transition to an Upper Credit Tranche (UCT)-quality arrangement. Importantly, the authorities have made progress on debt restructuring and will continue good faith negotiations with creditors. Nevertheless, Malawi remains a fragile country and growth prospects are presently subdued against the backdrop of protracted BOP challenges worsened by the interlocking shocks. **Within this context, the authorities request a new four-year ECF arrangement to consolidate progress achieved under the PMB and catalyze additional donor and trade financing.** In addition, Fund support under the ECF arrangement would be critical to restore macroeconomic stability, while fostering durable growth and poverty reduction to achieve the objectives of the Malawi 2063 vision.

Program Performance

3. Performance under the Second Review of the PMB has strengthened, as evidenced by the notable improvements in end-June 2023 targets when compared to the First Review. Specifically, five out of six end-June 2023 continuous quantitative targets (QTs) were met, as well as all three end-June 2023 Indicative Targets (ITs). However, the QT on the stock of monetary base was missed despite the RBM's efforts to mop up excess liquidity.

4. Seven out of ten Structural Benchmarks (SBs) were not met on time, but marked progress has been made on the missed SBs. The audited fiscal report of FY2021/22 was submitted to staff on time. Further, the notification for FY2022/23Q3 quarter allotment to the piloted Ministries, Departments and Agencies (MDAs) that is in line with the macroeconomic framework and allows for MDAs to commit up to the agreed threshold amounts through IFMIS was also met on time. The authorities also met the SB on the verification of arrears of national budget entities from July 1, 2020, to March 31, 2022, which was certified by the Auditor General, including compensations and utilities by end-December 2022. The SBs on the publication of monthly IFMIS-generated comprehensive fiscal reports and the operationalization of an executive Asset Liability Management Committee (ALCO) in accordance with recommendations of the 2021 Safeguards Assessment Report, were implemented with a delay.

5. The remaining SBs, including the amendments to the RBM Act as recommended by the 2021 safeguards assessment and Cabinet approval of the arrears' clearance and prevention strategy for

national budget entities were moved to SBs under the new ECF arrangement. Nonetheless, the authorities already prepared draft amendments to the RBM Act which they are currently discussing with staff, and they plan to submit the amendments to parliament as recommended. Meanwhile, the end-October 2023 SB on the publication the COVID-19 spending audit report, detailing the corrective actions and measures to pursue and respond to audit findings was shifted to a prior action for the ECF program.

6. Considering the satisfactory program performance and the fulfillment of prior actions undertaken amid a highly fragile context, **the authorities seek Executive Directors' support in completion of the second PMB review**.

Recent Economic Developments and Outlook

7. Real GDP growth is estimated to slow from 1.7 percent in 2022 to 1.6 percent in 2023, reflecting the constraining effects of recurrent foreign exchange shortages and tighter monetary policy. Nonetheless, stronger than expected performance in the tobacco sector moderated the growth decline. Going forward, growth prospects remain subject to adverse weather events, spillovers from the war in Ukraine, and subdued capital inflows. Inflation is expected to average 30.3 percent in 2023, representing an increase from 24.8 percent projected at the time of the First Review. Nevertheless, inflation is projected to start declining in 2024 partly owing to decisive monetary actions taken by RBM.

8. The current account deficit narrowed significantly from 14 percent of GDP in 2021 to 3.2 percent of GDP in 2022 partly due to a large exchange rate devaluation and import compression. Despite the large reduction in the current account deficit, reserve accumulation was limited, in part due to sizeable external debt service obligations. The current account deficit is, however, expected to widen to 7.6 percent of GDP in 2023 as foreign exchange market liquidity remains significantly tight. As a result, preliminary data shows that foreign exchange reserves remain under pressure and projected at 1.8 months by end 2023.

Fiscal Policy and Debt Management

9. Restoring fiscal discipline by enhancing revenue collection, managing expenditures, as well as improving transparency and monitoring of budget execution ranks high on the authorities' agenda. In this context, the authorities have aligned the FY2023/24 budget and the draft FY2024/25 budget that is currently in preparation, with the proposed ECF parameters. Specifically, the budget aligns spending with revenue projections to help contain domestic financing. At the same time, the authorities have adopted realistic revenue estimates along with the rationalization of spending, while protecting essential spending. Taken together, these efforts are expected to achieve a fiscal adjustment of about 1.9 percentage points of GDP in FY2023/24, resulting in a reduction of about 0.8 percentage points of GDP in the domestic primary deficit. Preliminary data suggest that the domestic primary fiscal balance is roughly on track to contain the overall deficit for FY2023/24 and FY2024/25, culminating in a decline to 11 percent of GDP and further to 8 percent of GDP, respectively. Should implementation risks crystalize, the authorities have developed a Contingency Plan to help close emerging financing gaps.

10. During FY2023/24, the authorities' plan to step up implementation of their Domestic Revenue Mobilization Strategy (DRMS). In this regard, they launched the DRMS in December 2021 to ramp up revenues by 5 percent of GDP over the five-year implementation horizon. To intensify implementation, they have incorporated the DRMS in the Malawi Revenue Authority's (MRA) strategic plan and in FY2022/23, they formulated a DRMS Monitoring Committee comprising

Ministry of Finance and Economic Affairs (MoFEA), MRA, the Accountant General, Immigration Department, Malawi Police Service and Registrar General. In this vein, they will continue with implementation of the tax policy and revenue measures already committed under the PMB. In addition, the authorities launched *Msonkho* online in December 2022, an Integrated Tax Administration System (ITAS) to strengthen tax administration, and all remaining modules will be completed by end-March 2024 (SB). Furthermore, the authorities plan to implement the Tax Administration Act and establish the Revenue Appeal Tribunal by December 2023.

11. To improve non-tax revenues, our authorities have implemented a host of measures, including ensuring that State-Owned Enterprises (SOEs) comply with the PFM Act by opening a holding account with the RBM; ensuring that MDAs remit non-tax revenue collection to the Malawi Government consolidated account (MG1) through their departmental receipts' accounts, and increasing some fees and charges to ensure that they reflect, where possible, full cost recovery. Additional increases to fees and charges are planned, as well as further measures, including automating the payment systems and business processes of the MDAs and enforcing the dividend and surplus policy.

12. On the expenditure front, the authorities plan to improve public spending efficiency to reduce non-critical spending. Specifically, they will continue to rationalize the Affordable Input Program (AIP), with the first phase of reform to the fertilizer and seed subsidy program already completed. They have also taken the necessary measures to prevent cost overruns in the AIP arising from escalating fertilizer prices and the Kwacha depreciation, including through increments to farmer contributions, while capping the government subsidy and fast-tracking beneficiary reforms. Concurrently, farmers at the lowest end of the income spectrum have been moved to social protection programs and those at the higher end of the spectrum to commercial agriculture programs, supported by development partners. Ultimately, the authorities aim to completely phase out the AIP. To manage the wage bill, the authorities are making efforts to rationalize public wage expenditure, with a freeze on new hiring into the public service and a Personnel Audit completed in 2021 to eliminate ghost workers. At the same time, they are taking additional measures geared to enhance the oversight of SOEs and implementation of the new IFMIS to strengthen budget execution and commitment control.

13. The authorities' efforts to seek debt restructuring and create sufficient borrowing space, are beginning to bear fruit. They have engaged with private creditors in good faith, by engaging in an early dialogue with them, sharing relevant information on a timely basis and providing them with an early opportunity to give input on the design of restructuring strategies. Specifically, the largest bilateral creditors, China and India, have provided specific and credible assurances that they will provide debt relief in line with program parameters. At the same time, regular discussions are continuing on good faith basis to resolve obligations to African Export–Import Bank (Afreximbank) and the Trade and Development Bank (TDB). Further, policy level meetings were recently held to reaffirm the need for debt restructuring terms consistent with the ECF program. The authorities will continue to rely on their strategy to build on key pillars to overcome current external debt challenges, including solvency and liquidity concerns. Going forward, they will continue to pursue negotiations with commercial and official bilateral creditors and commit that commercial debt will be repaid or restructured on terms that are consistent with the parameters of the ECF-supported arrangement.

14. The authorities will implement measures articulated in the MEFP, including through enhancing public debt management. In this regard, they have updated and published their Medium-Term Debt Strategy (MTDS) to consider on-budget externally and domestically financed projects either contracted or expected as reflected in the macro-fiscal framework. The MTDS also reflects the ceiling on new non-concessional external debt, contracted or guaranteed, that applies to Malawi as

required by the Fund's Debt Limits Policy. To strengthen data transparency, the authorities will continue to publish regular reports on outstanding debt figures on the government's official websites. They are also dedicated to building capacity on debt management and financing and will continue to seek further technical assistance from the IMF and other partners in this area.

Monetary, Exchange Rate and Financial Sector Policies

15. The RBM has taken important steps to contain pressures on inflation and the exchange rate. To this end, the RBM raised the policy rate by 200 basis points from 22 percent in June 2023 to 24 percent in July 2023. To further anchor inflation expectations, the RBM stands ready to tighten monetary policy as needed, while containing reserve money growth in line with its monetary control program. The monetary authorities' external policies will support the continued replenishment of foreign exchange reserves, alongside policy actions to facilitate a market-determined exchange rate. In this respect, the RBM resumed purchases of foreign exchange via monthly auctions in June 2023, to encourage price discovery. The central bank is committed to allow greater exchange rate flexibility to remove market distortions, reduce foreign exchange shortages, facilitate easier accumulation of international reserves, and improve trading conditions in the interbank market. In this context and in line with staff advice, the RBM further devalued the local kwacha currency's exchange rate to the dollar by about 44 percent effective on November 9, 2023. This is the second time in 18 months that Malawi allowed the significant weakening of the local unit which removes major economic distortions. Looking ahead, the authorities are committed to taking additional actions to ease these pressures and allow for sustained accumulation of international reserves.

16. To achieve the objective of rebuilding external buffers, the authorities' actions will include: (i) allowing for a greater flexibility in the exchange rate to substantially reduce foreign exchange shortages (ii) increase the effectiveness and transparency of the FX operations (iii) continue to rebuild foreign exchange reserves to comfortable levels that would provide adequate insurance against external shocks. This entails implementing the agreed path of reserves accumulation to reach at least 3.9 months of import cover in the medium term. Furthermore, the RBM will purchase foreign exchange as necessary to deliver this path, while at the same time limiting its sales of foreign exchange and thus becoming, on average, a net purchaser.

17. The authorities will safeguard coordination between fiscal and monetary policy to support their macroeconomic stabilization objectives. In particular, the government's adherence to the agreed fiscal program will support a well-functioning FX market and allow importers and exporters to plan with greater certainty. The authorities request approval to maintain four multiple currency practices (MCPs) and three exchange restrictions. These measures are temporary and are maintained mostly for balance of payments purposes and will thus be eliminated during the ECF-arrangement (SB).

Structural, Governance Reforms and Climate Adaptation

18. Structural reforms aimed to strengthen governance and oversight will continue to assume high priority on the authorities' reform agenda. In this vein, they plan to publish a follow-up report related to the COVID-19 spending audit, detailing the corrective actions and measures to pursue and respond to audit findings. To enhance transparency and accountability in the management of public finances, all payments across MDAs are, since 2021, exclusively being carried out through the Electronic Funds Transfer (EFT), while allowance transfers are linked to an employment number and a single bank account number. In addition, the authorities have operationalized the Financial Crimes Court to fast-track prosecution of financial and related crimes and removed the requirement by the Anti-Corruption Bureau (ACB) to obtain consent from the Director of Public

Prosecution to effect arrests in suspected corruption cases. The Public Procurement and Disposal of Assets Authority (PPDA) Act is also undergoing review to provide for declaration of beneficial ownership in the bidding process and to address anti-competitive practices by bidders in the procurement process. In addition, the ACB has signed a Memorandum of Understanding with selected MDAs to facilitate data and information sharing to help combat corruption.

19. The authorities have also reinforced measures to enhance the oversight of SOEs including by closely monitoring their government guaranteed debt. They have undertaken detailed reporting to the Parliament for FY2021/22 for high-risk SOEs. In parallel, the monitoring of the management accounts of relevant SOEs will be undertaken on a quarterly basis. Further, the authorities will continue to prepare an annual consolidated report of all SOEs in compliance with the new PFM Act. The measures to address longstanding governance weaknesses and corruption will be implemented alongside measures to protect the most vulnerable citizens. Given the limited fiscal space, the authorities will prioritize expenditure to ensure adequate support to the most vulnerable by safeguarding the government's contribution to social safety net programs such as the Social Cash Transfer Program (SCTP), and to protect priority investment in infrastructure.

20. Our authorities acknowledge the significant risks associated with climate change, given the frequent weather-related shocks experienced in Malawi that led to significant loss of lives and destruction of critical infrastructure. In this regard, they are developing policies to build resilience to climate shocks, including through the Disaster Risk Management (DRM) regulations and related policies to be submitted to Parliament by end-December 2024 (SB). The DRM regulations are designed to address gaps in disaster risk management and guide developments in disaster preparedness, risk reduction, as well as response and recovery of buildings. The authorities will also continue to work closely with key partners, including by developing a more efficient agricultural subsidy program to target the most vulnerable households. While agriculture remains fundamental to the economy, the authorities also aim to reduce dependence on agricultural exports. Furthermore, to help rebuild reserve buffers and improve liquidity, they aim to implement the *National Export Strategy*. Going forward, they view further support under the Resilience and Sustainability Facility (RSF), as critical to support efforts to build climate resilience.

Conclusion

21. Our Malawian authorities are committed to macroeconomic stability and consider a new UCT-quality Fund program as critical in augmenting progress already achieved under the PMB and placing public finances on a sustainable footing. They also view the ECF-supported arrangement as important in supporting their long-term vision to create an inclusively wealthy nation under *Malawi 2063*. Against this background, they look forward to the Executive Directors' favorable consideration of their request for a new four-year ECF- arrangement.