

Malawi: Use of Fund Resources—Request for Emergency Assistance—Staff Report and Press Release on the Executive Board Consideration

In the context of the Use of Fund Resources—Request for Emergency Assistance with Malawi, the following documents have been released and are included in this package:

- the staff report for the Use of Fund Resources—Request for Emergency Assistance, prepared by a staff team of the IMF, following discussions that ended on **July 30, 2002**, with the officials of **Malawi** on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on August 22, 2002.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a Press Release summarizing the **views of the Executive Board as expressed during its August 30, 2002** consideration of the staff report.

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INTERNATIONAL MONETARY FUND

MALAWI

Use of Fund Resources—Request for Emergency Assistance

Prepared by the African Department

(In consultation with the Fiscal Affairs, Legal, Monetary and Exchange Affairs, Policy Development and Review, Statistics, and Treasurer's Departments)

Approved by Michael Nowak and Masood Ahmed

August 22, 2002

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I. INTRODUCTION

1. In the attached letter of intent (LOI) to the Managing Director, dated August 22, 2002 (Appendix I), the Malawian authorities request a purchase in an amount of SDR 17.35 million (equivalent to 25 percent of quota) under the Fund's policy for emergency assistance related to natural disasters. This purchase would support imports of food to prevent large shortages, which are expected for later this year. The LOI sets out the authorities' commitment to the macroeconomic framework as well as the measures they intend to undertake to address food shortages. The authorities also reaffirm their intention to continue to work closely with the Fund, so that the first review under the Poverty Reduction and Growth Facility (PRGF) arrangement can be completed by year-end.
2. The last Article IV consultation was concluded by the Executive Board on August 5, 2002 (EBS/02/131, 7/22/02 and Supplement 1). At the time, Directors were broadly supportive of a possible request for emergency assistance related to natural disasters. If the request is approved and the purchase made, outstanding purchases and loans would amount to 104.3 percent of quota. Malawi's relations with the Fund are summarized in Appendix II.

II. BACKGROUND AND THE AUTHORITIES' RESPONSE

3. **As set out in EBS/02/131 (7/22/02) and supplement 1 (7/29/02) and the authorities' letter of intent of July 19, 2002 (EBS/02/131, Appendix I), Malawi is facing a severe food shortage of about 580,000 metric tons (maize equivalent) until the next harvest (April 2003).** The food shortage is expected to be addressed as follows:
 - Humanitarian aid pledges by donors of about 200,000 metric tons are expected to cover the needs of the most vulnerable in society, about 3.2 million people (or 30 percent of the population).
 - Additional, large-scale imports of food are required to close the food gap. The government intends to undertake most of these imports, of up to 350,000 metric tons (equivalent to about US\$97 million), as operations of this size cannot be reliably undertaken by the private sector. About 15 private traders, however, are also participating in the importation.
 - As a large part of the population would be unable to afford maize at import cost, the government intends to sell the imported maize at a subsidized price. The cost of this subsidy is estimated at about 1½ percent of GDP. The domestic fiscal deficit is, nonetheless, projected to narrow to 6 percent of GDP in 2002/03 (July-June) from about 8 percent of GDP in 2001/02, reflecting fiscal adjustment that is already under way. The authorities are working on mechanisms to ensure effective private sector involvement in the distribution.
4. **The external current account deficit (before grants) in 2002 could widen to almost 28 percent of GDP from 13 percent of GDP in 2001, mainly reflecting food**

imports. Although a large part of the external current account deficit is expected to be financed by humanitarian aid, international reserves could drop to below 1 month of imports in November 2002, before being replenished by support from the international community expected by year-end.

5. **The authorities and staff are concerned that such a low level of international reserves would provide insufficient protection against unforeseen shocks and could derail the macroeconomic program.** Thus, the authorities are requesting access to the Fund's emergency assistance equivalent to 25 percent of quota—an amount of about US\$23 million, or about one-quarter of the additional import need. Moreover, these resources would give the authorities flexibility to import additional food should the need arise, particularly in view of the still considerable uncertainty with regard to the estimate of the food shortage. The authorities have started discussions with the World Bank and donors on the need for additional assistance.

6. **The authorities are committed to setting out all elements of the forthcoming food security operation transparently, communicating them clearly to the public, and carefully monitoring and controlling their execution, including through civil society participation (LOI, paragraph 7).** This is to preclude governance issues that have arisen from food operations in the past.

7. **The authorities report good progress in the implementation of program measures, but note that there have been some delays (LOI, paragraph 9).** They have now set up a timetable for implementing the few measures outstanding as of end-July, but indicated that there might be a further delay in lifting import licenses.

III. ABILITY TO SERVICE FINANCIAL OBLIGATIONS TO THE FUND

8. Gross international reserves, after declining to US\$125 million at end-2002, are being targeted by the authorities at about US\$230 million (about 3½ months of imports) by end-2003 and US\$320 million (or almost 4½ months of imports) by end-2005. To achieve these targets, the authorities have indicated that they would approach donors to secure additional resources and close the balance of payments gap of US\$65 million projected in 2003. The Fund could possibly consider augmenting access under the PRGF at the time of the first review. **In light of these efforts, the authorities' intention to pursue sound economic policies under the PRGF arrangement, and their good record of payments to the Fund, it is expected that Malawi will be in a position to discharge its obligations to the Fund in a timely manner. Moreover, given the relatively high cost of the emergency assistance, the authorities have indicated their intention to undertake an early repurchase, if possible, after replenishing their reserves at end-2002.**

IV. STAFF APPRAISAL

9. The food shortage in early 2002 has caused immense human suffering. Many households still have not recovered, and, with another bad harvest this year, urgent and

decisive action by the authorities and the international community is required to avert widespread malnutrition and starvation.

10. The staff endorses the authorities' decision to undertake large-scale food imports, in order to complement the humanitarian aid efforts. Moreover, as effective targeting mechanisms are not available, the staff supports the provision of a price subsidy as the most efficient way of reaching the poor who do not benefit from humanitarian aid.

11. The staff welcomes that the authorities are involving the private sector in the importation and distribution of maize. It urges the authorities, with the assistance of the World Bank and other donors, to review and revamp their food security operations and agricultural policies, with a view to reducing the vulnerability of the poor to food shocks.

12. The staff is encouraged by the approach adopted by the authorities. Their effort to make the operation transparent is expected to avoid some of the governance problems associated with such operations in the past.

13. The staff welcomes the authorities' commitment to achieving their macroeconomic objectives. With the help of the international community, the authorities should be able to manage the crisis and achieve their macroeconomic objectives.

14. To facilitate the food imports and avoid depleting Malawi's international reserves, the authorities have requested emergency assistance from the Fund. The steps that the authorities have taken and proposed so far and the strong international support that has been promised are all encouraging signs that their efforts can succeed. The staff supports the authorities' request for emergency assistance in the amount of SDR 17.35 million. It urges the authorities to adhere to their economic program, so that the first review under the PRGF can be completed at year's end, facilitating an early repurchase as envisaged in the LOI.

Table 1. Malawi: Selected Economic and Financial Indicators, 2000-05

	2000	2001	2002		2003		2004	2005
	Act.	Act.	EBS/02/131	Proj.	EBS/02/131	Proj.	Proj.	
(Percentage change, unless otherwise indicated)								
GDP and prices								
GDP at constant market prices	1.7	-1.5	1.8	1.8	4.5	4.5	5.2	5.4
Consumer prices (end of period)	35.4	22.1	5.0	5.0	5.0	5.0	4.2	4.1
Consumer prices (annual average)	29.6	27.2	9.4	9.4	5.0	5.0	4.4	4.2
GDP deflator	25.2	26.1	12.2	12.2	4.7	4.7	4.1	4.6
Interest rates (end of period) 1/	86.6	54.6	...	...	...	...	...	...
Nominal effective exchange rate (end period) 2/	-32.0	38.8	...	...	...	...	...	...
Real effective exchange rate (end period) 2/	-15.6	52.2	...	...	...	...	...	...
External sector								
Exports, f.o.b. (millions of U.S. dollars)	405.5	406.8	421.1	421.1	451.2	451.2	481.3	513.5
Imports, c.i.f. (millions of U.S. dollars)	563.2	582.2	768.2	795.9	657.2	657.2	693.3	731.4
Terms of trade	-6.2	0.7	5.9	5.9	1.8	1.8	1.4	1.3
Money and credit 3/								
Money and quasi money	42.4	12.1	7.9	7.9	13.4	13.4	13.5	13.4
Net foreign assets	46.8	-15.1	-17.5	-29.5	41.8	43.1	27.0	22.5
Net domestic assets	-4.4	27.2	25.3	37.4	-28.4	-29.8	-13.5	-9.1
Credit to the government	6.9	33.7	12.1	12.1	-34.4	-32.1	-30.2	-29.0
Credit to the rest of the economy	12.4	-5.1	27.6	36.3	-2.5	-10.6	10.5	9.5
(Percent of GDP, unless otherwise indicated)								
Central government 4/								
Revenue (excluding grants)	18.3	16.8	18.0	18.0	17.8	17.8	17.7	17.7
Expenditure	33.3	32.7	31.4	31.9	28.5	28.5	27.2	26.1
Domestic primary balance (cash mod. basis) 5/ 6/	-1.7	-3.7	-2.2	-2.7	-2.3	-2.3	-1.7	-1.1
Domestic balance (cash mod. basis) 6/	-4.7	-8.1	-5.4	-6.0	-3.2	-3.2	-2.6	-2.0
Overall balance (cash mod. basis, including grants)	-5.8	-8.9	-2.7	-3.3	-0.1	-0.1	1.2	2.2
Domestic saving	0.5	-1.0	-15.9	-17.3	0.7	0.7	2.4	3.1
National saving	7.3	3.6	-2.3	-3.8	7.2	7.2	9.7	10.6
Foreign saving 7/	13.9	12.9	26.2	27.7	14.4	14.4	13.8	13.3
Gross investment	12.5	10.9	9.0	9.0	13.9	13.9	15.4	15.8
Public	10.0	8.1	8.0	8.0	9.6	9.6	8.9	8.2
Private	2.6	2.8	1.0	1.0	4.4	4.4	6.5	7.6
Stock building	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External sector								
Exports, f.o.b.	23.8	23.3	22.2	22.2	23.1	23.1	22.9	22.4
Imports, c.i.f.	33.0	33.3	40.5	41.9	33.6	33.6	32.9	31.9
External current account (including official transfers)	-5.3	-7.3	-11.3	-12.7	-6.7	-6.8	-5.7	-5.2
External debt	156.7	156.4	147.6	148.9	147.6	148.8	140.7	131.4
Debt-service ratio 8/	21.8	21.1	20.4	20.4	20.7	20.7	21.0	20.2
Of which: interest payments 8/	6.9	6.6	6.2	6.2	5.8	5.8	5.4	5.0
(In millions of U.S. dollars, unless otherwise indicated)								
Gross official reserves								
End-period stock	242.5	201.8	129.9	125.4	228.4	228.4	278.8	319.5
In months of imports of goods and nonfactor services 9/	4.4	2.7	2.1	2.0	3.4	3.4	3.9	4.3
External debt (disbursed and outstanding, end of period)	2,674	2,736	2,803	2,827	2,883	2,907	2,962	3,013
Memorandum items:								
GDP (in millions of kwacha)	101,634	126,266	144,175	144,175	157,783	157,783	172,768	190,462
Kwacha per U.S. dollar exchange rate (per. avg.)	59.5	72.2	...	...	...	...	...	...
Per capita GDP (U.S. dollars)	165.5	166.2	...	...	...	...	...	...
Population (millions)	10.3	10.5	10.7	10.7	11.0	11.0	11.2	11.4

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

1/ Compounded three-month interest bill.

2/ Positive value denotes appreciation of kwacha.

3/ Change in percent of money and quasi money at the beginning of the period.

4/ Fiscal year starting July 1; information for 2001 refers to fiscal-year 2001/02, etc.

5/ The domestic primary balance excludes grants, domestic and foreign interest, and foreign-financed development expenditure.

6/ Cash-modified basis defined as cash spending and expenditure in arrears.

7/ External current account, excluding official transfers.

8/ In percent of exports of goods and nonfactor services. Excludes debt relief.

9/ In percent of imports of goods and nonfactor services in the following period.

Table 2. Malawi: Central Government Operations, 2000/01-2003/04 1/

	2000/01	2001/02	2002/03		2003/04	
	Act.	Rev. Proj.	Prog. EBS/02/131	Rev. Proj.	Prog. EBS/02/131	Rev. Proj.
	(In millions of kwacha)					
Total revenue and grants	31,233	32,093	43,153	43,153	47,043	47,069
Revenue	20,880	22,663	27,144	27,144	29,413	29,413
Tax revenue	19,285	20,168	24,259	24,259	26,600	26,600
Taxes on income and profits	8,740	9,338	10,584	10,584	11,625	11,625
Taxes on goods and services	8,169	8,722	11,077	11,077	12,188	12,188
Taxes on international trade	2,385	2,396	2,928	2,928	3,149	3,149
Other (incl. refunds)	-10	-287	-330	-330	-363	-363
Nontax revenue	1,595	2,495	2,885	2,885	2,814	2,814
Departmental receipts	1,036	1,202	1,330	1,330	1,461	1,461
Petroleum levy for national roads authority (NRA)	559	1,180	1,232	1,232	1,353	1,353
Petroleum levy for safety nets	0	113	324	324	0	0
Transfer of RBM profits	0	0	0	0	0	0
Grants	10,353	9,429	16,009	16,009	17,630	17,656
Program	6,209	2,375	9,042	9,042	8,343	8,369
Project	3,565	3,668	3,558	3,558	3,569	3,569
HIPC Initiative	579	3,386	3,409	3,409	5,718	5,718
Total expenditure and net lending	37,887	44,143	47,286	48,174	47,274	47,274
Total expenditure	37,303	44,143	47,286	48,174	47,274	47,274
Current expenditure	25,772	33,157	34,847	35,735	33,825	33,825
Wages and salaries	5,954	8,687	9,283	9,283	10,196	10,196
Interest payments	5,267	7,644	7,046	7,046	3,915	3,915
Domestic	3,426	5,878	4,870	4,870	1,573	1,573
Foreign	1,841	1,766	2,177	2,177	2,343	2,343
Other current expenditure	13,869	16,709	18,517	19,405	19,713	19,713
Of which: maize subsidy	0	0	1,673	2,561	0	0
Expenditure in arrears	616	118	0	0	0	0
Development expenditure	11,530	10,986	12,439	12,439	13,450	13,450
Part I (foreign financed)	9,789	8,806	9,853	9,853	10,137	10,137
Part II (domestically financed)	1,741	2,180	2,586	2,586	3,313	3,313
Net lending	584	0	0	0	0	0
Overall balance (including grants)	-6,654	-12,050	-4,132	-5,020	-231	-205
Total financing	6,981	10,878	4,132	5,020	231	205
Foreign (net)	5,580	1,019	9,744	10,178	5,507	5,507
Balance of payments gap	0		4,824	5,258		
Borrowing	10,456	5,138	9,881	9,881	11,008	11,008
Program	4,521	0	3,587	3,587	4,440	4,440
Project	5,936	5,138	6,295	6,295	6,568	6,568
Amortization	-5,129	-3,799	-4,771	-4,771	-5,501	-5,501
Special loans (net)	253	-320	-191	-191	0	0
Domestic (net)	1,401	9,859	-5,611	-5,157	-5,276	-5,302
Banking system	-201	10,981	-5,818	-5,364	-5,576	-5,602
Nonbanks	1,083	-1,075	0	0	0	0
Domestic supplier credits (net)	573	-277	-196	-196	101	101
Change in arrears	-168	70	0	0	0	0
Privatization proceeds	114	158	403	403	200	200
Discrepancy	327	-1,173	0	0	0	0

Table 2. Malawi: Central Government Operations, 2000/01-2003/04 1/

	2000/01	2001/02	2002/03		2003/04	
	Act.	Rev. Proj.	Prog. EBS/02/131	Rev. Proj.	Prog. EBS/02/131	Rev. Proj.
(In percent of GDP, unless otherwise indicated)						
Total revenue and grants	27.4	23.8	28.6	28.6	28.4	28.4
Revenue	18.3	16.8	18.0	18.0	17.8	17.8
Tax revenue	16.9	14.9	16.1	16.1	16.1	16.1
Taxes on income and profits	7.7	6.9	7.0	7.0	7.0	7.0
Taxes on goods and services	7.2	6.5	7.3	7.3	7.4	7.4
Taxes on international trade	2.1	1.8	1.9	1.9	1.9	1.9
Other (incl. refunds)	0.0	-0.2	-0.2	-0.2	-0.2	-0.2
Nontax revenue	1.4	1.8	1.9	1.9	1.7	1.7
Grants	9.1	7.0	10.6	10.6	10.6	10.7
Program	5.5	1.8	6.0	6.0	5.0	5.1
Project	3.1	2.7	2.4	2.4	2.2	2.2
HIPC Initiative	0.5	2.5	2.3	2.3	3.5	3.5
Total expenditure and net lending	33.3	32.7	31.4	31.9	28.5	28.5
Total expenditure	32.8	32.7	31.4	31.9	28.5	28.5
Current expenditure	22.6	24.6	23.1	23.7	20.4	20.4
Wages and salaries	5.2	6.4	6.2	6.2	6.2	6.2
Interest payments	4.6	5.7	4.7	4.7	2.4	2.4
Domestic	3.0	4.4	3.2	3.2	0.9	0.9
Foreign	1.6	1.3	1.4	1.4	1.4	1.4
Other current expenditure	12.2	12.4	12.3	12.9	11.9	11.9
Of which: maize subsidy	0.0	0.0	1.1	1.7	0.0	0.0
Expenditure in arrears	0.5	0.1	0.0	0.0	0.0	0.0
Development expenditure	10.1	8.1	8.2	8.2	8.1	8.1
Part I (foreign financed)	8.6	6.5	6.5	6.5	6.1	6.1
Part II (domestically financed)	1.5	1.6	1.7	1.7	2.0	2.0
Net lending	0.5	0.0	0.0	0.0	0.0	0.0
Overall balance (including grants)	-5.8	-8.9	-2.7	-3.3	-0.1	-0.1
Total financing	6.1	8.1	2.7	3.3	0.1	0.1
Foreign (net)	4.9	0.8	6.5	6.7	3.3	3.3
Balance of payments gap	0.0	0.0	3.2	3.5	0.0	0.0
Borrowing	9.2	3.8	6.6	6.6	6.6	6.6
Amortization	-4.5	-2.8	-3.2	-3.2	-3.3	-3.3
Special loans (net)	0.2	-0.2	-0.1	-0.1	0.0	0.0
Domestic (net)	1.2	7.3	-3.7	-3.4	-3.2	-3.2
Discrepancy	0.3	-0.9	0.0	0.0	0.0	0.0
Memorandum items:						
Domestic balance 2/	-4.7	-8.1	-5.4	-6.0	-3.2	-3.2
Domestic primary balance 3/	-1.7	-3.7	-2.2	-2.7	-2.3	-2.3
Pro-poor expenditure (excl. donor-funded projects)	3.3	5.1	5.9	5.9	6.2	6.2
Total financing target 4/	6.9	8.5	6.8	7.4	4.7	4.7
Nominal GDP (in millions of kwacha)	113,828	135,021	150,794	150,794	165,628	165,628

Source: Malawian authorities; and Fund staff projections.

1/ Fiscal years runs from July to June.

2/ Overall balance excluding grants, foreign-financed development expenditure, and foreign interest payments.

3/ Domestic balance, excluding domestic interest payments.

4/ Total financing and grants, excluding foreign project-related financing.

Table 3. Malawi: Monetary Authorities' Balance Sheet, 2000-05
(In millions of Malawi kwacha, unless otherwise indicated)

	2001 Dec. Actual	2002 May Actual	2002 June Proj.	2002 Sep. Proj.	2002 Dec. EBS/02/131 Proj.		2003 Dec. EBS/02/131 Proj.		2004 Dec. Proj.	2005 Dec. Proj.
Reserve money 1/	7,665	9,051	8,849	9,002	8,236	8,236	9,005	9,005	9,818	10,710
Currency outside RBM	4,209	5,822	...	...	4,872	4,872	5,362	5,362	5,752	5,988
Commercial bank deposits with RBM	3,456	3,229	...	...	3,363	3,363	3,643	3,643	4,066	4,722
Net foreign assets (NFA) 2/	8,769	7,867	7,513	5,510	4,478	2,263	12,138	10,188	15,540	20,498
NFA (in millions of U.S. dollars)	130	104	98	70	56	28	149	125	188	246
Gross foreign assets	203	177	168	163	131	126	230	230	280	321
Foreign liabilities	-73	-73	-70	-93	-75	-98	-81	-105	-92	-75
Net domestic assets of the monetary authorities	-1,104	1,184	1,336	3,491	3,757	5,973	-3,133	-1,183	-5,723	-9,788
Credit to government (net)	3,663	3,016	6,782	7,222	5,888	5,888	-957	-503	-7,304	-14,725
Credit to statutory bodies (net) 3/	166	286	287	2,801	3,801	5,414	287	287	287	287
Credit to domestic banks	4	44	3	3	3	3	3	3	3	3
Other items (net)	-4,937	-2,162	-5,738	-6,535	-5,935	-5,333	-2,466	-970	1,291	4,646
Revaluation accounts	-1,653	-2,525	-2,608	-2,732	-2,798	-2,771	-2,888	-2,817	-2,954	-3,112
Open market operations: holdings of monetary policy bills	-7,746	-6,338	-9,025	-9,939	-9,906	-9,309	-8,038	-6,613	-4,939	-1,984
Others	4,462	6,700	5,896	6,136	6,768	6,748	8,460	8,459	9,184	9,742
Memorandum items:										
12-month percentage change in reserve money	13.5	9.8	12.7	5.4	7.4	7.4	9.3	9.3	9.0	9.1
Money multiplier	2.26	2.31	2.40	2.45	2.41	2.41	2.50	2.50	2.61	2.71
Currency-deposit ratio	0.30	0.39	...	...	0.32	0.32	0.31	0.31	0.29	0.26
Reserve-deposit ratio	0.28	0.21	...	...	0.22	0.22	0.21	0.21	0.21	0.21

Sources: Reserve Bank of Malawi (RBM); and Fund staff estimates and projections.

1/ To adjust for a temporary contraction at end-December 2000, reserve money is calculated as the simple average of reserve money on December 22 and 29, 2000, and January 5, 2001.

To adjust for a temporary expansion at end-December 2001, reserve money is calculated by adjusting for excess reserves of MK 500 million on December 31, 2001.

2/ For actuals, reserve money and NFA are calculated at the actual end-period exchange rate; for projections, reserve money and NFA are calculated at the projected end-period exchange rate.

3/ Includes net lending to the National Food Reserve Agency (NFRA) for the 2002/03 maize imports.

Table 4. Malawi: Monetary Survey, 2000-05
(In millions of Malawi kwacha, unless otherwise indicated)

	2001	2002	2002	2002	2002		2003		2004	2005
	Dec. Actual	May Actual	June Proj.	Sep. Proj.	Dec. EBS/02/131	Proj.	Dec. EBS/02/131	Proj.	Dec.	Dec. Proj.
Money and quasi money 1/	18,438	20,928	21,242	22,087	19,887	19,887	22,548	22,548	25,585	29,020
Money	9,312	11,158	...	...	...	...	...	...	...	...
Quasi money	9,126	9,770	...	...	...	...	...	...	...	...
Net foreign assets (NFA) 1/	11,777	10,235	11,055	9,278	8,553	6,338	16,866	14,916	20,993	26,758
NFA (in millions of U.S. dollars)	175	135	144	118	107	79	207	183	254	321
Gross foreign assets	263	223	228	225	197	193	305	305	366	418
Foreign liabilities	-88	-88	-84	-107	-90	-113	-98	-122	-112	-98
Monetary authorities	8,769	7,867	7,513	5,510	4,478	2,263	12,138	10,188	15,540	20,498
NFA of the monetary authorities (in millions of U.S. dollars)	130	104	98	70	56	28	149	125	188	246
Commercial banks	3,009	2,368	3,542	3,768	4,075	4,075	4,728	4,728	5,453	6,260
NFA of the commercial banks (in millions of U.S. dollars)	45	31	46	48	51	51	58	58	66	75
Net domestic assets (NDA)	6,661	10,693	10,187	12,809	11,334	13,549	5,682	7,631	4,592	2,263
Credit to government (net)	5,661	6,633	9,348	9,487	7,887	7,887	1,042	1,496	-5,305	-12,726
Credit to statutory bodies (net) 2/	-45	282	397	2,910	3,910	5,523	397	397	397	397
Credit to private sector	5,289	5,861	6,168	6,280	6,421	6,421	9,432	9,432	11,805	14,253
Other items (net)	-4,244	-2,083	-5,726	-5,869	-6,884	-6,282	-5,189	-3,693	-2,304	340
Revaluation accounts	-2,377	-3,586	-3,714	-3,910	-4,043	-4,016	-4,215	-4,144	-4,345	-4,559
Open market operations: holdings of monetary policy bills	-6,829	-5,534	-7,825	-7,939	-8,989	-8,392	-7,121	-5,696	-4,022	-1,067
Others	4,962	7,037	5,814	5,980	6,147	6,127	6,147	6,147	6,063	5,965
Memorandum items:										
Velocity of money (annual GDP divided by period-average broad money)	7.0	...	...	...	7.3	7.3	7.2	7.2	7.0	6.8
Broad money (12-month percentage change)	12.1	6.7	5.9	17.7	7.9	7.9	13.4	13.4	13.5	13.4
Private sector credit (12-month percentage change)	3.2	13.2	37.7	22.0	21.4	21.4	46.9	46.9	25.2	20.7

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

1/ For actuals, broad money and NFA are calculated at the actual end-period exchange rate; for projections, broad money and NFA are calculated at the projected end-period exchange rate.

2/ Includes net lending to the National Food Reserve Agency (NFRA) for the 2002/03 maize imports.

Table 5. Malawi: Balance of Payments, 2000-07
(In millions of U.S. dollars; unless otherwise specified)

	2000	2001	2002		2003		2004	2005	2006	2007
	EBS/02/131	EBS/02/131	EBS/02/131	Proj.	EBS/02/131	Proj.				
Current account balance (including grants)	-89.0	-127.7	-214.4	-242.1	-131.3	-132.2	-120.0	-118.2	-100.3	-107.7
Trade balance	-157.7	-175.4	-347.1	-374.8	-205.9	-205.9	-211.9	-217.9	-221.8	-226.0
Exports	405.5	406.8	421.1	421.1	451.2	451.2	481.3	513.5	542.5	572.7
Of which: tobacco	246.8	236.0	243.0	243.0	259.7	259.7	275.7	292.6	306.7	321.5
tea, sugar, and coffee	81.4	97.1	100.7	100.7	106.9	106.9	113.7	120.9	127.4	133.7
nontraditional exports	55.7	59.9	63.5	63.5	69.5	69.5	75.8	82.7	90.2	98.4
Imports	-563.2	-582.2	-768.2	-795.9	-657.1	-657.1	-693.3	-731.4	-764.3	-798.7
Of which: petroleum	74.5	68.0	69.9	69.9	69.1	69.1	68.7	68.2	69.5	72.5
maize	0.0	8.5	26.5	26.5	0.0	0.0	0.0	0.0	0.0	0.0
Projected future maize imports			110.2	137.9						
Donors 1/			41.0	41.0						
Government 2/			69.2	96.9						
Services balance	-86.9	-65.5	-166.4	-166.4	-91.1	-92.0	-95.6	-105.4	-109.5	-114.1
Interest public sector (net)	-20.6	-17.8	-26.8	-26.8	-23.1	-24.0	-17.6	-14.0	-11.2	-8.6
Receipts	12.1	8.7	2.4	2.4	5.8	5.8	11.7	15.0	17.1	19.2
Payments (amounts due before debt relief)	-32.7	-26.5	-29.2	-29.2	-29.0	-29.8	-29.3	-28.9	-28.3	-27.8
Other factor payments (net)	-17.7	-14.6	-14.8	-14.8	-15.5	-15.5	-16.3	-17.2	-18.1	-19.1
Nonfactor (net)	-48.7	-33.1	-124.8	-124.8	-52.5	-52.5	-61.7	-74.2	-80.1	-86.4
Receipts	45.3	48.7	49.2	49.2	50.1	50.1	51.1	52.1	53.2	54.2
Payments	-93.9	-81.8	-91.6	-91.6	-102.6	-102.6	-112.8	-126.3	-133.3	-140.6
Maize-related payments 3/			-82.4	-82.4						
Unrequited transfers (net)	155.6	113.2	299.1	299.1	165.6	165.6	187.5	205.1	231.0	232.4
Private (net)	7.8	15.5	15.8	15.8	16.0	16.0	16.3	16.6	16.9	17.3
Receipts	21.8	21.8	22.3	22.3	22.5	22.5	22.9	23.4	23.9	24.3
Payments	-13.9	-6.3	-6.5	-6.5	-6.5	-6.5	-6.7	-6.8	-6.9	-7.1
Official (net)	147.8	97.7	283.2	283.2	149.6	149.6	171.2	188.4	214.1	216.0
Receipts	148.4	98.3	283.8	283.8	150.3	150.3	171.9	189.1	214.7	216.7
Balance of payments assistance	78.4	51.0	74.4	74.4	92.6	92.6	112.7	128.5	152.8	153.3
Japan HIPC Initiative			14.0	14.0						
Donor humanitarian grants 2/			133.7	133.7						
Project related	69.9	47.3	61.8	61.8	57.7	57.7	59.1	60.6	62.0	63.4
Drought related	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Payments	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6	-0.7	-0.7
Capital account balance (incl. errors and omissions)	78.2	96.2	109.7	109.7	112.7	112.7	113.8	117.7	117.0	117.4
Medium- and long-term flows	65.0	59.8	70.5	70.5	74.0	104.0	68.0	67.4	62.5	58.5
Disbursements	124.9	127.0	126.0	126.0	138.5	138.5	138.5	138.6	138.6	138.6
Balance of payments support	31.4	55.0	45.0	45.0	52.6	52.6	54.7	56.8	58.9	61.0
Project support	93.5	72.0	81.0	81.0	85.9	85.9	83.8	81.7	79.6	77.6
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization (amounts due before debt relief)	-59.9	-67.2	-55.5	-55.5	-64.5	-64.5	-70.5	-71.2	-76.0	-80.1
Foreign direct investment and other inflows	27.0	28.0	47.6	47.6	38.7	38.7	45.8	50.3	54.5	59.0
Short-term capital and errors and omissions	-13.8	8.5	-8.5	-8.5	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-10.8	-31.5	-104.7	-132.4	-18.6	-19.5	-6.2	-0.5	16.8	9.7
Financing (-increase in reserves)	10.8	31.5	104.8	132.5	-41.4	-45.9	6.2	0.5	-16.8	-9.7
Central bank	16.6	11.8	73.3	101.0	-92.5	-97.0	-63.1	-57.5	-66.2	-56.0
Gross reserves (-increase)	1.7	40.7	71.9	76.4	-98.5	-103.0	-50.4	-40.8	-44.3	-40.0
Liabilities	14.9	-28.9	1.3	24.6	6.0	6.0	-12.7	-16.7	-21.9	-16.0
Of which: IMF (net)	-1.8	-7.8	0.3	23.5	5.9	5.9	-12.9	-16.9	-22.0	-16.1
Purchases/drawings	8.4	0.0	8.1	31.3	16.1	16.1	0.0	0.0	0.0	0.0
Repurchases/repayments	-10.2	-7.8	-7.8	-7.8	-10.2	-10.2	-12.9	-16.9	-22.0	-16.1
Commercial banks	-5.7	-7.7	-6.0	-6.0	-7.0	-7.0	-8.0	-9.0	-10.0	-10.5
Arrears	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt relief	0.0	27.4	37.5	37.5	58.1	58.1	77.3	67.0	59.4	56.7
Residual financing gap (+ = underfinanced)	0.0	0.0	0.0	0.0	60.0	65.4	0.0	0.0	0.0	0.0
Memorandum items:										
Gross official reserves										
In millions of U.S. dollars	242.5	201.8	129.9	125.4	228.4	228.4	278.8	319.5	363.9	403.9
In months of imports 4/	4.4	2.7	2.1	2.0	3.4	3.4	3.9	4.3	4.6	4.9
In months of imports 5/	4.4	3.6	1.8	1.7	3.6	3.6	4.1	4.5	4.9	5.2
Current account balance (percent of GDP)										
Excluding official transfers	-14.2	-12.9	-26.2	-27.7	-14.4	-14.5	-13.9	-13.4	-12.4	-12.0
Including official transfers	-5.3	-7.3	-11.3	-12.7	-6.7	-6.8	-5.7	-5.2	-3.9	-4.0
Export value growth (in percent)	-9.3	0.3	3.5	3.5	7.1	7.1	6.7	6.7	5.7	5.6
Import value growth excl. foodstuff (in percent)	-16.4	1.9	8.5	8.5	4.7	4.5	5.5	5.5	4.5	4.5
Prospective BOP financing (grants & loans) (millions of US\$)	...	106.0	119.4	119.4	145.2	145.2	167.5	185.3	211.7	214.2
Identified financing	...	106.0	119.4	119.4	88.0	88.0	0.0	0.0	0.0	0.0
Financing expected but not yet confirmed	...	0.0	0.0	0.0	57.2	57.2	167.5	185.3	211.7	214.2

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

1/ Donor food imports provided for humanitarian aid; amount provided by UN Consolidated Appeal in Response to the Humanitarian Crisis, 2002/03.

2/ Government imports of 350,000 metric tons, including 53,000 metric tons for the restocking of the NFRA.

3/ Costs related to humanitarian imports; amount provided by UN Consolidated Appeal in Response to the Humanitarian Crisis, 2002/03.

4/ In months of following year's imports of goods and nonfactor services.

5/ In months of current year's imports of goods and nonfactor services.

August 22, 2002

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Köhler,

1. Malawi is facing a serious food shortage. Although there is still considerable uncertainty surrounding the estimate of the food gap, it will be more severe than the one experienced at the beginning of the year. The macroeconomic framework underlying our letter of July 19, 2002 was predicated on the Food and Agricultural Organization (FAO)/World Food Program (WFP) May 2002 estimate, which identified an import requirement of 485,000 metric tons (maize equivalent) to cover the food gap expected until the new harvest in April 2002. However, more recently, the Ministry of Agriculture and Irrigation, together with USAID's Famine Early Warning System (FEWS), has revised the gap upward to about 580,000 metric tons (maize equivalent).
2. One-third of our population (about 3.2 million people) is expected to require humanitarian aid (including about 200,000 metric tons of food aid). We are grateful that donors have been making pledges broadly covering this need, and the first shipments have arrived in Malawi.
3. To cover the remaining food requirement, the government intends to import maize of up to 350,000 metric tons (equivalent to about US\$97 million), as needed. Private traders would not be able to handle an operation of this size, but we are involving the private sector in the importation in an effort to build up its capacity.
4. Payment for these imports, however, could result in a fall of international reserves of the Reserve Bank of Malawi (RBM) to a level that we regard as insufficient as a protection from unforeseen shocks. Thus, without additional financial assistance, our country would not have the resources it might need to feed its people without jeopardizing its macroeconomic objectives. Given the humanitarian risks involved and our experience last year, we believe that there is a need for swift action.
5. Thus, the government requests a purchase from the Fund of the equivalent of SDR 17.35 million (25 percent of quota) under the Fund's policy on emergency assistance. Although the amount of the assistance is small relative to our total needs, we believe that the

speed with which the resources could become available will assist us in seeking additional assistance from other donors.

6. Since a large part of the population is unable to afford maize at import cost, we will distribute this maize at a subsidized price, at a cost of about 1½ percent of GDP, resulting in a domestic fiscal deficit of about 6 percent of GDP; we are developing mechanisms to ensure effective private sector involvement in the distribution. The ability to cope with the impending shortage has been seriously eroded by the crisis earlier this year, when the poor sold their assets to purchase food. Thus, in addition to the one-third of the population receiving humanitarian aid, we believe that another one-third of the population (the remainder of those classified as poor) will need assistance as it will not have the purchasing power to afford the maize at import cost. Our preferred option would have been to provide a targeted subsidy. However, as there is little time to act and existing targeting mechanisms do not extend to the urban poor, the government decided that a price subsidy was the most efficient way to provide such a transfer. We are planning to set the price at MK 17.5 per kilogram, which we believe should be high enough to not discourage local maize production in the future.

7. As the government's maize operations have given rise to governance issues in the past, we will ensure that the current food security operation will be carried out transparently. First, we have decided that all transactions are to be carried out through the National Food Reserve Agency (NFRA). Second, the operation will be financed through the RBM, and proceeds from the sale of maize will be deposited by the NFRA in an account at the RBM. Third, we have created a task force that will monitor and control all aspects of the operation. The task force includes representatives from the government, the NFRA, and Agricultural Development and Marketing Corporation (ADMARC), donors, and the Malawi Economic Justice Network (MEJN), the umbrella organization for 61 civil society organizations. Fourth, we intend to publish on a monthly basis information on the food security operation, including the cost and volume of imports and the price and quantity of imports sold domestically. Finally, in particular in light of the uncertainty of the food gap estimates, we will update the assessment of the food situation and revise our operation, as needed. Any reassessment will be communicated to all stakeholders.

8. The great uncertainty regarding the estimate of the food shortage again highlights the urgency of the need to improve agricultural statistics. As a first step, we have transferred the responsibility for agricultural statistics from the Ministry of Agriculture and Irrigation to the National Statistics Office, as agricultural extension workers in the ministry had incentives to overestimate production in past years. We will seek donor assistance to overhaul the collection and compilation of agricultural statistics.

9. We would also like to take the opportunity to provide an update on the measures that we intended to implement by July 2002. The RBM has developed a medium-term action plan for the review of the financial sector regulatory framework. To remove ghost workers from the payroll, we have audited the payroll of the Ministry of Education, which accounts for 60 percent of the entire civil service, and have adjusted the payroll starting in August 2002.

Audits of the Ministries of Health, Police, and Defense will be completed by October 2002, and an audit of the Ministry of Agriculture will follow. To strengthen the operation of the Credit Ceiling Authority (CCA) system, we have assigned staff of the Ministry of Finance and Economic Planning to the RBM, eliminated unused budget balances in the CCA system carried forward between fiscal years, and reformatted the CCA system to include priority pro-poor expenditure (PPEs). Moreover, the cabinet has issued a directive on the divestiture options of ADMARC's main subsidiaries. While the liquidation of David Whitehead and Sons has been approved in principle, we have issued an information memorandum for privatization that requests responses for either an outright purchase of the assets, a concession or a management contract, as an interest in buying the company has been recently expressed. We have removed the import bans on cooking oil, dairy products and dry cells, but have introduced import licenses on dairy products and dry cells. These import licenses are being issued liberally and the one on cement is being issued automatically.

10. The government will continue to cooperate with the Fund and is confident that the first review under the Poverty Reduction and Growth Facility (PRGF) arrangement can be completed at year's end. We have attached a revised Table 1 on the quantitative benchmarks of our letter of July 19, 2002, reflecting lower net international reserves on account of higher food imports. Moreover, we intend to undertake an early repurchase of the emergency assistance, after replenishing our international reserves at end-2002. The government does not intend to impose new or intensify existing restrictions on payments and transfers for current international transactions, introduce new or intensify existing trade restrictions for balance of payment purposes, or enter into bilateral payments agreements, which are inconsistent with Article VIII of the Fund's Articles of Agreement.

Sincerely yours,

/s/

Dr. Ellias E. Ngalande
Governor
Reserve Bank of Malawi

/s/

Mr. Friday A. Jumbe
Minister of Finance and
Economic Planning

Table 1. Malawi: Quantitative Targets Under the PRGF Arrangement, 2002 1/
(In millions of Malawi kwacha, unless otherwise indicated)

	2002 End-Sep. Rev. Prog.	2002 End-Dec. Rev. Prog.
Ceiling on the stock of reserve money 2/ 3/	8,855	8,623
Floor on the net foreign assets (NFA) of the monetary authorities 4/ (in millions of U.S. dollars)	70	28
Ceiling on the total financing of the central government 5/	2,812	5,249
Clearance of new domestic budgetary arrears 6/	...	...
Ceiling on the stock of external arrears 7/	0	0
Ceiling on contracting or guaranteeing of external debt by the central government and the Reserve Bank of Malawi (RBM)		
Medium and long term 8/	0	0
Short term 9/	0	0
Memorandum item:		
Baseline for balance of payments support for NFA adjuster (in millions of U.S. dollars) 10/	82	157

1/ Targets for reserve money, net foreign assets, and external payment arrears relate to the respective stocks. All other targets for end-June are expressed as cumulative changes from December 31, 2001; targets for end-September and end-December are expressed as cumulative changes from June 30, 2002 onward. All targets are defined in the technical memorandum of understanding (TMU).

2/ The ceiling is set as an average of daily reserve money.

3/ The ceiling will be adjusted downward (upward) to reflect any decrease (increase) in the RBM reserve requirements on deposits.

4/ The floor will be adjusted downward (upward) for any shortfall (excess) of balance of payments support from its programmed levels, up to a maximum of US\$50 million.

5/ The ceiling will be adjusted downward for any transfers from the RBM to the central government and upward for promissory notes issued to cover the RBM's operational losses in 2001.

6/ Any new domestic budgetary arrears verified during the quarter, to be cleared by the end of the following quarter.

7/ Applicable on a continuous basis.

8/ Exclusions are specified in the TMU.

9/ Includes debt with maturity up to and including one year. Exclusions are specified in the TMU.

10/ Includes debt relief under the enhanced HIPC Initiative and excludes IMF disbursements. The adjuster is expressed cumulatively from December 31, 2001 onward.

Malawi: Relations with the Fund
(As of July 31, 2002)

I. **Membership Status:** Joined 07/19/1965; Article VIII (December 7, 1995)

II. General Resources Account:	<u>SDR million</u>	<u>%Quota</u>
Quota	69.40	100.0
Fund holdings of currency	67.13	96.7
Reserve position in Fund	2.28	3.3

III. SDR Department:	<u>SDR million</u>	<u>%Allocation</u>
Net cumulative allocation	10.98	100.0
Holdings	1.79	16.3

IV. Outstanding Purchases and Loans:	<u>SDR million</u>	<u>%Quota</u>
Enhanced Structural Adjustment Facility (ESAF)/Poverty Reduction and Growth Facility (PRGF) arrangements	55.05	79.3

V. **Financial Arrangements:**

<u>Type</u>	<u>Approval date</u>	<u>Expiration date</u>	<u>Amount approved (SDR million)</u>	<u>Amount drawn (SDR million)</u>
PRGF	12/21/2000	12/20/2003	45.11	6.44
ESAF/PRGF	10/18/1995	12/16/1999	50.96	50.96
Stand-By Arrangement	11/16/1994	06/30/1995	15.00	12.73

VI. **Projected Obligations to Fund** (SDR million; based on existing use of resources and present holdings of SDRs):

	<u>Forthcoming</u>				
	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Principal	2.8	7.2	9.2	10.2	9.2
Charges/interest	0.2	0.5	0.4	0.4	0.3
Total	3.0	7.7	9.6	10.6	9.5

VII. Implementation of HIPC Initiative:

	<u>Original framework</u>	<u>Enhanced framework</u>	<u>Total</u>
Commitment of HIPC assistance			
Decision point date		12/21/00	
Assistance committed (NPV terms) ¹			
Total assistance (US\$ million)		643	
<i>Of which:</i> Fund assistance (SDR million)		23.1	
Completion point date		Floating	
Delivery of Fund assistance (SDR million)			
Amount disbursed		2.3	2.3
Interim assistance		2.3	2.3
Completion point ²	
Amount applied against member's obligations (cumulative)		2.4	2.4

VIII. Safeguards Assessments:

Under the Fund's safeguards assessment policy, the Reserve Bank of Malawi (RBM) is subject to a safeguards assessment with respect to the Poverty Reduction and Growth Facility arrangement that was approved on December 21, 2000 and is scheduled to expire on December 20, 2003. A safeguards assessment of the RBM was completed on July 12, 2001. The assessment concluded that an on-site assessment was not needed at this stage, but proposed steps to address certain weaknesses in the areas of financial reporting and internal controls.

IX. Exchange Arrangements:

The exchange rate of the Malawi kwacha is market determined. The Reserve Bank of Malawi publishes a reference rate, based on interbank transactions, on a daily basis. The rate was US\$1 = MK 75.62 on July 31, 2002.

¹ Net present value (NPV) terms at the completion point under the original framework, and NPV terms at the decision point under the enhanced framework.

² Under the enhanced HIPC Initiative, the nominal amount of assistance disbursed will include an additional amount corresponding to interest on amounts committed but not disbursed during the interim period, calculated using the average return (during the interim period) on the investment of resources held by, or for, the benefit of the PRGF-HIPC Trust.

X. Article IV Consultation:

Malawi is on the standard 12-month Article IV consultation cycle. The last Article IV consultation (EBS/02/131; 7/22/02) was concluded by the Executive Board on August 5, 2002.

XI. Technical Assistance:

Date	Duration	Dept.	Recipient	Purpose	Form
1/99	1 week	MAE	Reserve Bank	Monetary operations	Advisor
1/99	4 weeks	MAE	Reserve Bank	Banking supervision	Advisor
8/99	1½ weeks	MAE	Reserve Bank	Monetary operations	Mission
12/99	1½ weeks	FAD	Ministry of Finance	Expenditure control	Mission
12/99	2 weeks	FAD	Ministry of Finance	Improvement and extension of surtax	Mission
12/99	1 year	FAD	Ministry of Finance	Expenditure management	Advisor
1/00	1 year	STA	National Statistical Office	Statistics	Advisor
6/00	1 year	FAD	Ministry of Finance	Revenue administration	Advisor
11/00	2 weeks	FAD	Ministry of Finance	Improvements of fiscal data and commitment control	Mission
9/01	1½ weeks	FAD	Ministry of Finance	Expenditure tracking and fiscal ROSC	Mission
11/01	2 weeks	MAE	Reserve Bank	Monetary operations and further developing financial markets	Mission
2/02	2 weeks	FAD	Ministry of Finance	Expenditure policy	Mission
5/02	6 months	FAD	Ministry of Finance	Expenditure management	Advisor
7/02	2 weeks	STA	National Statistical Office, RBM	GDDS	Mission

XII. Resident Representative:

Mr. Girma Begashaw, since February 2002.



Press Release No. 02/38
FOR IMMEDIATE RELEASE
September 3, 2002

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US\$23 Million in Emergency Credit to Malawi

The Executive Board of the International Monetary Fund (IMF) approved today SDR 17.35 million (about US\$23 million) in emergency credit to Malawi, which will support imports of food to prevent large shortages expected later this year.

Malawi experienced a severe food crisis in early 2002, causing immense human suffering. The food shortages resulted in widespread malnutrition and starvation, particularly for those infected with HIV/AIDS. Many households still have not recovered, and, with another bad harvest this year, decisive action is required.

“Malawi is facing a serious food shortage, “ said IMF Managing Director Horst Köhler, who, with World Bank President James Wolfensohn, has called on donor countries to step forward to support Malawi and other nations in southern Africa currently facing severe famine (see [News Brief No. 02/81](#)). “Our emergency assistance is a step toward helping the nation deal with its current food needs.”

Malawi’s food shortage is expected to be addressed through a combination of humanitarian aid of about 210,000 metric tons of grain, which will be distributed to about 30 percent of Malawi’s population, or about 3.2 million people, and maize imports by the government of up to 350,000 metric tons.

The IMF provides emergency assistance to member countries hit by natural disasters so that they can meet immediate balance of payments financing needs, and maintain or restore macroeconomic stability. The emergency loan, which currently carries a charge of 2.96%, will be repaid in eight equal installments over 3 1/4 and 5 years.

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