

Malawi: Selected Issues and Statistical Appendix

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MALAWI

Selected Issues and Statistical Appendix

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Approved by the African Department

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I. THE MALAWI BUDGET AND FISCAL POLICY¹

A. Introduction

1. **In Malawi, budget plans and outturns have differed significantly for a number of years with many adverse consequences.** The cumulative effects of repeated fiscal overruns have resulted in a precarious macroeconomic situation that is characterized by high domestic debt, high interest rates and interest expenditures, severely restricted non-interest budget envelope, high deficits, and rising inflation. In addition, such deviations affect the whole budget process. While deviations are a sign of a weak budget process, they also undermine the implementation of the next budget plan, resulting in renewed deviations. Ultimately, systematic deviations complicate the fiscal policy reaction to the macroeconomic situation.

2. **A budget is the quantified policy statement of a government, but systematic, repeated, and significant deviations of budget plan and outturn undermine the policy message.** Such deviations hinder outside stakeholders' understanding, and reactions to fiscal policies. For example, a Malawian banker was recently quoted as saying that "budgets have lost so much credibility that businesses stopped paying attention to their economic impact."² But not only outsiders are affected. Frequent policy shifts and unpredictable changes in resource allocations also impede civil servants' efforts to manage projects and programs and to achieve results. And not least, if such deviations become routine, they reduce accountability and transparency, both for politicians and civil servants. It is difficult for outsiders to monitor the legitimacy of administrative resource reallocations, and hence the automatic acceptance of such deviations can let inappropriate diversions of resources go unnoticed.

3. **This chapter analyzes the budget deviations in Malawi, their reasons, and the consequences for the fiscal policy process.** It documents the observed deviations of outturn to plan in Malawi, analyzes the reasons for such deviations, outlines some of the consequences, and considers options and actions needed for improvements.

B. Budget Plans and Budget Outturns in Malawi

4. **Budget plans and budget outturns differed significantly for key indicators.** For the past seven years expenditures exceeded program plans (often by more than 3 percent of

¹ Prepared by Christiane Roehler (FAD)

² Reported in "Malawi Nation", September 22, 2004, Internet Edition. The article reported on a post budget seminar of the previous week that had been organized by the Society of Accountants in Malawi (Socam) and was attended by high ranking government officials and business executives.

GDP), and in every year the domestic borrowing target was exceeded.³ But as the comparison with the initial medium-term projections shows, even before the beginning of the fiscal year annual targets were often revised significantly from the initial medium-term plan to the agreed annual program. Increases and decreases of expenditure targets exceeded 3½ percent of GDP for 4 out of 6 years with available data.

5. **The violation of annual program plans was particularly marked during 2002/3 and 2003/04.** Expenditures in both years were higher than planned by 8 percent of GDP. And instead of a repayment of domestic debt of more than 3 percent of GDP in each year, domestic borrowing reached 15 and 8 percent of GDP, respectively. Nevertheless, adjustment effort measured by the underlying balance⁴ was about 1 percent of GDP during each of these two years because of strong revenue performance. Domestic tax and non-tax revenue increased from expected collections of about 18 percent of GDP for the period 1995/96–2001/02 by about 2½ percent of GDP each year to 23½ percent of GDP in 2003/04.

6. **In order to understand the reasons for these significant shifts in more depth, the analysis uses the evolution of fiscal estimates for FY 2003/04 as a representative example.** Table I.1 presents detailed fiscal projections for 2003/04 made at different points of time. The analysis focuses on annual projections only because these relate to the published budget plans and the legally binding expenditure limits set by parliament.

7. **Even when some aggregate components of the 2003/04 budget evolved smoothly, there were significant compositional shifts.** “Other recurrent expenditures” for 2003/04 were targeted at about 11½ percent of GDP during the budget planning period 2002/03 and were compressed by 1½ percent of GDP under the first review program. However, general resources available to ministries declined from 8.6 percent of GDP in June 2002 estimates (which would have been an increase relative to previous years and was to be used for additional pro-poor spending) to 7.2 percent of GDP in the approved budget; they were disproportionately compressed under the first review program.

³ See Malawi—Ex Post Assessment of Longer-Term Program Engagement, <http://www.imf.org>. In particular, see p. 22.

⁴ This is a measure of domestic primary balance: Overall balance plus statistical discrepancy, excluding grants, revenue from maize, total interest, expenditure for maize, and foreign financed development expenditures.

Table I.1. Fiscal Developments, 2001/02 - 2004/05
(In percent of GDP, unless otherwise indicated)

	2001/02		2002/03		2003/04				2004/05			
	Actual	July 02 Art. IV 02	Oct 03 Actual 4/	July 02 Art. IV 02	Jan 03 Mission	May 03 Mission	July 03 Official Budget	Oct 03 1st Rev. PRGF 4/	Jan 04 Mission	April 04 2nd Rev. PRGF Draft	July 04 Actual	July 04 SMP
Revenue and grants	24.1	28.6	27.7	28.4	30.7	33.9	34.6	34.7	35.7	35.2	36.0	35.7
Revenue	17.2	18.0	20.7	17.8	20.9	20.8	20.8	21.8	23.3	23.2	23.5	24.0
Tax revenue	15.3	16.1	17.7	16.1	18.1	18.0	18.0	19.3	19.6	19.5	20.3	20.7
Non-tax revenue	1.9	1.9	3.1	1.7	2.8	2.8	2.8	2.5	3.7	3.7	3.2	3.3
of which: Maize	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.8	0.8	0.7	1.0
Grants	6.9	10.6	6.9	10.6	9.7	13.1	13.8	13.0	12.3	12.0	12.5	11.7
Total expenditure and net lending	31.9	31.4	39.7	28.5	31.8	33.3	32.8	35.2	38.1	40.3	43.3	40.0
Wages and salaries	6.9	6.2	7.1	6.2	7.3	6.6	6.6	6.3	6.5	6.6	6.8	7.1
Interest	5.1	4.7	7.1	2.4	4.4	6.0	6.0	9.6	10.4	10.7	11.0	9.0
Domestic	3.9	3.2	5.7	0.9	2.9	4.6	4.6	8.0	8.9	9.2	9.5	7.8
Foreign	1.2	1.4	1.4	1.4	1.4	1.4	1.4	1.5	1.4	1.5	1.5	1.2
Other recurrent	12.5	12.3	17.9	11.9	11.5	11.4	11.2	10.1	10.6	11.5	14.2	15.1
General recurrent (not further identified)	7.8	6.9	8.6	8.6	...	6.8	7.2	5.4	6.2	6.8	7.9	8.0
Maize/ fertilizer/ TIP	0.3	1.2	4.4	0.1	...	0.0	0.0	0.0	0.0	0.1	0.3	2.5
ADMARC/NFRA	0.6	0.8	1.3	0.0	...	0.0	0.0	0.0	0.0	0.2	0.2	0.6
National elections	0.0	0.0	0.0	0.0	...	0.9	0.9	0.9	0.9	0.8	1.1	0.0
Pensions and gratuities	1.0	1.0	0.9	1.0	...	1.0	1.0	1.0	0.9	0.9	1.1	1.1
Transfers to MRA and NRA from earmarked revenue	1.4	1.2	1.2	1.1	...	1.3	1.1	1.3	1.3	1.3	1.3	1.2
Subventions	1.1	1.1	1.4	1.1	...	1.5	1.1	1.5	1.1	1.1	1.6	1.6
Arrears	0.3	0.0	0.0	0.0	...	0.0	0.0	0.1	0.2	0.2	0.7	0.2
Domestic development	1.5	1.7	1.5	2.0	1.9	1.5	1.8	1.2	1.3	1.3	1.8	1.0
Foreign development	5.8	6.5	6.2	6.1	6.7	7.8	7.1	8.1	9.3	10.2	9.5	7.8
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-7.9	-2.7	-12.1	-0.1	-1.2	0.5	1.8	-0.5	-2.4	-5.2	-7.3	-4.3
Financing	6.9	2.7	11.7	0.1	1.2	-0.5	...	1.8	3.7	6.4	8.2	4.3
Foreign total	-0.2	6.5	-0.5	3.3	2.7	5.1	...	4.8	5.7	4.9	0.2	2.3
Borrowing, and accounts, special loans, BOP gap etc	2.4	9.6	3.1	6.6	6.5	8.8	...	8.5	9.7	8.9	4.4	6.2
Amortization	-2.6	-3.2	-3.5	-3.3	-3.8	-3.7	...	-3.7	-4.0	-4.0	-4.2	-3.9
Domestic	7.1	-3.7	12.2	-3.2	-1.6	-5.6	...	-3.1	-2.1	1.5	8.0	1.9
Financial instruments	6.9	-3.9	12.4	-3.4	-1.8	-5.8	...	-3.1	-2.1	1.5	8.0	1.9
Other	0.2	0.1	-0.2	0.2	0.2	0.2	...	0.0	0.0	0.0	0.0	0.0
Statistical discrepancy	1.0	0.0	0.3	0.0	0.0	0.0	...	-1.3	-1.2	-1.2	-0.9	0.0
Memorandum items:												
Nominal GDP (millions of Malawi Kwacha)	133,004	150,794	154,340	165,628	170,127	173,279	173,279	174,600	180,178	181,525	181,560	216,129
Maize operations: revenue less expenditure	...	-1.1	-3.6	0.0	0.0	0.0	...	0.0	0.8	0.8	0.7	-0.3
Underlying balance 1/	-2.8	-0.9	-1.8	-2.3	0.2	1.3	...	2.9	3.6	1.8	-0.9	1.2
Net foreign financing contribution 2/	0.8	10.5	0.3	7.8	5.7	10.4	...	9.7	8.8	6.6	3.2	6.2
Net domestic debt, ending balance as of June 30 3/	10.2	5.1	21.2	1.3	7.1	11.9	...	15.6	16.0	19.5	25.9	23.7
Net domestic debt, starting balance as of June 30 3/	...	9.0	8.8	4.6	8.9	17.7	...	18.7	18.1	18.0	18.0	...

Source: Malawi authorities; and IMF staff estimates.

1/ Defined as overall balance plus statistical discrepancy, less grants, less revenue from maize, plus total interest, plus expenditures for maize, plus foreign-financed development expenditures.

2/ Foreign grants plus foreign financing, less revenue from maize, plus expenditures for maize, plus foreign-financed development projects.

3/ Central government debt instruments, net of bank accounts.

4/ Includes 2001/02 and 2002/03 maize operations.

C. Explanations for the Observed Budget Deviations Overview

8. **In Malawi, deviations from the budget plan can be attributed to all aspects of the budget process, but also difficult external factors.** Budget planning is weak and the initial budget plan often cannot be implemented as stated. During budget implementation the directives of the budget have not been observed by the senior leadership, and public expenditure management regulations that bind the administration are not fully enforced. And last, budget monitoring and evaluation is complicated by the poor quality of budget information that reduces the credibility of budget announcements. In addition and interlinked with the three stages of the budget process, external factors create the need for within-year adjustments. Examples of such external factors include the pre-existing conditions created by the previous year's outturn, uncertainties about foreign aid flows, drought, and food supplies shocks and the terms of trade.

Budget planning

9. **Missed fiscal objectives in the previous year create the need for fiscal adjustments from the beginning of the fiscal year.** Table I.1 above shows that projections of domestic debt stocks and related interest payments for 2003/04 were continuously revised upward. As the budget framework needs to be prepared a few months before the beginning of a fiscal year, the approved budget underestimated the required interest expenditures initially by 3½ percent of GDP (and in the event by 5 percent of GDP) and hence overestimated the resource envelope for non-interest expenditures. Comparing the approved 2003/04 budget with the program at the first review, reductions of domestic discretionary expenditures⁵ of 1.7 percent of GDP were considered necessary to set in motion a virtuous cycle of domestic debt reduction and a reduction in domestic interest rates.

10. **Malawi's budgets in the past did not include all required and foreseeable expenditure.** While funding for ministries in the first part of FY 2003/04 was restrained, significant unbudgeted spending was funded. Some additional funding was made available to individual budget votes, but in particular the "special activities" vote controlled by the Ministry of Finance was used to record such spending. It is estimated that unbudgeted special activities for expenditures such as arrears, and payments on transportation equipment contracts exceeded 2 percent of GDP.

11. **Budget estimates for some expenditure are systematically poor, partly because of weak expenditure management.** The wage bill, and pensions and gratuities are often underestimated, and a recent audit of domestic arrears uncovered also pension arrears. Similarly, large accumulated utility arrears impede estimation of a baseline of required expenditures.

⁵ Domestic discretionary expenditures are other current expenditure (i.e., the recurrent budget excluding wages and salaries and interest) plus the domestically funded development budget.

12. **Budget planning instructions demand a reduction in certain expenditures, but no policy changes in support of such directives are instituted.** A long-term issue in this regard has been the size of the travel budget. In many fiscal years the travel budget exceeded 30 percent of the wage bill (Table I.2). While some progress has been made in restraining the travel budget recently, no changes to the rules and reimbursements for travel were instituted.

Table I.2. Travel Expenditures, 1999/00 - 2004/05
(In millions of Kwacha)

	Approved budget	Revised or Actual 1/	Change (in percent)		Revised as share of wage bill or Approved as share of wage bill
			Revised over Approved	Later over Earlier	
FY 1999/00	1,022	1,622	58.7	...	37.8
FY 2000/01	1,613	2,363	46.5	...	39.7
FY 2001/02	2,198	2,609	18.7	...	28.4
FY 2002/03	3,867	3,799	-1.8	...	34.8
FY 2003/04, Original	3,193	...	...	...	27.9
FY 2003/04, Supplementary	2,358	...	...	-26.2	20.1
FY 2004/05, Instructions 2/	1,769	...	...	...	11.8
FY 2004/05, Budget document	3,331	...	...	88.4	21.8

Source: Malawi authorities; and IMF staff estimates.

1/ Budget circular for the 2004/05 budget.

2/ Based on budget documents.

13. **The budget reserve for unforeseen expenditures is negligible, but Malawi effectively has additional reserves in the form of humanitarian donor assistance and the strategic grain reserve.** A budget reserve in a poor country like Malawi is difficult to defend politically. However, Malawi is regularly subject to shocks, in particular to the food supply. Government intervention on short notice beyond the assistance provided by development partners have been a major contributing factor to overexpenditure and the current overall macroeconomic difficulties.

14. **Malawi's budget planning process is focused on domestic resources, although large amounts of foreign assistance are managed by government agencies.** Malawi's budget plans (and monitoring) do not fully include foreign resources that are available for recurrent spending but subject to some restrictions. Recent examples include the lack of budgeting for resources in an account of Japanese debt relief, food assistance from the European Union for the Strategic Grain Reserve, a grant for environmental programs from USAID, and a World Bank emergency loan. Such resources are often treated as project financing even though they are available as direct substitutes for the government's own revenue. Hence, these resources are often not utilized fully nor timely, increasing the pressure on domestic financing.

15. **The budget is fragmented because foreign project resources are only partly integrated into policy design.** Even though many projects are effectively executed outside normal government budget management procedures, they substitute for the government's own resources. Anecdotal estimates suggest that more than 50 percent of grants are not reflected in the budget. Hence the resources available for government policy are significantly underestimated. Also, many projects seem to include recurrent expenditure components, not only capital expenditures. For example, the expansion in 2004/05 of the government's targeted input program is to a large extent substituting for a program previously operated by the United Kingdom DFID. While United Kingdom shifted its aid into other sectors and reduced recurrent expenditures on food security programs, only the government's expenditure increase in reaction to this shift is reflected in the budget documents, distorting an analysis of budget developments.

16. **Revenue projections are not based on a detailed analysis.** As the EPA shows, revenue swings can be very significant. Shortfalls have been as large as 5 percent of GDP, while more recently revenue collections exceeded projections by 2½ percent of GDP per year. As the reasons behind these stark changes are not well understood, projection errors are easily made, resulting in violations of the macroeconomic framework.

17. **The annual budget is not well integrated into a medium-term planning framework.** While some medium-term plans exist,⁶ medium-term considerations do not seem to guide the preparation of the annual budget. The EPA shows large swings in expenditures between the medium-term program projections and the initial annual budget. Some adjustments were caused by necessary reactions to macroeconomic developments. However, unpredictable increases and contractions of allocations prevent government agencies from planning their activity level and adjusting the size of their operations accordingly, leading to requests for extrabudgetary funding.

Budget implementation

18. **Budget implementation is characterized by repeated attempts to reduce spending by administrative cuts within the year, often in response to macroeconomic considerations or emergency spending needs.** Hence, ministries cannot expect to receive the full cash allocation, and moreover, cash releases may only be made late in the fiscal year. This complicates planning for ministries. In order to be able to enforce cash sequestration, the "cash budgeting system" was introduced. Under this system, ministries are obliged to commit spending only up to the cash releases approved by the Ministry of Finance, which thus in principle retains full control over the available resources.

⁶ The Malawi Poverty Reduction and Growth Strategy Paper (MPRSP), the recently revived Public Sector Investment Program (PSIP), and the medium term projections presented in each budget document.

Table I.3. Malawi: Expenditure by Vote in the Recurrent Budget, 2003/04

	Actual compared to original budget	Actual compared to supplementary budget
Aggregate overexpenditure (in percent of budget)	32	33
Overexpenditure (in percent of budget)	39	36
Underexpenditure (in percent of budget)	-7.0	-2.9
Number of votes with overexpenditure		
> 50 percent	5	13
25 - 50 percent	5	4
10 - 25 percent	6	7
0 - 10 percent	4	11
Total votes with overexpenditures	20	35
Share of budget in votes with overexpenditure (in percent)	73	78
Number of votes with underexpenditure		
0 - 10 percent	5	4
10 - 25 percent	8	13
25 - 50 percent	21	6
< 50 percent	5	1
Total votes with underexpenditure	39	24
Share of budget in votes with underexpenditure (in percent)	27	22

Source: Malawi authorities; and IMF staff estimates.

Note: The analysis includes 59 out of 63 votes. Excluded are the statutory expenditure votes presidency (only personnel emoluments) and debt service, and the voted expenditures from earmarked revenues to the MRA and NRA. Both the MRA and NRA received higher allocations than was budgeted.

19. **In the event, cash sequestration often failed, but allowed for significant shifts of resources between expenditure votes.** Votes representing more than 70 percent of budget allocations had overexpenditures in 2003/04, and some votes exceeded their allocation by more than 50 percent (Table I.3). On the other hand, some votes were severely constraint, receiving less than 50 percent of their initial allocation.

20. **Extrabudgetary requests were approved regularly.** As cash allocation is under the control of the Ministry of Finance, overexpenditures can only occur with its approval. The sizable overexpenditures for statehood activities indicate that such extrabudgetary requests were condoned by senior leadership (Table I.4).

Table I.4. Statehood Expenditures, 1998/99 - 2004/05, 1/
(Millions of Kwacha)

	Approved budget	Supplementary	Revised or Actual
FY 1998/99	238	297	227
FY 1999/00	345	...	621
FY 2000/01	663	...	1,059
FY 2001/02	1,142	...	1,373
FY 2002/03	1,194	...	1,844
FY 2003/04, SMP 2/	1,617	1,753	2,521
FY 2004/05, SMP 2/	1,824	...	2,024

Source: Malawi authorities; and IMF staff estimates.

1/ Statehood expenditures here are defined as voted expenditures (wages and salaries, and goods and services) for Office of the President and Cabinet, Office of the Vice Presidents, State Residences, and National Assembly. Data except for "Accounts" column are from budget documents.

2/ Data in the "Revised or Actual" column refer to the printed 2004/05 budget document.

21. **The practice of significant within-year adjustments to resource allocations provides incentives to circumvent public expenditure management (PEM) regulations and procedures.** While ministries are not allowed to commit beyond cash allocations, irregular cash releases encourage unauthorized commitments, as evidenced by the existence of arrears in ministries. As PEM regulations are apparently put aside at an early stage in the spending process, the general system of controls over public resources is not fully enforced. This provides increased opportunities for inappropriate diversion of resources, and the recent investigations of former senior officials for corruption attest to the weaknesses in governance. Such diversions increase the scarcity of resources for legitimate government spending needs.

22. **The existence of arrears creates new arrears, and undermines the enforcement of public expenditure management regulations.** The quarterly Auditor General reports on arrears show⁷ that ministries regularly clear a large share of their acknowledged arrears, while creating new arrears on invoices received during the reporting period. Moreover, the 2004 special audit of domestic arrears has uncovered significant additional arrears which were not documented in the ministries' accounting records. Whenever payments for such unacknowledged arrears are being made, PEM regulations have to be violated, and at the same time payments for current period expenditures curtailed.

23. **The government lacks full control over the wage bill.** Even though no general wage increase has been approved since 2000/01, the wage bill has increased significantly (Table I.5). An important reason was the introduction of new policies with significant within-

⁷ These reports are based on ministries' data from the commitment control system (CCS).

year cost implications, for example the contractual scheme for senior staff and new benefits for all civil servants. However, even during 2003/04 when no such effects were present and the government had committed to a hiring freeze outside of the social sector, the wage bill continued to increase as a share of GDP.

Table I.5. Wage Bill, 1998/99-2004/05
(In percent of GDP)

	Plan 1/ Wage bill		Actual Wage bill	
	Million MK	Percent of GDP	Million MK	Percent of GDP
FY 1998/99	3,155	5.5	3,209	4.8
FY 1999/00			4,296	4.7
FY 2000/01	6,066	5.3	5,954	5.2
FY 2001/02	7,795	5.9	9,201	6.9
FY 2002/03	9,283	6.2	10,930	7.1
FY 2003/04 2/	11,431	6.6	12,302	6.8
FY 2004/05	15,300	7.1		

1/ Planned wage bill is reported based on estimates close to the beginning of the fiscal year.

2/ Planned wage bill as per budget. The program at the first review aimed at a wage bill of 6.3 percent of GDP. Outturn as per SMP.

24. **Public expenditure management and controls are weak, a fact that has been extensively documented elsewhere.**⁸ While many of the weaknesses in PEM can be attributed to a lack of enforcement by senior leadership, technical capacity also seems to be on a decline. For example, incomplete and inconsistent budget reports are frequent; bank account reconciliation is not timely and is incomplete; below-the-line accounts are not cleared; financial record management is weak; and internal audit is very limited. These systemic issues reduce the potential control that could be exercised by the government.

Budget monitoring and evaluation

25. **Malawi's budget classification structure and budget documentation allow a satisfactory understanding of government policies, but weaknesses arise in practice.** Malawi's budget is classified in a detailed administrative, economic, and program

⁸ A summary of PEM systems and issues was provided as background to the 2002 Article IV consultation (Malawi—Selected Issues and Statistical Appendix,” 2002, in particular Chapter III, “Selected Expenditure Management and Fiscal Data Issues”). Other reports include “Malawi—Country Financial Accountability Assessment,” 2003, World Bank, Report No. 26765-MAI; Government of Malawi: “Malawi Financial Accountability Action Plan,” March 11, 2003; “Malawi—HIPC Assessment and Action Plan,” 2004 (forthcoming); and “Malawi—HIPC Assessment and Action Plan,” 2001.

breakdown, which is the main classification for the management of budget execution and accounting. In the budget documents, programs state their objectives and expected outputs, allowing some output orientation, in addition to the input-oriented detailed classification. However, the summary volume of the budget documentation is presented in an output classification which does not align with the subprogram structure of the detailed budget allocations. Thus, it is not possible to move directly from detailed budget execution reports based on accounts to policy reports in the output structure. Moreover, protected pro-poor spending is only allocated and reported in the output classification. Thus, pro-poor spending during budget execution can only be monitored with the assistance of supplementary reports, and not from the main budget execution and accounting system. Currently, reports on pro-poor spending rely on cash release information from the Ministry of Finance.

26. **The quality of fiscal data is poor, creating additional uncertainty about the fiscal position.** Fiscal reporting is to take place on a cash basis. However, most expenditure data are reported at the funding stage, i.e., at the stage of cash releases by the Ministry of Finance, not at the “check issued” stage. Reporting at the funding stage does not allow the monitoring of the actual use of resources by line ministries, which may shift resources, and only an administrative and broad economic breakdown is available. Hence the use of funding data decreases accountability for ministries. Moreover, there are significant time lags between cash releases and the payment stage, making cash management and projections difficult. Alternative data from the government’s payment system are not currently used for cash management.⁹ But in addition to the systemic weakness of using funding data for fiscal reporting, compilation errors and data revisions are common, even though funding data should be under the direct control of the Ministry of Finance.

27. **Baseline information is lacking that is necessary to determine appropriate policies for the future.** Monthly expenditure reports from line ministries that report at the “check-issued” stage and provide details on the economic and program classification are often incomplete or inconsistent. Until recently, final accounts data were compiled with such long lags that their information was no longer relevant for current fiscal decisions. However for the first time in many years the 2002/03 accounts were prepared within 12 months, and hence provide more timely details on spending patterns.

28. **The incomplete coverage and parallel administrative structures of foreign financed projects weaken budget monitoring and evaluation.** The special administrative structures that are often used to ensure satisfactory accountability to the donors complicate

⁹ The government manages its payments through the Credit Ceiling Authority (CCA) System that is operated by the Reserve Bank of Malawi. As the system manages separate bank accounts for each ministry and broad economic spending category, data from this system would allow an aggregate assessment of budget execution at the payment stage. The use of these data for budget monitoring is being developed under the current Staff-Monitored Program.

monitoring of projects for the government. In addition, the use of the government's own resources for managing foreign projects cannot be determined, because many projects are not even included in fiscal reports. Also, information on the nature of spending is missing as foreign projects classified in the development budget (which is presumably the capital budget) contain recurrent components. Some projects directly support recurrent spending requirements (like the DFID targeted input program), while most projects have a technical assistance and capacity building component. Project financing typically also covers administrative expenses, which may be significant because of the duplicative project management structures.

External factors

29. **External factors are an important reason for observed budget deviations.** Two types of such external factors may be distinguished. First, economic shocks—in Malawi's case in particular, poor harvests and international price changes to oil and tobacco—need immediate reaction that may include higher spending. Second, the resource flows from international aid are decided by third parties and may be delayed, altering the resource envelope. While all countries need to deal with external factors, the weak budget management practices detailed above at times aggravated them. For example, the small budget reserve implies that any within-year government decisions on additional social assistance should be off-set by spending cuts elsewhere in order to stay within the macroeconomic framework. Such cuts, however, have been difficult to implement, and usually overexpenditure have arisen. This problem is worsened because of preexisting commitments such as debt service or civil services wages cannot be changed in the short term.

30. **Malawi's poverty limits the scale of government interventions, even though humanitarian needs are pressing.** Malawi's economy and government resources are small relative to basic needs of the population, and even small external shocks—for example to the food supply—can necessitate assistance for a large share of the population. Short-term financing can only be obtained on the domestic market, but this immediately crowds out credit to the private sector and impedes long-term development of the country. Even bridge financing in advance of foreign assistance can be very costly to the government. Hence, Malawi is effectively operating under a binding cash constraint, requiring cuts in other spending, in order to avoid macroeconomic destabilization. Recently, however, sufficient cuts could not be implemented, which set in motion the vicious cycle observed over the last two years.

31. **Malawi is highly aid dependent, but such aid can be volatile.** Table I.1 shows that the net foreign financing contribution toward the recurrent budget was much less than anticipated in 2003/04 and such shortfalls occur regularly. Uncertainties about the amount and timing of resource flows arise in particular for flexible budget support, because donor conditionality can be stringent. If the Malawi government misses agreed reform targets, a political decision about the release of funds is required from the donor organization.

32. **The share of flexible spending in the short term is fairly small.** A large part of the expenditure program is determined by the implementation schedule of foreign financed projects, and the interest bill, wage bill, and spending from earmarked resources can only be adjusted over time. Thus, for macroeconomic stabilization reason it was considered necessary to attempt a compression of “general recurrent spending (not further identified)” under the 2003/04 fiscal program by about 2½ percent of GDP relative to previous levels of 8 percent of GDP.

D. Implications for Fiscal Policy

33. **Malawi is locked into a self-reinforcing cycle of poor budgeting.** Under budgeting of required spending, erratic within-year cash allocations, the existence of arrears, and other weaknesses of the budget process lead to missed targets for the fiscal year. As the upcoming budget is planned on the basis of such targets, the new budget also becomes difficult to achieve, leading to a new cycle of missed targets.

34. **Fiscal policy announcements are not credible because of weaknesses in all aspects of the budget.** A history of weak budget plans and weak fiscal data on budget outturns reduce the value of the budget documents. Overspending and the significant shift in resources across expenditure votes required the acceptance and approval of senior government leadership. In addition, weak expenditure management practices at the ministry level and at the Ministry of Finance reduce transparency and accountability, making it difficult for outsiders to penetrate government actions. Simultaneous action will be needed to improve credibility.

35. **Malawi is receiving significant external assistance but unless budgeting is improved, stakeholders will be reluctant to put resources at the full disposal of the government.** Thus the fragmentation of the budget into a domestic section and project financing is perpetuated, and the uncertainties about resource flows for the financing of the recurrent budget remain.

36. **Volatile cash flows reduce the efficiency of government operations.** Only a small share of ministries’ expenditures can be adjusted in the very short term. Hence, expenditures are being incurred for wages and salaries, and fixed costs, while necessary complementary resources are missing to carry out the planned work.

37. **Arrears lock the Malawi government into high cost procurement as private suppliers will anticipate delays in payment.** Requirements for advance payments put additional strain on available cash resources, and reduce the government’s leverage for demanding delivery of service up to the specified standard. Payment processes also become more costly as suppliers demand safeguards through bank guarantees.

38. **Malawi is highly vulnerable to external factors, but improved budget planning would allow better preparation.** In particular, better medium-term planning would identify the scope for short-term interventions to ameliorate external shocks without risking

macroeconomic stability. It would also allow for a considered and phased process of adjustment of expenditures that can only be shifted over the medium term.

E. Options and Actions

39. **In order to break the cycle of budget deviations and improve fiscal policy delivery, simultaneous improvements of budget planning, implementation, and information provision are needed.** While it will take time to build confidence, delivering a budget with few deviations would provide a strong signal that reforms undertaken take hold. But even if deviations are necessary, for example because of external shocks, regular, timely and well-prepared information about budget developments and their reasons would help.

40. **The new government is already taking actions to improve the budget process.**

- The senior leadership of the new government has publicly committed to the integrity of the budget, i.e., to include all required and foreseeable expenditures in the budget plan, and to reject extrabudgetary spending requests.
- A strategy for public expenditure management reforms, the “Malawi Financial Accountability Action Plan,” was approved by Cabinet in May 2004. Support for key elements of this plan has been committed by UK’s DFID, and the World Bank.
- Public expenditure management is to be improved by placing experienced civil servants in line positions at the Ministry of Finance and Accountant General’s Department. It is expected that these staff would immediately improve fiscal management, initiate the enforcement of regulations, and push the medium-term reform process forward.
- An audit of domestic arrears is being carried out by an external audit firm under the supervision of the Auditor General. This work could provide the basis for reinstating commitment controls, and addressing the stock of existing arrears and breaking the cycle of arrears creation. Some arrears were already cleared in 2003/04, and additional clearance is expected in 2004/05.
- The final accounts for 2002/03 were prepared within 12 months of the end of the fiscal year, strengthening the information base for next year’s budget process.
- The Public Sector Investment Program (PSIP) is being revived, and as a first step a comprehensive database of all foreign financed projects is being created. This prepares the way for a better integration of such projects into budget planning.
- Negotiations are under way to support the recurrent budget in the health sector through a six-year program, which would be pool-funded by a number of donors. This arrangement would make some foreign resource flows more predictable.

- Technical assistance on tax policy has been requested, which would also be beneficial to improvements of revenue projections.

But additional actions would be desirable to improve the guidance provided by the budget to government insiders and outside stakeholders.

41. **A government-owned medium-term policy perspective is needed with a particular focus on the strategy for macroeconomic stabilization by reducing domestic debt.** It is the prerogative, but also the responsibility of the government of Malawi to set the fiscal policy framework. A medium-term framework will allow phased adjustments needed for macroeconomic stabilization, the initiation of structural reforms, the integration of the large amount of unbudgeted foreign grant aid into the budget policy framework, and informed discussions with development partners about budget and project aid. Key decision that the government is likely to face include:

- Size of government. Higher domestic revenues would allow more public expenditure, including pro-poor spending, and reduce the dependency on foreign aid. However, increased revenue puts a burden on the private sector and restrains private sector growth.
- Intertemporal trade-offs. The current size of domestic debt imposes significant restrictions on the size of public expenditures, and hence debt reduction is desirable. The government will need to decide jointly on the time path of public expenditures and debt reductions.
- An outline of anticipated key policy reforms. These include the next step of the wage policy and size and structure of the civil service, and reforms to the pension system.

42. **In the context of the medium term plan, budget reserves should be assessed, including available humanitarian assistance.** On this basis, contingency plans for government interventions to external shocks should be developed (jointly with development partners), to avoid the disruptive effects of large expenditure overruns and debt stock increases.

43. **Forceful steps should be taken to improve expenditure management, and budget information.** This forms the basis for building confidence in the government's ability to manage resources and deliver the budget promises.

44. **While improved budget management is important and can contribute to better utilization of government resources, the resolution of some pressing policy issues may be beyond Malawi's resources, and will require international cooperation.** For example, addressing the shortages of qualified health professionals will require difficult decisions on the appropriate level of supplementary wages. Higher wages will attract health personal, but will reduce incentives for staff to join other important services like the teaching service.

Similarly, HIV drugs are only affordable with foreign assistance. A better budget plan will support a good discussion on such issues, and help attract additional resources.

F. Conclusion

45. **Improvements to all aspects of the budget process are essential to Malawi's development goals.** Governments are large and highly diverse organizations, and managing a turnover of 30–40 percent of the annual output of an economy is always a challenge. In Malawi these challenges are amplified by pressing humanitarian needs, binding cash constraints, unpredictable resource inflows, fragmented budget formulation and execution, and weak public expenditure management. However, only if government actions become better focused and more predictable by strengthening the budget process, more effective utilization of available government resources can be expected. Commitment by the senior leadership toward better budget processes is an important step, but needs to be proven in the future. In addition, the difficult public expenditure management reforms need to be pursued. Better understood and predictable fiscal policy would reduce uncertainty for development partners, as well as the private sector and stimulate their activities and engagement.

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II. A NOTE ON PUBLIC DOMESTIC DEBT SUSTAINABILITY¹⁰

A. Background

46. **Recent economic developments in Malawi have been characterized by significant fiscal overspending, with the overall fiscal deficit, excluding grants, averaging 17 percent over the past two fiscal years.** The authorities, receiving less external support than they anticipated, have resorted to domestic financing. As a result, interest rates and government domestic debt have risen, threatening macroeconomic stability and Malawi's implementation of its poverty reduction strategy.

47. **Domestic and external public debt share important characteristics but are also fundamentally different in several ways.** Both types of debt are liabilities of the government and must be serviced. External debt is denominated in foreign currencies and, therefore, carries an exchange rate risk. In addition, for Malawi, external debt is highly concessional and generally longer term, whereas domestic debt is almost entirely short term and carries high market interest rates. Thus, a high level of domestic debt generally warrants a different policy response than debt denominated in foreign currencies.

48. **There are, furthermore, several reasons why it makes sense to analyze the sustainability of domestic debt sustainability separate from external debt sustainability analysis.** First, the quality of historic data on domestic debt is frequently inferior to data on external debt, which makes comparability an issue. Second, the economic implications of domestic debt are fundamentally different from those of external debt. For example, domestic debt could stimulate the development of domestic financial markets, while over certain levels domestic debt could lead to higher domestic interest rates with economy wide repercussions through the effects on private sector investments. The impact of a default on domestic obligations would in many countries be more severe than a default on foreign obligations. Furthermore, it is also problematic to deal with sustainability of the total debt. An example would be if external debt were below a certain threshold for sustainability and domestic debt were reaching critical levels. In such a case, then there could be economic merit in increasing external borrowing to reduce the domestic debt.¹¹

49. Against this background, this note assesses the sustainability of Malawi's domestic debt. Section B describes the evolution and composition of the domestic debt, and Section C presents a simple debt sustainability model and applies some sensitivity analysis based on Malawian data. On the basis of the model, Section D discusses the merits of initiating an upfront fiscal adjustment as envisaged in FY 2004/05 budget versus continuing the recent

¹⁰ Prepared by Magnus Alvesson (AFR)

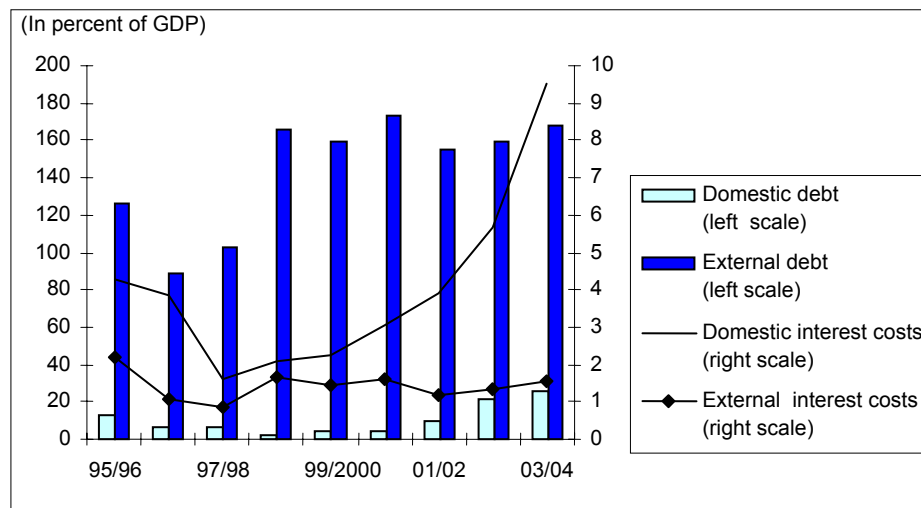
¹¹ See Debt Sustainability in Low-Income Countries—Further considerations on an Operational Framework and Policy Implications.

trends of lax fiscal policy implementation. The last section offers conclusions and recommendations.

B. Malawi Public Debt

50. While Malawi's nominal debt stock is predominantly external, debt-servicing costs originate mainly from its domestic debt (Figure II.1).¹² In 2000, Malawi reached its decision point under the HIPC initiative and has received interim debt relief in the order of US\$30-60 million per year.¹³ Although the external debt is substantial, Malawi is on track to reach its HIPC completion point. The rapidly increasing costs of servicing the domestic debt pose the largest risk to macroeconomic stability in the short to medium term.

Figure II.1. Government Debt and Interest Costs.



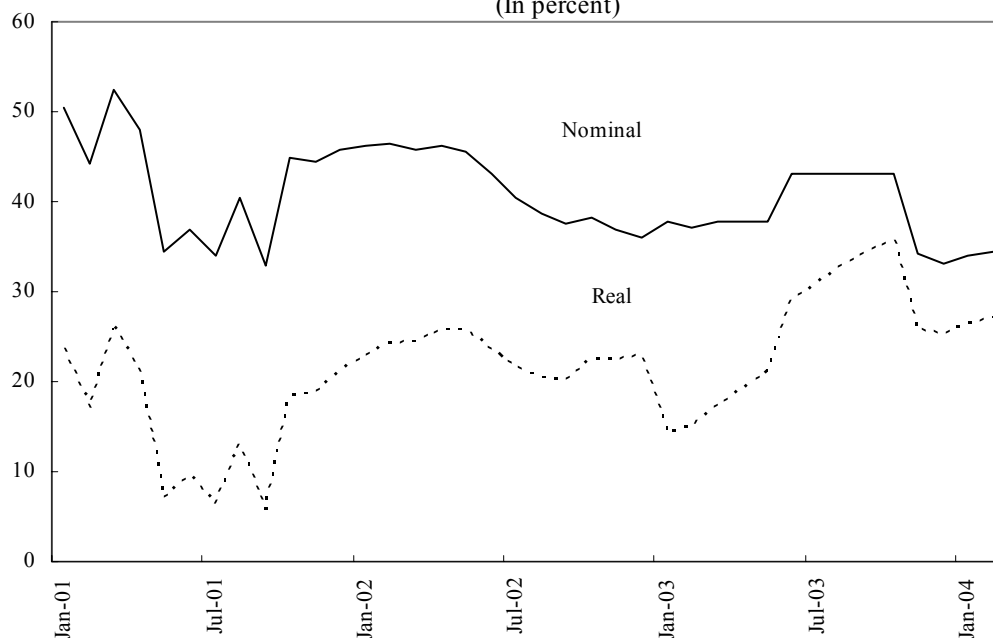
51. Domestic debt started to increase in 1999 and 2000 following above budget fiscal spending.¹⁴ With the start of the Poverty Reduction and Growth Facility Arrangement (PRGF) in late 2000, the government implemented a tight monetary policy that resulted in high real interest rates, further exacerbating the domestic debt burden (Figure II.2). Following a drought in 2001, Malawi experienced a food shortage in 2002 that, together with continued lax fiscal policy implementation, led to a rapid expansion of domestic debt, which stood at 23 percent of GDP at end-2003. Although inflation decreased, higher real interest rates on domestic debt service threaten pro-poor fiscal policy and macroeconomic stability.

¹² Domestic debt consists of all debt denominated in domestic currency.

¹³ For more information on the HIPC process, see Appendices VII and VIII in the accompanying Article IV staff report.

¹⁴ See Selected Issues Paper I. The Malawi Budget and Fiscal Policy (page 4).

Figure II.2. Nominal and Real Interest Rates
(In percent)



52. **Central bank financing of the government deficit increased rapidly in 2001; over the past four years, the Reserve Bank of Malawi (RBM) has held, on average, one-third of the government debt** (Table II.1). Debt-servicing costs remain high, however, because the government is charged market rates on debt held by the RBM, whose high operating costs have precluded any transfer of profits to the treasury.

Table II.1. Central Government Domestic Debt, 1997 - 2004 (end-June)

	1997	1998	1999	2000	2001	2002	2003	2004
(in millions of kwacha)								
Credit to government	3,338	767	2,273	5,897	9,069	25,821	38,397	47,104
Banking sector	1,235	-425	-719	485	5,829	15,626	18,694	27,025
RBM	586	-837	-781	-1,068	3,663	9,666	8,245	17,215
Commercial banks	649	411	63	1,553	2,166	5,960	10,449	9,809
Non-banks	2,103	1,192	2,991	5,412	3,240	10,195	19,703	20,080
Credit to government	3,339	767	2,273	5,897	9,069	25,821	38,397	47,104
Treasury bills, loans, and other	3,588	5,622	6,133	7,317	9,502	26,574	41,626	50,764
Bonds	599	600	830	878	2,315	3,777	3,752	3,734
Deposits	-848	-5,456	-4,691	-2,297	-2,749	-4,530	-6,981	-7,394
(In percent of total)								
Credit to government								
Banking sector	37.0	-55.5	-31.6	8.2	64.3	60.5	48.7	57.4
RBM	17.5	-109.1	-34.4	-18.1	40.4	37.4	21.5	36.5
Commercial banks	19.5	53.7	2.8	26.3	23.9	23.1	27.2	20.8
Non-banks	63.0	155.5	131.6	91.8	35.7	39.5	51.3	42.6
Credit to government								
Treasury bills, loans, and other	107.5	733.2	269.8	124.1	104.8	102.9	108.4	107.8
Bonds	17.9	78.3	36.5	14.9	25.5	14.6	9.8	7.9
Deposits	-25.4	-711.5	-206.4	-39.0	-30.3	-17.5	-18.2	-15.7

Sources: Malawi authorities; staff estimates

C. Domestic Debt Sustainability in Malawi

53. **Domestic debt sustainability (or, more generally, fiscal sustainability) can be analyzed through several different approaches.** Fiscal solvency can be distinguished from fiscal liquidity, sustainability, and vulnerability. The liquidity of the government is based on its ability to meet current obligations, while vulnerability measures the resilience of the government's fiscal position to shocks. Solvency of the government depends on a medium-term framework in which the primary surplus can finance interest costs under given assumptions for growth and inflation.

54. **The following model will measure, in a simple way, the solvency the fiscal policy in Malawi.** Various numerical indicators can be constructed to highlight inconsistencies between current policies and fiscal sustainability. In what follows, the sustainability analysis of Malawi's domestic debt is based on the concept of the primary gap indicator. However, the inclusion of foreign financing net of debt service reveals the degree to which external support reduces or, alternatively, adds to the domestic debt burden becomes explicit. Thus, domestic debt sustainability is defined as primary balance plus foreign financing in excess of foreign debt service (ds), as a share of GDP, exceeding the differential of nominal interest rate (r) and nominal GDP growth (y) times the beginning-of-period nominal debt as a share of nominal GDP (d):

$$ds_t \geq (r_t - y_t)d_{t-1}$$

55. The following section presents two scenarios that exemplify the potential impact of domestic debt dynamics in Malawi. The first scenario shows the benefits of an early adjustment, while in the second illustrates the cost of delaying adjustment.

D. Outlook Under Different Scenarios

Adjustment scenario

56. **The adjustment scenario assumes, in line with the budget, that domestic financing is contained at less than 2 percent of GDP in FY 2004/05** (Table II.2). The adjustment is achieved through a combination of lower expenditures, higher revenues and greater external support. Inflation is assumed to increase temporarily as a result of expansionary monetary policy in the first half of 2004, and economic growth is expected to remain relatively low before increasing to a level that will lead to poverty reducing later in the period.

Table II.2. Adjustment scenario, 2002/03-08/09

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
	Est.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.
Real							
Real GDP growth	3.1	4.1	4.1	4.3	4.9	5.6	5.9
Inflation (average)	10.5	10.4	19.9	9.4	7.8	6.2	6.0
Fiscal (in percent of GDP)							
Revenues	20.7	23.5	24.0	23.7	23.6	23.5	23.4
Grants	6.9	12.5	11.7	11.9	10.0	8.3	7.8
Expenditures	39.7	43.3	40.0	38.3	36.0	35.1	34.5
Of which: Domestic primary expenditures 1/	26.4	22.8	23.2	22.2	22.5	22.7	22.9
Of which: Domestic interest	5.7	9.5	7.8	6.8	4.2	3.0	2.3
Overall balance (including grants)	-12.1	-7.3	-4.3	-2.7	-2.4	-3.3	-3.3
Underlying balance 2/	-1.8	-0.9	1.2	1.6	1.1	0.8	0.5
Foreign financing (net)	-0.5	0.2	2.3	0.2	1.2	2.8	2.5
Domestic financing (net)	12.2	8.0	1.9	2.5	1.2	0.5	0.8
Statistical discrepancy	0.3	-0.9	0.0	0.0	0.0	0.0	0.0
Memorandum domestic debt dynamic variables							
Central government debt (net, percent of GDP)	21.2	25.9	23.7	22.9	21.5	19.6	18.3
Interest rate (weighted, percent)	42.2	37.9	31.6	26.2	19.9	15.7	12.7
Nominal GDP growth (percent)	15.5	17.6	19.0	16.2	13.1	12.1	11.9
Primary balance plus foreign finance (percent of GDP)	-6.8	2.4	5.9	4.4	3.0	2.6	1.5
Debt stabilizing level of primary balance and foreign financing (percent of GDP)	2.7	4.3	3.3	2.4	1.6	0.8	0.2

Sources: Malawi authorities; and Fund staff estimates and projections

1/ Expenditures excluding foreign financed development expenditures, and interest payments on foreign and domestic debt.

2/ A measure of domestic primary balance, excluding maize operations. Definition: Overall balance plus statistical discrepancy, less grants, less revenue from maize, plus total interest, plus expenditures for maize, plus foreign financed development expenditures.

57. **As a result of the adjustment in 2004/05, the primary balance including net foreign financing will exceed the level required to stabilize the debt, and domestic debt will start to decrease as a share of GDP.** Inflation will be contained and then start to decrease, and economic growth reach the level necessary for poverty reduction. Interest rates will come down, creating room for increased domestic primary expenditures and making a reduction of tax revenues possible. Furthermore, Malawi's dependency on foreign external aid is assumed to decrease.

Delayed adjustment scenario

58. **The delayed adjustment scenario, in contrast, offers no break with past fiscal performance for FY 2004/05 (Table II.3).** Overall expenditures remain high, and inflation continues to increase. Tax revenues are eroded and economic growth does not pick up after the recovery from the external shock in 2001.

Table II.3. Delayed adjustment scenario, 2002/03-08/09

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
	Est.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.
Real							
Real GDP growth (in percent)	3.1	4.1	2.5	1.0	2.0	3.0	3.0
Inflation (average)	10.5	10.4	30.3	34.0	16.0	12.0	10.0
Fiscal (in percent of GDP)							
Revenues	20.7	23.5	22.2	22.2	22.4	22.6	22.6
Grants	6.9	12.5	9.4	8.0	7.9	7.9	7.8
Expenditures	39.7	43.3	42.9	37.6	36.7	35.4	33.3
Of which: Domestic primary expenditures 1/	26.4	22.8	23.7	19.2	17.7	17.2	16.5
Of which: Domestic interest	5.7	9.5	9.1	9.6	9.7	8.9	7.5
Overall balance (including grants)	-12.1	-7.3	-11.3	-7.4	-6.4	-4.9	-2.9
Underlying balance 2/	-1.8	-0.9	-0.9	3.0	4.7	5.4	6.1
Foreign financing (net)	-0.5	0.2	1.2	0.2	0.6	2.8	2.5
Domestic financing	12.2	8.0	10.1	7.2	5.8	2.1	0.4
Statistical discrepancy	0.3	-0.9	0.0	0.0	0.0	0.0	0.0
Memorandum domestic debt dynamic variables							
Central government debt (net, % GDP)	21.2	25.9	27.3	29.9	31.8	29.9	27.1
Interest rate (weighted, percent)	42.2	37.9	41.4	36.3	33.4	30.7	27.7
Nominal GDP growth (percent)	15.5	17.6	40.0	20.0	15.0	14.0	12.0
Primary balance plus foreign finance (percent of GDP)	-6.8	2.4	-1.0	2.4	3.9	6.8	7.1
Debt stabilizing level of primary balance and foreign financing (percent of GDP)	2.7	4.3	0.4	4.5	5.5	5.3	4.7

Sources: Malawi authorities; and Fund staff estimates and projections

1/ Expenditures excluding foreign financed development expenditures, and interest payments on foreign and domestic debt.

2/ A measure of domestic primary balance, excluding maize operations. Definition: Overall balance plus statistical discrepancy, less grants, less revenue from maize, plus total interest, plus expenditures for maize, plus foreign financed development expenditures.

59. **The government is assumed to reduce fiscal expenditures in FY 2005/06 to avoid an unmanageable expansion of the domestic debt.** However, the scenario also shows that adjustment will be substantially costlier, and that domestic debt will only start decreasing only in FY2007/08 under this scenario. Furthermore, debt-servicing costs will remain high for an extended period, reducing the room for other fiscal expenditures.

Sensitivity analysis

60. **The model can also be used to illustrate the sensitivity of domestic debt sustainability in Malawi to changes in interest rates (Table II.4).**¹⁵

Table II.4. Scenario with a five percent increase in the interest rate

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
	Est.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.
Debt stabilizing level of primary balance (percent of GDP)	2.7	4.4	4.7	3.8	3.0	2.2	1.5
Debt (percent of GDP)	21.2	26.1	25.1	25.9	26.0	25.7	25.8
Interest rate (nominal, percent)	42.2	37.9	36.6	31.2	24.8	20.7	17.7

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

61. As shown by the table, a five percent increase in the nominal interest rate from FY 2004/05 onwards raises the domestic debt and the threshold for domestic debt sustainability in the medium term.

¹⁵ The sensitivity analysis is carried out relative the baseline scenario.

E. Conclusions

62. **Domestic debt dynamics analysis shows that Malawi is at a critical juncture.** A rising domestic debt and increasing debt-servicing costs jeopardizes pro-poor spending and macro economic stability. As shown above an early adjustment would lead to a path of lower debt servicing costs. However, if adjustment is delayed, the government will incur significant costs that will extend beyond the period of adjustment.

III. A NOTE ON THE RELATIONSHIP BETWEEN MONEY AND PRICES¹⁶

A. Introduction

63. **Fiscal slippages over the past two years have resulted in a large build-up in reserve money and a sizeable monetary overhang. This has created uncertainty over the future path of prices.** In addition, price increases in the past two years have been slow to catch up to growth in monetary aggregates (Figure III.1). This is true for both nonfood and food prices. In the past, movements in prices and money were more closely associated (Figure III.2). Therefore, one might expect a large buildup in inflation as the price level adjusts.

64. **Given the large uncertainty that exists over future inflation, it is important to try and understand the long-run relationship that might exist between money and prices, and whether or not there was a structural break in 2002.** This can not only help inform inflation projections, but in turn help the Reserve Bank of Malawi improve monetary policy decisions. In similar countries, this is often achieved through statistical methods. In this note, we try to apply similar methods to the data available for Malawi.

B. Framework

65. **Prices are typically modeled either as a mark-up over input prices (cost-push inflation), or as an endogenous outcome variable in the money market.** Large monetary shocks and periods of high inflation have characterized Malawi's recent history. For that reason, money, and consequently equilibrium in the money market, should play an important role in the determination of the aggregate price level. **We use the quantity theory of money as a starting point:**

$$m + v = p + y \quad \text{or} \quad \Delta m + \Delta v = \Delta p + \Delta y$$

66. **As written, prices and money should exhibit a one-for-one relationship.** Holding velocity (v) and output (y) constant, increases in the nominal money supply (Δm) should be reflected in equal changes in prices (Δp). In other words, real money balances are directly related to output when velocity is unchanged. This relationship appears to be true in Malawi until 2002 (Figure III.2). Since then, however, growth in the money supply has outstripped inflation pointing to the risk of inflation in the near term.

67. **This formulation also predicts a negative relationship between prices and output and explains two features of the Malawi economy.** First, holding money and velocity fixed, the equation predicts rising prices during periods of drought and falling prices during periods of good harvest in Malawi. Second, when the equation is rewritten as a function of real money ($m-p$), and holding velocity fixed, changes in output determine changes in real

¹⁶ Prepared by Chad Steinberg (AFR)

money demand. This also seems consistent with the strong seasonal pattern in Malawi when money demand jumps during the tobacco harvest. The lower half of Figure III.2 usefully plots the long-run trends in output and real money balances.

68. **Notably, the long-run formulation does not include relative prices, such as the exchange rate,¹⁷ food prices, and the international price of oil.** These are assumed to affect short-run dynamics and not the aggregate price level in the long-run.

C. Statistical Analysis¹⁸

69. **Data for output, price, and broad money are obtained from IFS for the period 1980Q1 through 2004Q2.** Output data are interpolated from an annual to quarterly time series¹⁹ and money and prices are not seasonally adjusted.²⁰

70. **The statistical analysis is done in three steps.** First, the time-series are tested for stationarity one variable at a time. This is a prerequisite for our second test of a cointegrating relationship between the three main variables, money, prices, and output. Third, we analyze the long-run coefficients on the adjustment path from the short-run to the long-run equilibrium.

Unit-root test

71. **If a series has a unit root it is nonstationary.** That is, a one time shock today will carry over to tomorrow, and thus, the series will not converge to a constant value. In this section, we test for the order of integration, which refers to the number of times a series must be differenced in order to achieve stationarity. Series which are integrated of order zero are stationary.

¹⁷ It is unclear if exchange rate depreciations would be positively associated with inflation in the long-run. While a monetary expansion at home would certainly lead to a combination of depreciation and inflation such that the real exchange rate is unchanged, a monetary expansion abroad (e.g., Zimbabwe), would lead to an appreciation of the currency and an ambiguous effect on domestic inflation.

¹⁸ The methodology of this section is based on de Brouwer and Ericsson (1998) and Hendry and Doornik (2001).

¹⁹ The data are interpolated under the assumption that a quarterly series follows a unit root process. The code for the filter was used in Maliszewski (2003) and obtained from the author.

²⁰ As noted in Ericsson, Hendry, and Tran (1994), seasonally adjusted data can obscure statistical tests commonly used in cointegration analysis.

72. **Tests were completed for the three variables of interest: money, prices, and output (Table III.1).** Augmented Dickey-Fuller statistics are listed on top, with one minus the estimated coefficient on the lagged variable below. The estimated coefficient should be approximately one if the series has a unit root and is nonstationary because as stated above, a shock today will persist tomorrow.²¹

Empirically, money, prices, and output are nonstationary²² and are integrated of order two or one. From the Dickey-Fuller statistic alone, money and output appear to be integrated of order one, whereas prices are integrated of order two. The estimated root for Δp , however, is 0.49, which is much less than unity. Thus, all three series are treated as integrated of order one and are suitable for estimation of a long-run relationship through cointegration analysis.

Cointegrating analysis

73. **Cointegration analysis allows us to test for the existence of a set of coefficients, the cointegrating vector, that define a linear combination of money, prices, and output that is stable over time.** If the three variables are not integrated, the difference between these variables could become very large, with no tendency for them to come back together. Economically, however, this seems unlikely given the evidence of a past money-price relationship. Therefore, large deviations between the three variables are not expected to continue, and the difference should have a tendency to return to its mean value.

74. **The Johansen procedure (1998) is used to help clarify the long-run relationship (Table III.3).²³ There is evidence of a single cointegrating vector between money, prices,**

²¹ Unit root tests are given for all the variables in logs, for their changes, and for the changes of the changes. This allows for testing on whether a series is integrated of order zero, one, two, or three.

²² Multivariate statistics for testing the stationarity of a given variable were also done as part of the succeeding cointegration analysis and are reported in the last row of table III.3. These test the restriction that the cointegrating vector includes zeros except for unity on the designated variable and no restriction on the trend term. Empirically, all these tests are consistent with the unit root tests in table III.1. That is, stationarity in p , m , and y are strongly rejected.

²³ Empirically, the lag order of the VAR is not known *a priori*, so sequential testing of the lag order was used to ensure a reasonable power of the Johansen procedure. Beginning with a twelve-order VAR in p , m , and y that includes an intercept, a trend term, and seasonal dummies, Table III.2 shows that it is only statistically acceptable to simplify to an eight-order VAR. This may result from the persistence of inflation levels through expectations.

and output,²⁴ which means that the three variables converge to a stable equilibrium. However, at any time period, there can be temporary deviations as there are economic forces that force money, prices, and output back toward the equilibrium relationship. **Furthermore, there is little evidence to suggest that there was a structural break after 2000.**²⁵ The estimated coefficients in the long-run relationship are as follows:

$$p = v + 0.79m + 2.15y - 0.01t$$

75. **All variables are significant at the 5 percent threshold. The coefficient on money is the correct sign and is close to unity,**²⁶ **as predicted by the money demand equation.** This suggests that changes in money are associated with close to equal changes in prices and there is a long-run stable relationship between prices and money. In consequence, the recent two year increase in money should soon be accompanied by an equal change in prices, or in other words, a pickup in inflation. The speed of this change will depend on the adjustment mechanism discussed in the subsequent section.²⁷

Adjustment to equilibrium

76. **Cointegration analysis also measures the mechanism and speed in which disequilibrium in the long-run relationship is corrected.** In table III.4, the coefficients in the first column of α measure the feedback effects of disequilibrium. A larger feedback coefficient indicates a faster adjustment to equilibrium, while a feedback coefficient close to zero could indicate no adjustment through changes in that specific variable. **For example, table III.3 reports that about 40 percent of the temporary disequilibrium between money, prices, and output is corrected through changes in broad money after one quarter.**

²⁴ The maximal eigenvalue and trace eigenvalue statistics reject the null of no cointegrating in favor of at least one cointegrating relationship. Likewise, there is little evidence for more than one vector. Parallel statistics with a degree of freedom adjustment, however, fail to reject the null of no cointegrating vector, but with p-values in the teens.

²⁵ The price equation passes several tests for parameter constancy (Figure III.3). One-step ahead residuals are within a two-standard deviation band, and all three Chow tests do not reject stability of the parameters at the one percent level after 2000. However, there is some evidence of a break in 1996.

²⁶ A test of the restriction that the coefficient is one, however, is rejected.

²⁷ The coefficient on output, however, is oddly the wrong sign. The coefficient may be upwardly biased due to the exclusion of a proxy for velocity. Some robustness checks were completed, and it appears the inclusion of inflation does decrease this bias. Alternatively, output may just be poorly measured in Malawi. Different measures of output were also tested for robustness with varying results.

77. **Tests on the feedback coefficients are referred to as weak exogeneity tests.** Specifically, these are tests of whether or not the corresponding value of α is zero. If the value is zero, disequilibrium in the cointegrating vector does not feedback onto the associated variable and the variable is considered weakly exogenous. Economically, this means adjustment does not take place through changes in the associated variable.

78. **Oddly, tests reveal that prices are weakly exogenous.** This result is robust to various specifications²⁸ and indicates that disequilibrium in the money market does not adjust through changes in prices. However, this result is difficult to understand in terms of economics and may point to deficiencies in the data used for this analysis.²⁹

79. **Finally, weak exogeneity of money is strongly rejected** suggesting that disequilibrium in the cointegrating vector is adjusted through changes in money, and not changes in prices.

D. Conclusions

80. **These results suggest that a long-run stable relationship exists between money, prices, and output without a structural break in 2002.** This indicates that either money will need to be reduced or prices will have to adjust to bring the relationship back to equilibrium.

81. **Disappointingly, the statistical analysis implies that adjustment to equilibrium happens through changes in money and not necessarily changes in prices.** This is hard to reconcile with our understanding of the economy in Malawi, and suggests that there may be some deficiency in the data used to test the relationship.

²⁸ These results are robust to various specifications (Table III.4). Prices remain weakly exogenous with the inclusion of real interest rates and the exchange rate. Estimation of a model with inflation and real money find inflation is weakly exogenous, while disequilibrium is adjusted through changes in real money balances. These results are also robust to different measures of output. Models excluding output, including a measure of industrial output, including an output measure interpolated without a filter, and including a measure of output adjusted for seasonal factors are tested. Weak exogeneity is accepted for prices in all cases.

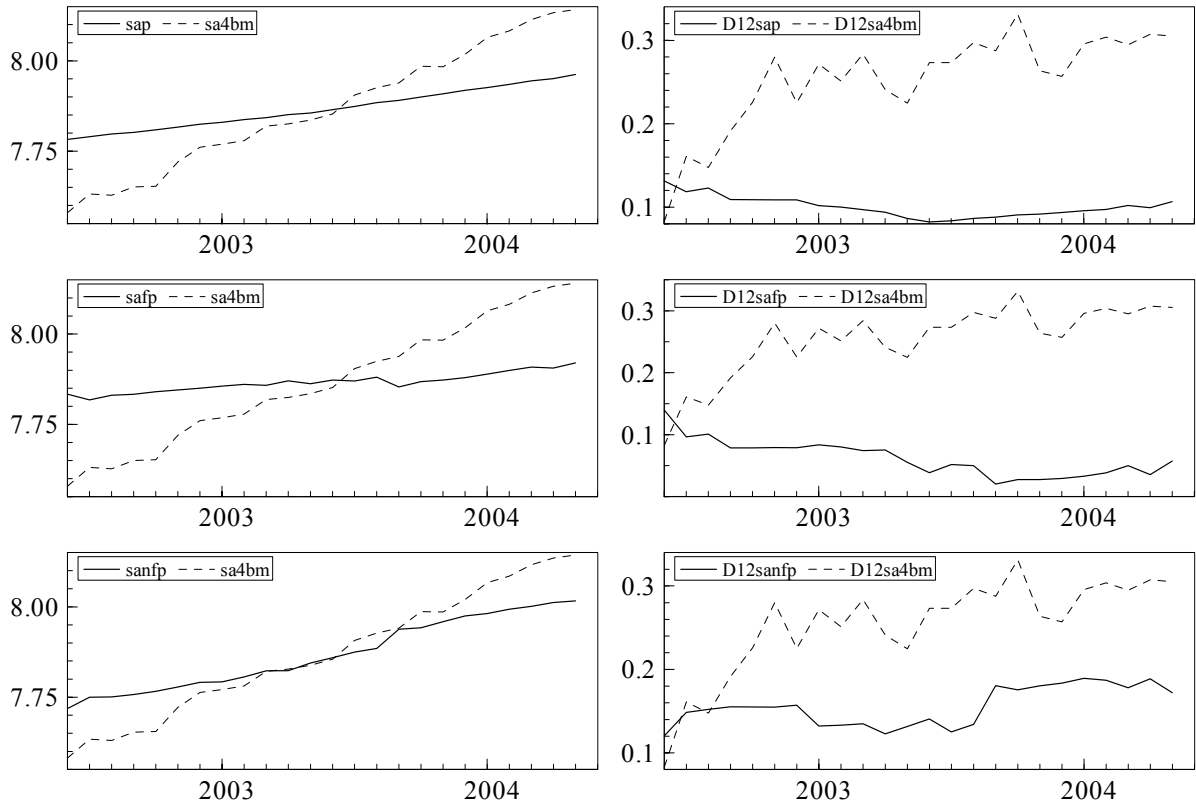
²⁹ Douoguih and Kostial (2002) were also unable to find an economically meaningful result when modeling money demand in Malawi.

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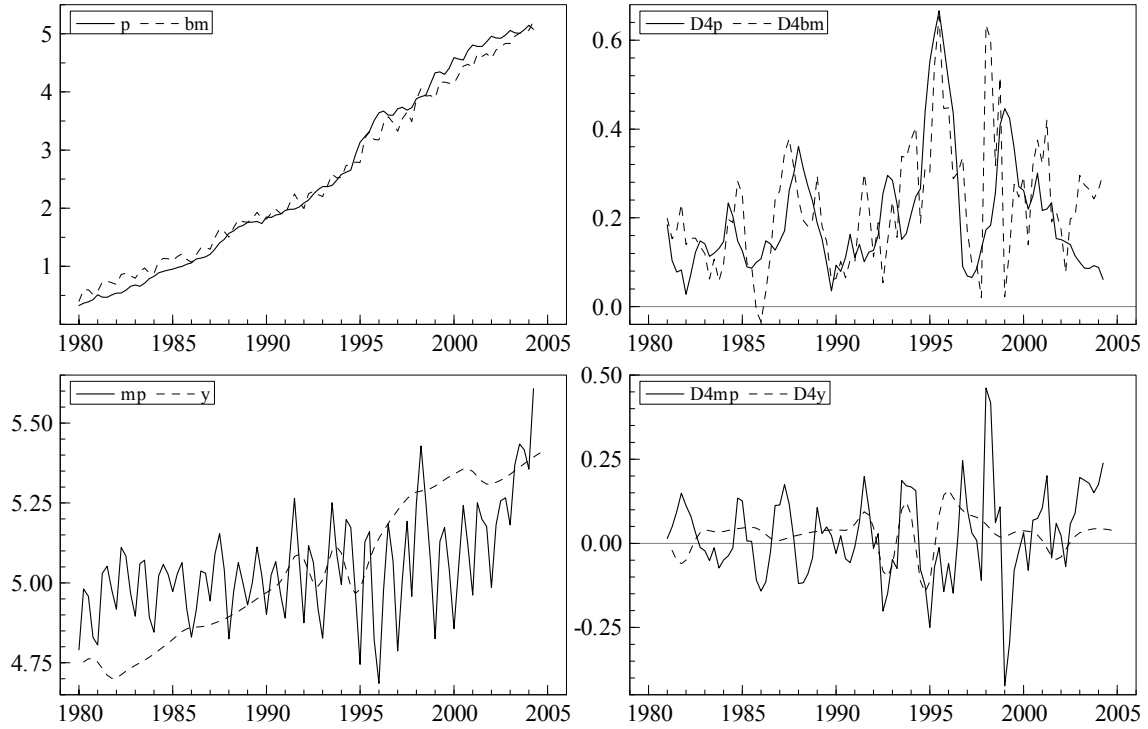
Figures and Tables

Figure III.1. Recent Patterns in Broad Money and Prices 1/
(Variables are the log of seasonally adjusted values)



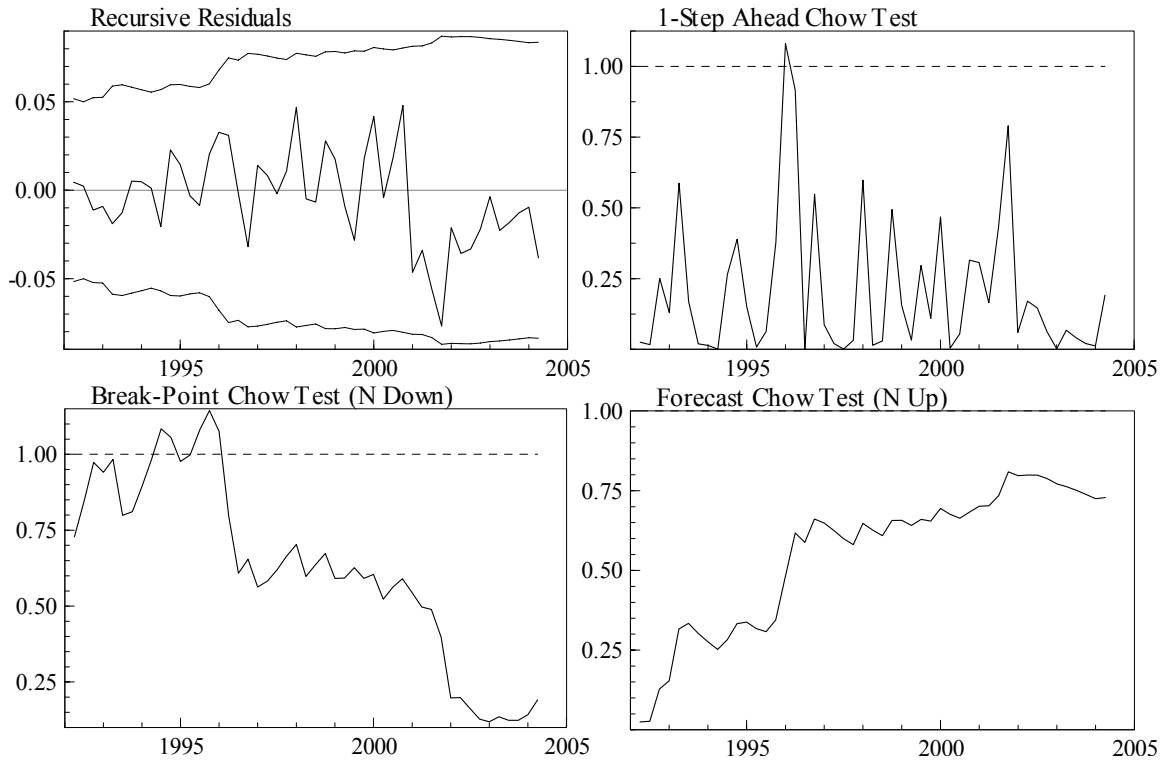
1/ sap is the log of seasonally adjusted prices; safp is the log of seasonally adjusted food prices; sanfp is the log of seasonally adjusted nonfood prices; sa4bm is the log of seasonally adjusted broad money from the four-bank survey; D12 is the twelve month difference.

Figure III.2. Basic Patterns of Series 1/



1/ p is the log of the price index; bm is the log of broad money; mp is the log difference between bm and p; y is the log of the real output index; and D4 is the four quarter difference.

Figure III.3. Tests for Parameter Constancy 1/



1/ The y-axes are the p-values in the graphs for the various Chow tests with the dotted line representing significance at 1 percent.

Table III.1. ADF Statistics for Testing of a Unit Root 1/

Null order	p		m		y	
	lag 2/	value 3/	lag 2/	value 3/	lag 2/	value 3/
I(1)	ADF(4)	-2.87	ADF(2)	-1.58	ADF(2)	-3.20
	81(2)-04(2)	0.94	80(4)-04(2)	0.94	83-03	0.01
I(2)	ADF(4)	-3.40	ADF(2)	-9.32**	ADF(0)	-6.89**
	81(3)-04(2)	0.49	80(4)-04(2)	-0.49	82-03	-0.38
I(3)	ADF(3)	-5.61**	ADF(9)	-6.08**	ADF(0)	-10.76**
	81(3)-04(2)	-0.96	83(1)-04(2)	-8.36	83-03	-0.72

1/ Equations are estimated with a constant, seasonals (for quarterly data only), and a linear trend over the sample period.

2/ The top value is the lag length of the augmented dickey fuller statistic, and the bottom value is the sample period. The number of lags was based on F-tests for the joint significant of lags and the Akaike information criterion

3/ The top value is the augmented dickey fuller statistic, the bottom value is one minus the estimated coefficient on the lagged variable. Asterisks * and ** denote rejection at the 5% and 1% critical values that are obtained from the PC Give econometric package.

Table III.2. Statistics for the Sequential Reduction to an Eighth-Order VAR

System	Null Hypothesis 1/			Maintained Hypothesis				
	k	L	SC	VAR(11)	VAR(10)	VAR(9)	VAR(8)	VAR(7)
VAR(11)	114	668.8	-9.78					
↓								
VAR(10)	105	663.3	-10.12	0.66				
↓				[0.75]				
				(9,109)				
↓								
VAR(9)	96	656.4	-10.43	0.77	0.9			
↓				[0.73]	[0.53]			
				(18,127)	(9,116)			
↓								
VAR(8)	87	647.5	-10.69	0.91	1.06	1.24		
↓				[0.59]	[0.40]	[0.28]		
				(27,132)	(18,136)	(9,124)		
↓								
VAR(7)	78	629.9	-10.75	1.35	1.61	1.98	2.71	
↓				[0.12]	[0.04]*	[0.01]*	[0.01]**	
				(36,133)	(27,140)	(18,144)	(9,131)	
↓								
VAR(4)	51	587.4	-11.16	1.93	2.19	2.46	2.74	1.88
				[0.00]**	[0.00]**	[0.00]**	[0.00]**	[0.02]*
				(63,135)	(54,143)	(45,152)	(36,160)	(18,161)

1/ The first four columns report the VAR with its order, and for each system, the number of unrestricted parameters, k, the log-likelihood, L, and the Schwartz criterion SC.

2/ The three entries within each block are the F statistic for testing the null hypothesis against the maintained hypothesis, the tail probability associated with that value of the F statistic [in brackets], and the degrees of freedom for the statistic (in parentheses). Asterisks * and ** denote rejection at the 5% and 1% critical values.

Table III.3. Cointegration Analysis

Statistic	Null hypothesis for summary test statistics 1/			
	r=0	r≤1	r≤2	
Eigenvalue	0.277	0.189	0.055	
λ trace	52.62**	23.75	5.08	
p value	[0.003]	[0.089]	[0.593]	
λ max	28.88*	18.67	5.08	
p value	[0.016]	[0.061]	[0.594]	
λ trace (T-nK)	38.43	17.34	3.71	
p value	[0.131]	[0.398]	[0.780]	
λ max (T-nk)	21.09	13.64	3.71	
p value	[0.193]	[0.290]	[0.782]	
Standardized eigenvectors β'				
Variable	p	m	y	Trend
p	1.000	-0.794	-2.152	0.009
m	-0.787	1.000	-2.354	0.001
y	-1.210	1.612	1.000	-0.033
Standardized adjustment coefficients α				
p	-0.018	0.016	-0.070	
m	0.389	-0.221	-0.058	
y	0.018	0.012	0.000	
Weak exogeneity test statistic 2/				
Variable	p	m	y	
$\chi^2(1)$	0.084	4.603	4.301	
p value	[0.772]	[0.032]*	[0.038]*	
Statistic for testing the significance of a given variable				
Variable	p	m	y	Trend
$\chi^2(1)$	5.882	3.861	6.675	4.254
p value	[0.015]*	[0.049]*	[0.010]**	[0.039]*
Multivariate statistics for testing stationarity				
Variable	p	m	y	
$\chi^2(2)$	12.717	12.922	11.838	
p value	[0.002]**	[0.002]**	[0.003]**	

1/ The VAR includes eight lags, an intercept, seasonal dummies, and a trend. The estimation period is 1982Q2 to 2004Q2. The statistics λ trace and λ max are the Johansen's maximal and trace eigenvalue statistic for testing cointegration. The null hypothesis is in terms of the cointegrating rank r. The lower two statistics are the same with degree-of-freedom adjustments.

2/ The statistics for testing weak exogeneity, significance, and stationarity are evaluated under the assumption that r=1. They are asymptotically distributed $\chi^2(1)$, $\chi^2(1)$, and $\chi^2(2)$, respectively, if r is actually unity and if the associated null hypothesis is valid.

Table III.4. Robustness Check on Weak Exogeneity Result 1/

Tests on different specifications				
1. Including real interest rate	p	m	y	RI
$\chi^2(1)$	0.096	4.080	8.636	0.406
p value	[0.7566]	[0.0434]*	[0.0033]**	[0.5242]
2. Including exchange rate	p	m	y	er
$\chi^2(1)$	1.658	1.136	8.278	0.178
p value	[0.1979]	[0.2864]	[0.0040]**	[0.6727]
3. Including inflation	m-p	pi	y	
$\chi^2(1)$	18.263	0.369	0.230	
p value	[0.0000]**	[0.5434]	[0.6315]	
Tests on different measures of output				
1. Excluding output measure	p	m		
$\chi^2(1)$	0.33149	8.8891		
p value	[0.5648]	[0.0029]**		
2. Including measure of industrial output	p	m	i	
$\chi^2(1)$	0.626	10.071	2.724	
p value	[0.4287]	[0.0015]**	[0.0989]	
2. Including unfiltered output variable	p	m	y (simple)	
$\chi^2(1)$	0.133	9.325	1.991	
p value	[0.7156]	[0.0023]**	[0.1583]	
3. Including output variable adjusted for seasonal patterns	p	m	y (adjusted)	
$\chi^2(1)$	0.430	0.007	8.827	
p value	[0.5118]	[0.9328]	[0.0030]**	

1/ The VAR includes eight lags, an intercept, seasonal dummies, and a trend. The estimation period is 1982Q2 to 2004Q2. The statistics for testing weak exogeneity are evaluated under the assumption that $r=1$. They are asymptotically distributed $\chi^2(1)$, $\chi^2(1)$, and $\chi^2(2)$, respectively, if r is actually unity and if the associated null hypothesis is valid.

IV. VOLATILITY AND PREDICTABILITY OF EXTERNAL AID INFLOWS³⁰

A. Introduction

82. Malawi is an economy highly dependent on foreign aid. This dependency is particularly evident in the case of the central government operations, where the magnitude of foreign aid inflows is on average 75 percent of central government revenue.³¹ In view of the high dependency, the authorities are concerned about the volatility and unpredictability of foreign aid inflows, which they claim have increased in recent years, affecting Malawi's macroeconomic stability. In this context, the objectives of this chapter are to evaluate the volatility and predictability of foreign aid inflows and the need for the government to modify its policies, if necessary.

83. This chapter is organized as follows, section B discusses the sources of data used; section C evaluates the volatility of total foreign aid and its components; section D assesses the predictability of total foreign aid; and section E identifies the lessons to be learned from past experience.

B. Sources of Data

84. This chapter uses information from two sources, the IMF and the Organization for Economic Co-operation and Development (OECD). The IMF information refers to Malawi's central government revenue, GDP, and foreign assistance. The later includes inflows of foreign aid recorded in the central government operations during fiscal years 1992/93-2003/04. Aid inflows refer to grants and medium- and long-term loans received from bilateral and multilateral sources and recorded in the budget. Not all aid inflows are included in the budget. In particular, when a domestic counter part is not necessary, government entities often do not report foreign aid inflows. In accordance with IMF information, during 1992/93-2003/04, Malawi's aid dependency (total foreign aid received to GDP ratio) averaged 13.3 percent of GDP during the above-indicated period. The aid dependency reached its lowest level in 1997/98 (7.7 percent of GDP, 42 percent lower than the average) and its highest in 1994/95 (21.9 percent, 65 percent higher than the average).

85. Given the narrow coverage of the foreign aid data included in the central government operations and for comparability purposes, this chapter also uses annual data from OECD for Malawi and Sub-Saharan Africa (SSA) for 1970-2002. OECD information used refers to total Official Development Assistance (ODA), which includes grants and loans undertaken

³⁰ Prepared by Cecilia Mongrut (PDR).

³¹ While central government revenue represented on average about 18 percent of GDP per year during 1992/93-2003/04, foreign aid amounted to on average about 13 percent of GDP per year during the same period.

by Malawi's official sector.³² This database includes data on commitments and actual inflows of aid to Malawi and SSA.

C. Volatility of Foreign Aid Flows

86. In assessing the volatility of foreign aid inflows, Paul Collier³³ follows an approach that consists of measuring volatility by scaling it for the mean level (coefficient of variation)³⁴. Collier found that foreign aid is more reliable than tax revenues. Based on a sample of 36 African countries (1970-95) and using per capita aid and revenue, he estimated that the coefficient of variation of aid (0.35) was slightly lower than the same for revenue (0.37). In addition, he concluded that aid flows have acted as a buffer to revenue shocks in these countries, increasing when revenue was low (negative normalized covariance of aid and revenue³⁵ of 0.0007). In the case of Malawi, however, Collier found the opposite, the coefficient of variation of aid was higher (0.39) than the one of revenue (0.17), and the normalized covariance was positive (0.021).

87. We estimated measures of volatility using a different scaling of variables. Instead of using per capita aid flows and revenue, we used percentages of GDP, which are more relevant from a domestic policy point of view, because the Malawian authorities do their financial programming in domestic currency and in percent of GDP. As shown in table IV.1, based on information from 1992/93 to 2003/04 and applying the standard statistics suggested by Collier, we found that the coefficient of variation of total aid inflows (0.30) was higher than the one of revenue (0.13). In line with main findings of Bulíř and Hamann,³⁶ Malawi's total aid flows have been less volatile than any of its components but more volatile than central government revenue. As indicated by the coefficient of variation, different components of total foreign aid flows have different volatility. As shown in table IV.2, project inflows are less volatile (0.38) than any other aid inflow component. As expected, food aid shows a high volatility (0.73), since it is only received in cases of food crises, but the other aid inflows (which includes HIPC debt relief from 2001 onward) are even more

³² The main objective of ODA is to promote economic development and welfare at concessional terms. In the case of a loan, it should have a grant element of at least 25 percent.

³³ Collier, Paul, 1999, Aid 'Dependency': a Critique, *Journal of African Economies*, Vol. 8 (December), pp. 528-45.

³⁴ A measure of volatility that scales for the mean level of aid inflows (standard deviation over mean).

³⁵ Normalized covariance of aid and revenue is defined as covariance of the two variables over product of the means.

³⁶ Bulíř, Ales and Hamann, Javier, 2001, How Volatile and Predictable Are Aid Flows, and What Are the Policy Implications?, IMF Working Paper.

volatile (2.03). We also found that the normalized covariance of foreign aid and revenue was 0.007. These results indicate that the resources of a government with a large component of revenue would be more stable than the resources of another government with a large component of foreign aid. In addition, the normalized variance of aid and revenue in the case of Malawi, indicates that aid does not smooth out revenue shocks; on the contrary, it is procyclical (i.e., foreign aid tends to increase when revenue is increasing).

Table IV.1. Coefficient of Variation

	Central Government Revenue	ODA Total Actuals	ODA Grants Actuals	ODA Loans Actuals	ODA Total Commitments
1970-2002					
Mean	0.18	0.19	0.12	0.07	0.21
Standard deviation	0.02	0.09	0.07	0.03	0.10
Coefficient of variation	0.10	0.49	0.61	0.38	0.46
1993-2002					
Mean	0.17	0.27	0.18	0.09	0.26
Standard deviation	0.01	0.07	0.05	0.03	0.09
Coefficient of variation	0.08	0.26	0.29	0.32	0.33

Source: OECD.

88. OECD data suggest that contrary to the authorities' claims, the volatility of total foreign aid may have decreased in the last few years, while the volatility of revenue remained almost the same, as shown in table IV.2. The coefficient of variation for actual total ODA during 1970-2002 was 0.49 and during the last 10 years of the sample it was 0.26. The change in the coefficient of variation is even more important in the case of ODA grants, it goes down from 0.61 in 1970-2002 to 0.29 in 1993-2002. The same pattern has been observed in ODA for SSA. These findings suggest that ODA has become less volatile, which could in part reflect the fact that for some donors procedures for budget approval and disbursements have become less cumbersome.

Table IV.2. Volatility of Foreign Aid Inflows Included in the Central Government Operations, 1992/93-2003/04
(In percent of GDP)

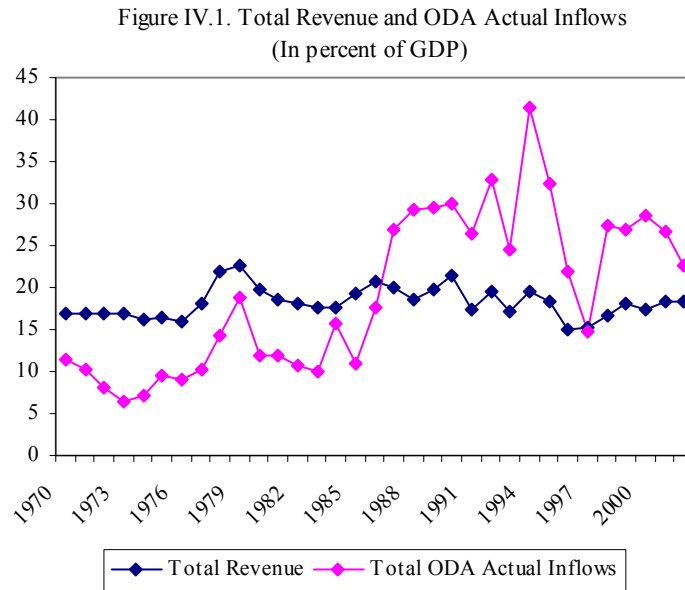
	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	Coefficient Prel. of Variation
Program	3.0	9.5	9.9	5.7	8.3	4.1	9.2	5.6	9.4	1.9	0.8	2.5	0.57
Project	4.7	1.9	5.1	5.0	3.1	3.6	6.5	8.4	8.3	5.8	6.2	8.5	0.38
Food Security	2.2	0.3	6.9	1.1	0.0	0.0	1.8	0.0	0.0	0.4	0.1	0.0	0.73
Other 1/	0	0	0	1.2	0	0	0	0	0	1.92	3	5.5	2.03
Total Aid Inflows	9.9	11.7	21.9	13.0	11.4	7.7	17.5	14.1	17.8	10.1	10.1	16.5	0.30
Memorandum Item :													
Central Government Revenue	19.8	17.3	16.9	17.3	15.5	14.8	18.1	17.4	18.3	17.2	20.8	23.5	0.13
Total Aid Inflows/ Central Government Revenue	49.8	67.8	129.4	75.4	73.7	52.2	96.8	80.8	96.9	58.5	48.6	70.2	...

Source: Malawian authorities.

1/ Includes HIPC debt relief from 2001 onward.

89. We have also analyzed the implications of trends for measuring the relative volatility of aid flows and revenue. Following Bulř and Hamann, we calculated the relative volatility

defined as $\Phi = \theta_A/\theta_R$ ³⁷. If Φ is greater than one, it implies that aid is more volatile than revenue. Figure IV.1, suggests that revenue in percent of GDP is less volatile than aid flows in percent of GDP. This was confirmed by the estimate of Φ . Given the low relative volatility of revenue, Φ was estimated to be 12.8, significantly higher than one. In addition, the correlation coefficient between detrended aid and revenue is positive (0.5), indicating that aid flows are procyclical. This is in line with the main results of Bulíř and Hamann for countries with high aid dependency, i.e. aid is more volatile than revenue and it is procyclical.

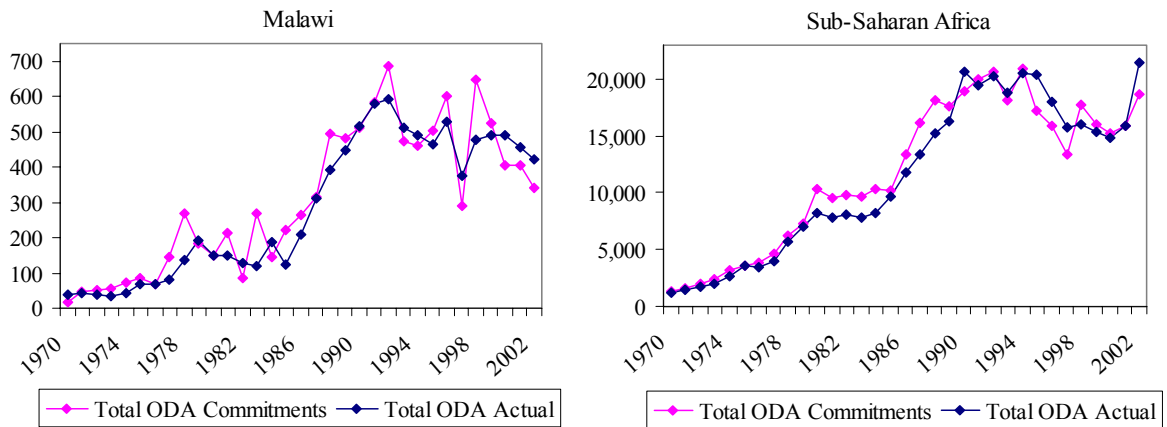


D. Predictability of foreign aid flows

90. Based on information on actual ODA inflows and ODA commitments (in current US dollars) from OECD, we assessed the contribution of commitments (C) to the prediction of actual ODA inflows (D) for Malawi and SSA. Figures IV.2 shows that ODA commitments have been systematically above actual ODA inflows in the case of Malawi (23 out of the 33 observations) and SSA (27 out of 33 observations), respectively.

³⁷ Where θ_A and θ_R are the trend corrected variances for aid flows and revenue, respectively.

Figure IV.2. Actual Inflows and Commitments
(In millions of U.S. dollars)



91. To determine the significance of commitments in predicting total ODA actual inflows we estimated the following regression for Malawi and for SSA in first differences:

$$D_t = \beta_0 + \beta_1 D_{t-1} + \gamma C_t + \delta T + \varepsilon_t$$

Where T is a time trend. We would expect β_1 and γ to be positive and statistically significant³⁸. It is expected that if commitments contain high marginal information value, γ should be close to one.

92. The estimated γ s are statistically significant for Malawi and SSA but lower than one (t Stat = 3.855 and 4.263, respectively). The magnitude of γ in the case of Malawi (0.29) is about half the one in the case of SSA (0.57). This indicates that the information content of commitments in the case of Malawi is lower than in the case of SSA. The marginal predictive power of commitments is low in the case of total aid. We have also estimated γ s for grants and loans inflows in the case of Malawi. While in the case of grants γ is statistically significant and higher than the γ obtained for total aid in SSA (0.61), in the case of loans γ is low (0.06) and not statistically significant. This suggests that the marginal predictive power of commitments is high in the case of grants but insignificant in the case of loans. In this connection, projections of aid inflows cannot be directly based on aid commitments but on discounted values.

93. In the case of Malawi, as well as in SSA, the estimated β_1 is not statistically significant, indicating that past experience is of little relevance in predicting future aid. This suggests that the authorities deem past aid flows unreliable predictors of future flows and prefer to base their decisions on more current information, such as commitments.

³⁸ Following Bulíř and Hamann, to address nonstationarity issues we estimated the parameters by running this equation in first differences, using data on current US dollars.

E. Lessons

94. The analysis carried out in this chapter suggests that foreign aid is more volatile than revenue in the case of Malawi. Therefore, for the authorities to reduce the volatility of central government resources, they should make the necessary efforts to increase revenue and reduce central government's dependency on foreign aid. Moreover, because the normalized covariance is positive, the government should not expect to offset revenue shocks with additional foreign aid.

95. Regarding the predictability of foreign aid, we conclude that ODA commitments were significantly higher than actual ODA inflows in Malawi as well as in SSA during most of the period under evaluation. Moreover, we found that the contribution of commitments to predict ODA inflows is smaller in the case of Malawi and past disbursement experience is of limited relevance to predict future aid inflows. Therefore, while the authorities should base their projections of foreign aid on commitments, they should heavily discount foreign aid commitments to project foreign aid.

96. The high volatility and unpredictability of aid can increase the probability that Malawi's government would need to recourse to borrowing from nonconcessional sources (domestic or external), printing money, or to adjust fiscal expenditure. Therefore, the authorities should coordinate their foreign aid projections with donors and creditors and improve their compliance with conditionality attached to foreign aid. A smoother path of foreign aid will help the authorities to avoid expensive domestic financing.

Table 1. Malawi: GDP by Economic Activity at Constant 1994 Factor Cost, 1999-2003 1/

	1999	2000	2001	2002	2003
(In millions of Malawi kwacha)					
Agriculture	4,944	5,206	4,894	5,026	5,395
Smallholders	3,992	4,055	3,862	3,846	4,358
Estates	951	1,151	1,033	1,180	1,037
Mining and quarrying	170	188	202	124	153
Manufacturing	1,749	1,696	1,583	1,475	1,491
Electricity and water	171	189	176	186	188
Construction	292	286	273	311	324
Distribution	2,760	2,752	2,782	2,826	2,891
Transport and communication	573	549	546	619	632
Financial and professional services	1,031	1,052	1,020	1,085	1,151
Ownership of dwellings	180	185	190	195	200
Private community services	264	271	279	287	295
Government services	1,309	1,180	1,189	1,183	1,199
Unallocable financial charges	-378	-387	-386	-437	-463
GDP at constant 1994 factor cost	13,065	13,166	12,748	12,880	13,456
(Annual percentage change, unless otherwise indicated)					
Agriculture	10.1	5.3	-6.0	2.7	7.3
Smallholders	13.4	1.6	-4.8	-0.4	13.3
Estates	-1.9	21.0	-10.3	14.2	-12.1
Mining and quarrying	3.4	10.8	7.5	-38.7	23.5
Manufacturing	1.8	-3.0	-6.6	-6.9	1.1
Electricity and water	-0.4	10.2	-7.0	5.8	0.9
Construction	15.5	-2.2	-4.7	14.1	4.0
Distribution	-1.8	-0.3	1.1	1.6	2.3
Transport and communication	4.8	-4.2	-0.6	13.4	2.2
Financial and professional services	-0.3	2.0	-3.0	6.4	6.0
Ownership of dwellings	2.1	2.6	2.8	2.8	2.8
Private community services	0.7	2.7	2.9	2.9	2.9
Government services	-1.8	-9.9	0.8	-0.5	1.4
GDP at constant 1994 factor cost	3.5	0.8	-3.2	1.0	4.5
Memorandum items:					
GDP at current factor cost (in millions of Malawi kwacha)	76,990	102,383	121,828	141,543	164,314
GDP at current factor cost (percentage change)	46.3	33.0	19.0	16.2	16.1
GDP deflator at factor cost (1994=100)	589	778	956	1,099	1,221
GDP deflator at factor cost (percentage change)	41.3	32.0	22.9	15.0	11.1

Sources: Malawian authorities; staff estimates.

1/ Figures for 2003 are provisional.

Table 2. Malawi: GDP by Expenditure at Constant 1994 Market Prices, 1999-2003 1/

	1999	2000	2001	2002	2003
(In millions of Malawi kwacha)					
GDP at constant 1994 market prices	14,371	14,598	13,999	14,265	14,893
Net exports or imports(-) of goods and services	-3,185	-2,287	-2,195	-3,261	-1,979
Exports of goods and services	3,862	3,601	4,002	4,064	3,607
Exports and reexports of goods	3,430.5	3,205.0	3,510.7	3,644.4	3,252.6
Exports of nonfactor services	431.1	395.8	491.1	419.4	354.4
Imports of good and services	-7,047	-5,888	-6,197	-7,325	-5,586
Imports of goods, f.o.b.	-5,247	-4,289	-4,579	-5,549	-4,183
Imports of nonfactor services	-1,800	-1,599	-1,618	-1,775	-1,403
Gross domestic expenditure	17,556.4	16,884.6	16,194.4	17,526.4	16,871.9
Consumption	15,252	14,977	14,300	15,951	15,314
Government	1,989	2,051	2,214	2,161	2,508
Compensation of employees	904	904	904	904	904
Goods and services	939	939	939	939	939
Private	13,263	12,926	12,087	13,790	12,806
Fixed capital formation	1,994	1,715	1,726	1,418	1,412
Government and statutory bodies	1,621	1,551	1,578	1,276	1,326
Private	373	164	148	142	86
Stock building	310	192	168	158	145
(Annual percentage change, unless otherwise indicated)					
GDP at constant 1994 market prices	3.0	1.6	-4.1	1.9	4.4
Exports of goods and services	-16.6	-6.8	11.1	1.5	-11.2
Exports and reexports of goods	-20.6	-6.6	9.5	3.8	-10.7
Exports of nonfactor services	41.1	-8.2	24.1	-14.6	-15.5
Imports of good and services	14.3	-16.4	5.3	18.2	-23.7
Imports of goods, f.o.b.	15.3	-18.3	6.8	21.2	-24.6
Imports of nonfactor services	11.5	-11.2	1.2	9.7	-21.0
Gross domestic expenditure	13.4	-3.8	-4.1	8.2	-3.7
Consumption	13.7	-1.8	-4.5	11.5	-4.0
Government	-4.8	3.1	7.9	-2.4	16.1
Compensation of employees	0.0	0.0	-1.2	1.4	-2.5
Goods and services	0.0	0.0	-1.3	5.8	-2.0
Private	17.1	-2.5	-6.5	14.1	-7.1
Fixed capital formation	16.9	-14.0	0.6	-17.9	-0.4
Government and statutory bodies	18.9	-4.3	1.7	-19.1	4.0
Private	8.9	-56.0	-9.6	-4.4	-39.3
Stock building	-13.9	-38.0	-12.9	-6.0	-7.9
Memorandum items:					
GDP at current market prices (in millions of Malawi kwacha)	78,297	103,815	123,080	142,928	165,751
GDP at current market prices (percentage change)	45.1	32.6	18.6	16.1	16.0
GDP deflator at market prices (1994=100)	545	711	887	1,003	1,116
GDP deflator at market prices (percentage change)	40.8	30.5	24.8	13.1	11.2

Sources: Malawian authorities; staff estimates.

1/ Figures for 2003 are provisional.

Table 3. Malawi: GDP by Expenditure at Current Market Prices, 1999-2003 1/

	1999	2000	2001	2002	2003
GDP at current market prices	78,297	103,815	123,080	142,928	165,751
Net exports or imports(-) of goods and services	-11,957	-12,552	-13,794	-26,355	-26,833
Exports of goods and services	21,941	26,580	34,753	36,171	42,753
Exports and reexports of goods	19,712	23,928	30,797	32,289	39,158
Exports of nonfactor services	2,229	2,653	3,956	3,883	3,596
Imports of good and services	-33,898	-39,133	-48,547	-62,527	-69,587
Imports of goods, f.o.b.	-25,240	-28,508	-35,869	-47,371	-52,111
Imports of nonfactor services	-8,657	-10,625	-12,678	-15,155	-17,475
Gross domestic expenditure	90,254	116,367	136,874	169,283	192,584
Consumption	78,784	102,285	119,774	153,756	173,968
Government	10,528	15,134	19,591	21,858	28,025
Compensation of employees	4,678.6	4,678.6	4,678.6	4,678.6	4,678.6
Goods and services	4,920.2	4,920.2	4,920.2	4,920.2	4,920.2
Private	68,256	87,151	100,182	131,898	145,942
Fixed capital formation	9,871	12,792	15,741	14,110	17,058
Government and statutory bodies	8,026	10,401	12,799	11,473	16,019
Private	1,845	2,391	2,942	2,637	1,039
Stock building	1,600	1,290	1,360	1,417	1,559
GDP at market prices	100.0	100.0	100.0	100.0	100.0
Exports of goods and services	28.0	25.6	28.2	25.3	25.8
Exports and reexports of goods	25.2	23.0	25.0	22.6	22.6
Exports of nonfactor services	2.8	2.6	3.2	2.7	2.2
Imports of good and services	-43.3	-37.7	-39.4	-43.7	-42.0
Imports of goods, f.o.b.	-32.2	-27.5	-29.1	-33.1	-31.4
Imports of nonfactor services	-11.1	-10.2	-10.3	-10.6	-10.5
Gross domestic expenditure	115.3	112.1	111.2	118.4	116.2
Consumption	100.6	98.5	97.3	107.6	105.0
Government	13.4	14.6	15.9	15.3	16.9
Compensation of employees	6.0	...	3.8	3.3	2.8
Goods and services	6.3	...	4.0	3.4	3.0
Private	87.2	83.9	81.4	92.3	88.0
Fixed capital formation	12.6	12.3	12.8	9.9	10.3
Government and statutory bodies	10.3	10.0	10.4	8.0	9.7
Private	2.4	2.3	2.4	1.8	0.6
Stock building	2.0	1.2	1.1	1.0	0.9
Memorandum items:					
Indirect taxes (in millions of Malawi kwacha)	1,307	1,432	1,252	1,385	1,437
Indirect taxes	1.7	1.4	1.0	1.0	0.9

Sources: Malawian authorities; staff estimates.

1/ Figures for 2003 are provisional.

Table 4. Malawi: Agricultural Production by Principal Crops, 1999-2003

	1999	2000	2001	2002	2003
(In thousands of metric tons)					
Total production					
Tobacco (auction sales)	133	160	125	138	121
Flue cured	14	11	8	11	14
Fire cured	8	...	1	2	5
Northern division	7	...	1	1	4
Southern division	1	...	0	0	1
Burley	110	142	115	125	103
Other	1	...	0	0	0
Tea	39	...	37	39	42
Sugar	200	...	215	261	260
Smallholder production					
Maize	2,246	2,290	1,899	1,557	1,983
Rice	93	72	93	92	88
Groundnuts	125	117	155	158	190
Tobacco	85	99	83	89	94
Cotton	51	35	38	40	40
Sorghum	41	37	37	39	45
Millet	20	20	20	21	25
Pulses	234	263	304	283	324
Cassava	895	2,757	3,362	1,540	1,735
Sweet potatoes	1,680	1,877	2,587	1,061	1,535
(Annual percentage change)					
Total production					
Tobacco (auction sales)	-1.8	0.2	-22.0	10.8	-12.3
Flue cured	0.7	-0.2	-22.4	33.7	23.5
Fire cured	18.8	...	-84.9	57.0	181.3
Northern division	15.9	...	-85.5	49.0	178.5
Southern division	50.0	...	-78.6	121.3	196.0
Burley	-3.0	0.3	-18.9	8.7	-18.0
Other	-44.4	...	...	...	...
Tea	-4.7	...	-12.7	6.6	6.4
Sugar	-4.6	...	-5.1	20.9	-0.2
Smallholder production					
Maize	46.4	0.0	-14.1	-18.0	27.4
Rice	34.9	-0.2	38.6	-1.0	-4.2
Groundnuts	28.2	-0.1	33.3	1.7	20.4
Tobacco	-10.1	0.2	-16.4	8.3	5.5
Cotton	39.4	-0.3	7.7	6.1	1.3
Sorghum	-0.2	-0.1	0.3	6.2	15.8
Millet	3.1	0.0	4.6	2.4	17.2
Pulses	11.9	0.1	22.4	-6.8	14.3
Cassava	7.9	2.1	21.9	-54.2	12.7
Sweet potatoes	17.3	0.1	58.3	-59.0	44.7

Sources: National Statistics Office, *Monthly Statistics Bulletin*; and Tobacco Control Commission (TCC).

Table 5. Malawi: Average Auction Prices for Tobacco and Tea, 1999-2003

	1999	2000	2001	2002	2003
(Malawi kwacha per kilogram)					
Tobacco 1/	62.2	54.1	89.5	124.6	136.6
Flue cured	64.7	67.9	148.2	143.7	154.4
Fire cured	67.7	53.6	110.7	143.1	144.6
Northern division	67.8	54.2	110.9	143.1	146.4
Southern division	65.7	47.0	109.3	143.7	135.4
Burley	61.5	53.1	85.1	87.0	110.8
Other	43.1	23.1	117.3	...	...
Tea, Malawi auction 2/	37.0	64.7	57.4	68.1	73.0
(Annual percentage change)					
Tobacco 1/	12.3	-13.1	12.0	39.2	9.6
Flue cured	7.9	5.0	41.3	-3.0	7.4
Fire cured	-10.7	-20.7	84.6	29.3	1.0
Northern division	-13.0	-20.1	80.6	29.0	2.3
Southern division	17.7	-28.5	152.5	31.5	-5.8
Burley	14.5	-13.7	7.7	2.2	27.3
Other	-5.0	-46.5	417.7	...	...
Tea, Malawi auction 2/	25.5	74.9	-28.8	18.7	7.2

Source: National Statistics Office, *Monthly Statistical Bulletin*.

1/ Weighted average of auction prices in Lilongwe and Limbe.

2/ Simple average.

Table 6. Malawi: National Composite Consumer Price Index, 1999-2004 (August)

	All Items	Food	Nonfood	All Items	Food	Nonfood	All Items	
Weights (In percent)	100.0	55.5	44.5	100.0	55.5	44.5	100.0	
	(Base 1990 = 100)			(12-month inflation) 1/			(Average inflation) 2/	
1999	1,264	1,418	1,072	28.2	21.9	40.3	44.8	
2000	1,712	1,735	1,684	35.4	22.4	57.0	29.6	
2001	2,091	2,301	1,829	22.1	32.6	8.6	27.2	
2002	2,250	2,405	2,034	7.6	4.5	11.2	14.9	
	All Items	Food	Nonfood	All Items	Food	Nonfood	All Items	
Weights (In percent)	100.0	58.1	41.9	100.0	58.1	41.9	100.0	
	(Base 2000 = 100)			(12-month inflation) 1/			(Average inflation) 2/	
2002	147.6	143.3	153.6	...	...	...	...
2003	Jan.	154.7	153.7	156.1	10.7	8.7	13.4	14.3
	Feb.	159.1	158.9	159.4	10.6	8.4	13.7	13.8
	Mar.	158.1	155.2	161.9	10.3	7.7	13.7	13.2
	Apr.	154.5	148.9	162.3	9.8	7.8	12.4	12.7
	May	151.7	142.7	164.1	9.0	5.7	13.3	12.1
	Jun	146.4	132.7	165.4	8.5	4.0	13.9	11.6
	Jul	146.3	130.4	168.3	8.7	5.3	12.5	11.1
	Aug	147.3	130.8	170.1	9.0	5.1	11.8	10.6
	Sep	155.8	139.5	178.4	9.2	2.0	18.2	10.2
	Oct	155.8	139.6	178.2	9.5	2.8	17.8	9.9
	Nov	159.4	143.8	181.2	9.6	2.8	18.3	9.7
	Dec	162.1	147.6	182.2	9.8	3.0	18.6	9.6
2004	Jan.	170.3	158.9	186.1	10.1	3.4	19.2	9.5
	Feb.	175.4	165.1	189.6	10.2	3.9	19.0	9.5
	Mar.	175.0	163.3	191.3	10.7	5.2	18.2	9.6
	Apr.	171.7	157.6	191.3	11.1	5.8	17.8	9.7
	May	168.9	151.2	193.3	11.3	6.0	17.8	9.9
	Jun	163.4	141.1	194.3	11.6	6.3	17.5	10.1
	Jul	163.0	138.6	196.8	11.4	6.3	16.9	10.3
	Aug	163.9	139.1	198.3	11.3	6.3	16.5	10.5

Source: Malawian authorities; staff estimates.

1/ Annual data refer to 12-month inflation rate at end-December.

2/ Monthly data refer to percentage change of the average index for the 12-month period ending in that month over the corresponding index for the previous year.

Table 7. Malawi: Central Government Operations, FY 1998/99-2003/04

	1998/99	1999/2000	2000/01	2001/02	2002/03 Est.	2003/04 Est.
(In millions of MWI kwacha)						
Total revenue and grants	16,316	22,104	31,233	31,997	42,685	65,365
Revenue	12,075	15,808	20,880	22,853	32,009	42,754
Tax revenue	10,301	14,353	19,285	20,382	27,251	36,902
Taxes on income and profits	4,816	6,590	8,740	9,458	12,146	15,839
Individual	2,136	3,104	3,816	4,174	5,708	7,954
Corporate	2,002	2,570	3,140	2,914	3,678	4,589
Withholding tax	679	916	1,785	2,371	2,760	3,295
Taxes on goods and services	4,012	5,834	8,169	8,935	12,379	16,634
Surtax	3,577	5,189	6,091	6,684	9,322	11,778
Domestic	1,265	1,626	2,429	2,850	4,007	5,546
Import	2,312	3,563	3,663	3,834	5,316	6,231
Excise duties	435	644	2,078	2,251	3,056	4,856
Domestic	0	0	476	483	638	927
Import	0	0	1,602	1,768	2,419	3,930
Taxes on international trade	1,721	2,201	2,385	2,423	3,136	5,082
Other	-248	-271	-10	-435	-410	-653
Misc. duties	29	41	520	-79	243	167
Tax refunds	-277	-432	-460	-320	-652	-820
Tax adjustment (RD) cheques	0	0	-69	-45	0	0
Collection of arrears	0	120	0	9	0	0
Nontax revenue	1,773	1,455	1,595	2,471	4,758	5,852
Departmental receipts	450	1,050	1,036	1,141	1,614	2,237
Petroleum levy for NRA	248	400	559	1,113	1,222	1,285
Petroleum levy for safety nets	0	0	0	169	464	884
Sale receipts from maize (from NFRA)	1,042	0	0	0	591	1,351
Dividends	0	0	0	49	868	95
Transfer of RBM profits	33	5	0	0	0	0
Grants	4,242	6,296	10,353	9,144	10,675	22,611
Program	2,733	3,725	6,209	2,544	1,220	4,580
Food security program	0	0	0	581	188	0
Partially tied grants	...	...	...	...	...	903
EDRC	...	...	...	...	...	1,090
Project	1,508	2,571	3,565	3,479	4,604	9,635
Financing of elections	0	0	0	0	0	653
HIPC Initiative debt relief	0	0	579	1,718	3,588	5,261
Japanese debt relief	0	0	0	821	1,075	490
Total expenditure and net lending	19,736	27,229	37,850.8	42,490	61,322	78,598
Total expenditure	19,475	27,221	37,266	42,490	61,260	78,598
Current expenditure	13,952	17,638	25,736.0	32,675	49,473	58,086
Wages and salaries	3,209	4,296	5,954	9,201	10,930	12,302
Interest payments	2,535	3,400	5,267	6,820	10,985	20,024
Domestic	1,409	2,081	3,426	5,242	8,871	17,253
Foreign	1,126	1,319	1,841	1,578	2,114	2,771
Other current expenditure	8,207	9,942	14,515	16,654	27,559	25,761
Goods and services	5,315	7,043	7,659	10,731	20,127	16,902
<i>Of which: maize purchase</i>	...	...	...	...	6,078	0
Subsidies and other current transfers	2,525	2,624	6,239	5,543	7,431	7,510
Transfer to NRA and MRA	351	542	884	1,844	1,912	2,293
Transfer to National Roads Authority	346	400	552	1,113	1,222	1,285
Transfer to Malawi Revenue Authority	5	141	332	732	690	1,007
Pension and gratuities	667	1,206	1,273	1,376	1,431	1,950
Separation benefits	0	4	79	0	0	0
Discretionary exemptions	12	0	0	0	0	0
Transfer to NFRA/ADMARC	0	0	2,141	858	1,940	353
Other	1,495	872	1,863	1,466	2,148	2,914
Expenditure in arrears (non-cash)	368	276	616	380	0	0
Expenditure for arrears	0	0	0	0	0	1,349

Table 7. Malawi: Central Government Operations, FY 1998/99-2003/04

	1998/99	1999/2000	2000/01	2001/02	2002/03 Est.	2003/04 Est.
(In millions of MWI kwacha)						
Development expenditure	5,524	9,583	11,530	9,816	11,787	20,512
Foreign-financed	4,333	7,651	9,789	7,761	9,521	17,231
Domestically financed	1,190	1,932	1,741	2,055	2,266	3,281
Net lending	261	8	584	0	61	0
Overall balance (including grants)	-3,420	-5,125	-6,618	-10,493	-18,637	-13,233
Total financing	1,908	6,258	6,945	9,148	18,099	14,938
Foreign (net)	4,563	4,373	5,544	-268	-730	425
Borrowing	5,616	6,473	10,456	4,282	4,917	7,185
Program	2,791	1,393	4,521	0	0	0
EDRC	0	0	0	0	0	1,386
Project	2,825	5,080	5,936	4,282	4,917	5,799
Amortization	-1,527	-2,137	-5,129	-3,510	-5,448	-7,577
Special loans (net)	475	37	217	-332	-323	0
Japanese debt relief account	0	0	0	-708	125	759
WB EDRC accounts (NY)	...	...	...	...	...	58
Domestic (net)	-2,655	1,886	1,401	9,416	18,829	14,512
Banking system	-2,774	-1,253	-201	7,402	13,922	7,562
Nonbanks	-40	3,449	1,083	1,797	5,213	6,888
Domestic supplier credits (net)	0	0	573	-277	0	0
Change in arrears	23	-310	-168	332	-307	0
Privatization proceeds	136	0	114	161	0	62
Statistical discrepancy	1,513	-1,133	-327	1,346	538	-1,704

Table 7. Malawi: Central Government Operations, FY 1998/99-2003/04

	1998/99	1999/2000	2000/01	2001/02	2002/03 Est.	2003/04 Est.
	(In percent of GDP)					
Total revenue and grants	24.4	24.1	27.5	24.1	27.7	36.0
Revenue	18.1	17.2	18.4	17.2	20.7	23.5
Tax revenue	15.4	15.6	17.0	15.3	17.7	20.3
Taxes on income and profits	7.2	7.2	7.7	7.1	7.9	8.7
Individual	3.2	3.4	3.4	3.1	3.7	4.4
Corporate	3.0	2.8	2.8	2.2	2.4	2.5
Withholding tax	1.0	1.0	1.6	1.8	1.8	1.8
Taxes on goods and services	6.0	6.4	7.2	6.7	8.0	9.2
Surtax	5.3	5.7	5.4	5.0	6.0	6.5
Domestic	1.9	1.8	2.1	2.1	2.6	3.1
Import	3.5	3.9	3.2	2.9	3.4	3.4
Excise duties	0.6	0.7	1.8	1.7	2.0	2.7
Domestic	0.0	0.0	0.4	0.4	0.4	0.5
Import	0.0	0.0	1.4	1.3	1.6	2.2
Taxes on international trade	2.6	2.4	2.1	1.8	2.0	2.8
Other	-0.4	-0.3	0.0	-0.3	-0.3	-0.4
Misc. duties	0.0	0.0	0.5	-0.1	0.2	0.1
Tax refunds	-0.4	-0.5	-0.4	-0.2	-0.4	-0.5
Tax adjustment (RD) cheques	0.0	0.0	-0.1	0.0	0.0	0.0
Collection of arrears	0.0	0.1	0.0	0.0	0.0	0.0
Nontax revenue	2.7	1.6	1.4	1.9	3.1	3.2
Departmental receipts	0.7	1.1	0.9	0.9	1.0	1.2
Petroleum levy for NRA	0.4	0.4	0.5	0.8	0.8	0.7
Petroleum levy for safety nets	0.0	0.0	0.0	0.1	0.3	0.5
Sale receipts from maize (from NFRA)	1.6	0.0	0.0	0.0	0.4	0.7
Dividends	0.0	0.0	0.0	0.0	0.6	0.1
Transfer of RBM profits	0.0	0.0	0.0	0.0	0.0	0.0
Grants	6.3	6.9	9.1	6.9	6.9	12.5
Program	4.1	4.1	5.5	1.9	0.8	2.5
Food security program	0.0	0.0	0.0	0.4	0.1	0.0
Partially tied grants	...	...	...	...	...	0.5
EDRC	...	...	...	...	...	0.6
Project	2.3	2.8	3.1	2.6	3.0	5.3
Financing of Elections	0.0	0.0	0.0	0.0	0.0	0.4
HIPC Initiative debt relief	0.0	0.0	0.5	1.3	2.3	2.9
Japanese debt relief	0.0	0.0	0.0	0.6	0.7	0.3
Total expenditure and net lending	29.5	29.7	33.4	31.9	39.7	43.3
Total expenditure	29.1	29.6	32.8	31.9	39.7	43.3
Current expenditure	20.9	19.2	22.7	24.6	32.1	32.0
Wages and salaries	4.8	4.7	5.2	6.9	7.1	6.8
Interest payments	3.8	3.7	4.6	5.1	7.1	11.0
Domestic	2.1	2.3	3.0	3.9	5.7	9.5
Foreign	1.7	1.4	1.6	1.2	1.4	1.5
Other current expenditure	12.3	10.8	12.8	12.5	17.9	14.2
Goods and services	7.9	7.7	6.8	8.1	13.0	9.3
Of which: maize purchase	...	...	...	...	3.9	0.0
Subsidies and other current transfers	3.8	2.9	5.5	4.2	4.8	4.1
Transfer to NRA and MRA	0.5	0.6	0.8	1.4	1.2	1.3
Transfer to National Roads Authority	0.5	0.4	0.5	0.8	0.8	0.7
Transfer to Malawi Revenue Authority	0.0	0.2	0.3	0.6	0.4	0.6
Pension and gratuities	1.0	1.3	1.1	1.0	0.9	1.1
Separation benefits	0.0	0.0	0.1	0.0	0.0	0.0
Discretionary exemptions	0.0	0.0	0.0	0.0	0.0	0.0
Transfer to NFRA/ADMARC	0.0	0.0	1.9	0.6	1.3	0.2
Other	2.2	0.9	1.6	1.1	1.4	1.6
Expenditure in arrears (non-cash)	0.5	0.3	0.5	0.3	0.0	0.0
Expenditure for arrears	0.0	0.0	0.0	0.0	0.0	0.7

Table 7. Malawi: Central Government Operations, FY 1998/99-2003/04

	1998/99	1999/2000	2000/01	2001/02	2002/03	2003/04
					Est.	Est.
	(In percent of GDP)					
Development expenditure	8.3	10.4	10.2	7.4	7.6	11.3
Foreign-financed	6.5	8.3	8.6	5.8	6.2	9.5
Domestically financed	1.8	2.1	1.5	1.5	1.5	1.8
Net lending	0.4	0.0	0.5	0.0	0.0	0.0
Overall balance (including grants)	-5.1	-5.6	-5.8	-7.9	-12.1	-7.3
Total financing	2.9	6.8	6.1	6.9	11.7	8.2
Foreign (net)	6.8	4.8	4.9	-0.2	-0.5	0.2
Borrowing	8.4	7.1	9.2	3.2	3.2	4.0
Program	4.2	1.5	4.0	0.0	0.0	0.0
EDRC					0.0	0.8
Project	4.2	5.5	5.2	3.2	3.2	3.2
Amortization	-2.3	-2.3	-4.5	-2.6	-3.5	-4.2
Special loans (net)	0.7	0.0	0.2	-0.2	-0.2	0.0
EU food security account	...	...	...	...	...	...
WB EDRC accounts (NY)	...	...	...	...	...	0.0
Domestic (net)	-4.0	2.1	1.2	7.1	12.2	8.0
Banking system	-4.1	-1.4	-0.2	5.6	9.0	4.2
Nonbanks	-0.1	3.8	1.0	1.4	3.4	3.8
Domestic supplier credits (net)	0.0	0.0	0.5	-0.2	0.0	0.0
Change in arrears	0.0	-0.3	-0.1	0.2	-0.2	0.0
Privatization proceeds	0.2	0.0	0.1	0.1	0.0	0.0
Statistical discrepancy	2.3	-1.2	-0.3	1.0	0.3	-0.9
Memorandum items:						
Primary balance (including grants)	-1.3	-1.9	-1.2	-2.8	-5.0	3.7
Nominal GDP	66,881	91,809	113,447	133,004	154,340	181,560

Sources: Malawian authorities; and Fund staff calculations.

Table 8. Malawi: Functional Classification of Central Government Expenditure, Functional Classification, 1998/99-2003/04

	1998/99	1999/2000	2000/01	2001/02	2002/03 Est.	2003/04 Est.
	(In millions of Malawi kwacha)					
Total spending	16,404	23,189	28,724	45,875	37,510	44,467
General public services	4,096	5,805	9,556	13,553	14,798	17,200
General administration	3,175	4,227	8,027	10,830	11,252	13,588
Defense	446	698	698	988	1,185	1,306
Public order and safety	475	881	831	1,734	2,360	2,307
Social and community services	6,481	9,197	8,791	18,552	16,565	17,582
Education	2,451	3,395	3,722	6,045	7,128	8,714
Health	1,714	1,975	1,868	5,303	4,532	5,559
Social security and welfare	857	1,680	1,199	4,363	1,466	2,149
Housing and community amenity	1,381	1,946	1,857	2,611	3,283	963
Recreational, cultural, and other	37	61	63	101	59	87
Broadcasting and publishing	42	141	83	128	96	109
Economic services	2,145	4,935	5,050	6,950	5,143	9,685
Energy and mining	12	13	20	25	47	1,830
Agriculture and natural resources	1,124	2,058	1,421	3,187	2,630	2,131
Tourism	5	27	30	32	154	257
Physical planning and development	24	46	16	55	126	3,304
Transport and communication	849	2,523	2,371	3,004	1,813	1,613
Industry and commerce	89	174	157	253	120	296
Labor relations and employment	10	21	34	46	237	235
Environmental protection and conservation	18	37	154	296	0	0
Scientific and technological services	8	26	23	36	0	0
Other economic services	6	9	825	15	15	18
Unallocable services	3,681	3,251	5,327	6,821	1,005	0
Total recurrent spending	11,080	13,950	21,856	32,199	25,037	29,029
General public services	3,557	3,778	9,210	10,333	9,172	11,443
General administration	2,660	2,459	7,701	8,023	6,118	8,155
Defense	439	623	688	890	1,122	1,136
Public order and safety	458	696	821	1,420	1,931	2,152
Social and community services	3,373	5,778	5,657	12,431	11,521	12,861
Education	1,679	2,556	2,491	4,300	5,968	6,412
Health	762	1,421	1,750	3,366	3,589	3,654
Social security and welfare	768	1,583	1,199	4,363	1,466	2,129
Housing and community amenity	90	136	118	247	376	510
Recreational, cultural, and other	37	42	54	86	55	77
Broadcasting and publishing	37	40	45	68	66	79
Economic services	689	1,143	1,662	2,615	3,339	4,726
Energy and mining	11	13	20	25	47	136
Agriculture and natural resources	517	798	986	1,787	2,263	2,130
Tourism	5	26	20	25	144	172
Physical planning and development	16	39	10	22	92	130
Transport and communication	63	105	404	445	437	1,609
Industry and commerce	50	89	148	203	103	296
Labor relations and employment	10	21	34	46	237	235
Environmental protection and conservation	2	20	4	9	0	0
Scientific and technological services	8	23	23	36	0	0
Other economic services	6	9	12	15	15	18
Unallocable services	3,462	3,251	5,327	6,821	1,005	0
Total development spending	5,323	9,239	6,868	13,676	12,474	15,438
General public services	539	2,027	346	3,219	5,626	5,757
General administration	515	1,768	326	2,807	5,134	5,432
Defense	7	74	10	98	63	170
Public order and safety	17	184	10	314	429	155
Social and community services	3,109	3,420	3,134	6,121	5,044	4,721
Education	772	839	1,231	1,745	1,160	2,302
Health	952	554	118	1,937	943	1,905
Social security and welfare	88	97	0	0	0	20
Housing and community amenity	1,291	1,810	1,738	2,364	2,907	454
Recreational, cultural, and other	0	19	8	15	4	10
Broadcasting and publishing	6	101	38	60	30	30
Economic services	1,456	3,792	3,388	4,335	1,804	4,959
Energy and mining	1	0				1,694
Agriculture and natural resources	607	1,261	435	1,400	367	2
Tourism	0	1	9	7	10	85
Physical planning and development	8	7	6	33	34	3,174
Transport and communication	785	2,418	1,967	2,559	1,376	4
Industry and commerce	38	86	8	50	17	0
Labor relations and employment	0	0	0	0	0	0
Environmental protection and conservation	16	18	150	287	0	0
Scientific and technological services	0	2	0	0	0	0
Other economic services	0	0	813	0	0	0
Unallocable services	220	0	0	0	0	0

Table 8. Malawi: Functional Classification of Central Government Expenditure, Functional Classification, 1998/99-2003/04

	1998/99	1999/2000	2000/01	2001/02	2002/03 Est.	2003/04 Est.
	(In percent of total for each category of spending)					
Total spending	100.0	100.0	100.0	100.0	100.0	100.0
General public services	25.0	25.0	33.3	29.5	39.4	38.7
General administration	19.4	18.2	27.9	23.6	30.0	30.6
Defense	2.7	3.0	2.4	2.2	3.2	2.9
Public order and safety	2.9	3.8	2.9	3.8	6.3	5.2
Social and community services	39.5	39.7	30.6	40.4	44.2	39.5
Education	14.9	14.6	13.0	13.2	19.0	19.6
Health	10.4	8.5	6.5	11.6	12.1	12.5
Social security and welfare	5.2	7.2	4.2	9.5	3.9	4.8
Housing and community amenity	8.4	8.4	6.5	5.7	8.8	2.2
Recreational, cultural, and other	0.2	0.3	0.2	0.2	0.2	0.2
Broadcasting and publishing	0.3	0.6	0.3	0.3	0.3	0.2
Economic services	13.1	21.3	17.6	15.1	13.7	21.8
Energy and mining	0.1	0.1	0.1	0.1	0.1	4.1
Agriculture and natural resources	6.9	8.9	4.9	6.9	7.0	4.8
Tourism	0.0	0.1	0.1	0.1	0.4	0.6
Physical planning and development	0.1	0.2	0.1	0.1	0.3	7.4
Transport and communication	5.2	10.9	8.3	6.5	4.8	3.6
Industry and commerce	0.5	0.8	0.5	0.6	0.3	0.7
Labor relations and employment	0.1	0.1	0.1	0.1	0.6	0.5
Environmental protection and conservation	0.1	0.2	0.5	0.6	0.0	0.0
Scientific and technological services	0.0	0.1	0.1	0.1	0.0	0.0
Other economic services	0.0	0.0	2.9	0.0	0.0	0.0
Unallocable services	22.4	14.0	18.5	14.9	2.7	0.0
Total recurrent spending	100.0	100.0	100.0	100.0	100.0	100.0
General public services	32.1	27.1	42.1	32.1	36.6	39.4
General administration	24.0	17.6	35.2	24.9	32.6	0.0
Defense	4.0	4.5	3.1	2.8	4.5	0.0
Public order and safety	4.1	5.0	3.8	4.4	8.6	0.0
Social and community services	30.4	41.4	25.9	38.6	46.0	44.3
Education	15.2	18.3	11.4	13.4	23.8	22.1
Health	6.9	10.2	8.0	10.5	14.3	12.6
Social security and welfare	6.9	11.3	5.5	13.6	5.9	7.3
Housing and community amenity	0.8	1.0	0.5	0.8	1.5	1.8
Recreational, cultural, and other	0.3	0.3	0.2	0.3	0.2	0.3
Broadcasting and publishing	0.3	0.3	0.2	0.2	0.3	0.3
Economic services	6.2	8.2	7.6	8.1	13.3	16.3
Energy and mining	0.1	0.1	0.1	0.1	0.2	0.5
Agriculture and natural resources	4.7	5.7	4.5	5.5	9.0	7.3
Tourism	0.0	0.2	0.1	0.1	0.6	0.6
Physical planning and development	0.1	0.3	0.0	0.1	0.4	0.4
Transport and communication	0.6	0.8	1.8	1.4	1.7	5.5
Industry and commerce	0.5	0.6	0.7	0.6	0.4	1.0
Labor relations and employment	0.1	0.2	0.2	0.1	0.9	0.8
Environmental protection and conservation	0.0	0.1	0.0	0.0	0.0	0.0
Scientific and technological services	0.1	0.2	0.1	0.1	0.0	0.0
Other economic services	0.1	0.1	0.1	0.0	0.1	0.1
Unallocable services	31.2	23.3	24.4	21.2	4.0	0.0
Total development spending	100.0	100.0	100.0	100.0	100.0	100.0
General public services	10.1	21.9	5.0	23.5	45.1	37.3
General administration	9.7	19.1	4.7	20.5	41.2	35.2
Defense	0.1	0.8	0.2	0.7	0.5	1.1
Public order and safety	0.3	2.0	0.1	2.3	3.4	1.0
Social and community services	58.4	37.0	45.6	44.8	40.4	30.6
Education	14.5	9.1	17.9	12.8	9.3	14.9
Health	17.9	6.0	1.7	14.2	7.6	12.3
Social security and welfare	1.7	1.1	0.0	0.0	0.0	0.1
Housing and community amenity	24.2	19.6	25.3	17.3	23.3	2.9
Recreational, cultural, and other	0.0	0.2	0.1	0.1	0.0	0.1
Broadcasting and publishing	0.1	1.1	0.6	0.4	0.2	0.2
Economic services	27.3	41.0	49.3	31.7	14.5	32.1
Energy and mining	0.0	0.0	0.0	0.0	0.0	11.0
Agriculture and natural resources	11.4	13.6	6.3	10.2	2.9	0.0
Tourism	0.0	0.0	0.1	0.1	0.1	0.6
Physical planning and development	0.2	0.1	0.1	0.2	0.3	20.6
Transport and communication	14.8	26.2	28.6	18.7	11.0	0.0
Industry and commerce	0.7	0.9	0.1	0.4	0.1	0.0
Labor relations and employment	0.0	0.0	0.0	0.0	0.0	0.0
Environmental protection and conservation	0.3	0.2	2.2	2.1	0.0	0.0
Scientific and technological services	0.0	0.0	0.0	0.0	0.0	0.0
Other economic services	0.0	0.0	11.8	0.0	0.0	0.0
Unallocable services	4.1	0.0	0.0	0.0	0.0	0.0

Sources: Economic Report, National Economic Council; and budget documents, Ministry of Finance.

1/ Fiscal year beginning April 1 until 1997/98; beginning July 1, from 1998/99 onward.

Table 9. Malawi: Accounts of Main Public Enterprises, 1998/99-2003/2004
(In thousands of Malawi kwacha)

	Revenue	Interest Charges	Depreciation	Net Profit or Loss	Gross Investment
Agricultural Development and Marketing Corporation					
1998/99	1,536,228	123,336	26,887	133,793	45,842
1999/2000	3,062,802	323,204	46,998	-350,943	40,756
2000/2001	2,137,727	232,270	49,266	-210,418	112,754
2001/2002	1,624,786	220,495	55,722	-582,230	124,970
2002/2003	1,094,842	328,840	62,294	-180,449	19,799
2003/2004	1,494,042	19,629	52,850	-188,649	...
Air Malawi					
1998/99	1,017,998	28,763	56,389	176,120	2,085,424
1999/2000	1,131,322	16,715	117,401	47,472	2,272,520
2000/2001	1,405,277	32,896	126,692	-177,852	3,253,449
2001/2002	1,488,193	25,868	257,388	-210,847	2,630,630
2002/2003	1,725,459	47,323	196,233	10,790	2,824,688
2003/2004	2,155,127	48,053	206,123	15,421	3,230,290
Electricity Supply Commission (ESCOM)					
1998/99	1,130,285	291,878	160,119	67,721	1,487,965
1999/2000	1,675,378	315,667	194,338	311,287	340,397
2000/2001	2,619,207	418,197	219,259	-378,227	473,147
2001/2002	3,378,421	869,714	404,001	879,593	11,635,334
2002/2003	3,337,038	422,862	623,089	-2,223,069	718,125
2003/2004	3,723,435	978,527	690,050	-2,831,215	1,156,085
Malawi Development Corporation I/					
1998	80,455	25,749	624	-118,234	10,899
1999	1,053,365	141,485	41,246	-54,486	120,618
2000	1,169,931	162,008	47,877	-97,945	385,437
2001	1,684,830	159,703	22,459	-157,052	279,444
2002	1,671,170	220,356	101,871	-401,602	48,063
2003	2,076,583	275,167	108,701	-313,694	718,816
Malawi Housing Corporation					
1998/99	162,821	4,359	26,933	33,862	152,309
1999/2000	221,804	2,742	72,775	12,416	...
2000/2001	253,801	2,827	62,675	-47,628	253,666
2001/2002	214,242	1,831	54,387	-119,349	39,573
2002/2003	295,249	636	55,175	49,549	32,884
2003/2004	399,154	204	52,572	80,475	31,686
Malawi Telecommunications Limited					
1998/99	...	...	...	...	...
1999/2000	...	...	...	...	...
2000/2001	2,443,082	199,485	211,264	-15,958	3,281,759
2001/2002	2,718,985	150,467	273,305	415,469	687,788
2002/2003	3,985,032	73,957	361,975	225,111	1,996,501
2003/2004	5,782,259	209,684	596,550	444,396	352,228
Malawi Posts Corporation					
1998/99	...	...	...	...	...
1999/2000	...	...	...	...	...
2000/2001	273,334	11,204	16,114	-136,570	3,630
2001/2002	295,897	9,311	16,831	-184,597	6,397
2002/2003	323,576	13,811	23,379	-53,334	62,361
2003/2004	397,335	13,380	20,424	-6,363	...

Table 9 (concluded). Malawi: Accounts of Main Public Enterprises, 1998/99-2003/2004
(In thousands of Malawi kwacha)

	Revenue	Interest Charges	Depreciation	Net Profit or Loss	Gross Investment
Blantyre Water Board					
1998/99	346,742	5,936	72,207	36,243	118,416
1999/2000	504,511	87,535	79,091	5,006	84,418
2000/2001	662,867	92,955	81,479	20,351	61,193
2001/2002	910,376	84,876	114,451	-21,301	118,216
2002/2003	962,401	98,150	170,016	-258,799	56,120
2003/2004	324,319	109,198	173,936	-283,547	36,411
Lilongwe Water Board					
1998/99	111,939	21,215	21,827	-56,879	10,275
1999/2000	126,898	27,072	42,694	-147,733	21,514
2000/2001	260,975	28,734	46,804	26,137	16,699
2001/2002	348,411	29,387	53,027	109,071	48,238
2002/2003	440,402	70,597	71,494	19,525	884,771
2003/2004	507,263	62,432	77,597	-233,311	63,528
Cental Region Water Board					
1998/99	49,023	4,632	6,512	-17,747	9,746
1999/2000	68,588	7,161	4,888	-27,737	12,392
2000/2001	83,795	10,677	5,478	-33,447	27,817
2001/2002	115,871	12,215	5,599	-7,716	288,908
2002/2003	178,706	11,997	47,796	2,655	24,359
2003/2004	210,800	22,221	6,199	-5,905	670,623
Northern Region Water Board					
1998/99	45,208	4,746	5,976	-9,118	61,697
1999/2000	78,564	11,529	5,342	13,852	4,356
2000/2001	109,209	25,353	5,585	14,764	669,126
2001/2002	188,196	28,225	6,446	12,876	18,586
2002/2003	167,443	8,963	6,742	-3,823	23,648
2003/2004	165,676	8,521	13,162	-31,024	1,458,438
Southern Region Water Board					
1998/99	54,813	2,001	4,953	-2,599	416,273
1999/2000	109,316	1,498	8,386	7,505	700,883
2000/2001	148,125	1,052	8,423	29736	330,627
2001/2002	189,901	272	59,887	-60590	229,255
2002/2003	261,727	398	62,816	12484	69,755
2003/2004	282,197	1,783	58,975	-1057	16,681

Source: Malawian authorities.

1/ Year-end December 31.

Table 10. Malawi: Interest Rates, 1999-2003
(In percent per annum, unless otherwise indicated; end of period)

	1999	2000	2001	2002	2003
Reserve Bank of Malawi					
Bank rate	47.0	50.2	46.8	40.0	35.0
Treasury bills 1/					
91 days	39.6	86.6	54.6	36.1	33.1
182 days	60.1	65.1	56.4	37.2	34.0
271 days	53.8	83.6	50.9	38.6	33.9
Commercial banks 2/					
Lending rates 3/					
Minimum (= prime lending rate)	47.0	53.0	46.0	40.0	36.0
Maximum	53.0	59.0	52.0	46.0	42.0
Deposits					
Savings					
Short term 4/	30.0	35.0	26.0	18.5	12.0
3 months	33.0	37.5	30.0	...	...
12 months	nego.	nego.	nego.	nego.	nego.
Other financial institutions 4/					
New Building Society					
Fixed deposits (6-11 months)	30.0	36.0	30.0	23.0	18.0
Savings deposits	25.0	27.0	23.0	16.0	14.0
Investment deposits	26.0	32.5	27.0	17.0	18.0
Minimum mortgage rate 3/	...	38.0	35.5	31.5	28.5
Leasing and Finance Co.					
Lending rate	51.0	37.0	54.0	54.0	41.0
3-month time deposits	...	39.0	35.0	26.0	26.0
Investment and Development Bank					
24-hour notice of withdrawal	7.0	6.0	7.0	7.0	6.0
30-day time deposits 5/	29.0	31.0	32.0	22.0	19.0
12-month time deposits 5/	...	nego.	nego.	nego.	nego.
Local registered stocks 6/	42.0	38.5	38.5	40.0	40.0
Memorandum items:					
Real interest rates 7/					
Commercial banks					
Prime lending rate	14.7	13.0	19.6	30.1	23.9
Savings deposits	1.4	-0.3	3.2	10.1	2.0
Local registered stock	10.8	2.3	13.4	30.1	27.5
Composite consumer price index					
(12-month rate of change, in percent)	28.2	35.4	22.1	7.6	9.8

Source: Reserve Bank of Malawi; and IMF staff estimates.

1/ Annualized interest rate at end period.

2/ Selected from a much wider range of rates offered by the institutions.

3/ Effective July 23, 1987, these rates were deregulated and set independently by the commercial banks.

4/ MK 10,000 or over; subject to 30 days' written notice of withdrawal; maximum MK 1 million.

5/ MK 250,000 or over.

6/ Maximum available nominal rate on stock with five years or more to redemption.

7/ Deflated by 12-month rate of change in the consumer price index.

Table 11: Malawi: Monetary Survey March 2001 - June 2004 1/

	2001			2002			2003			2004				
	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.
Money and quasi-money	16,951	22,081	20,974	21,725	20,058	23,983	25,402	27,210	26,641	31,521	33,869	35,183	35,776	42,741
Money	8,877	11,755	11,014	10,343	9,712	12,791	13,213	13,440	13,421	17,154	18,008	17,464	17,012	23,503
Quasi-money	8,075	10,327	9,960	11,382	10,346	11,192	12,189	13,770	13,220	14,367	15,861	17,718	18,764	19,238
Of which: foreign currency deposits	2,541	3,235	2,289	3,149	3,094	3,560	3,655	4,505	4,549	4,772	5,886	5,362	7,234	7,719
Net foreign assets (NFA) 2/	16,729	18,693	15,218	11,652	7,208	11,391	5,222	-380	-489	3,883	3,322	5,466	6,128	6,585
NFA (In millions of U.S. dollars)	212	247	239	156	94	149	65	-4	-5	43	31	50	56	60
Gross foreign assets	321	336	329	244	180	237	171	153	138	148	141	167	170	175
Foreign liabilities	-109	-89	-90	-89	-86	-88	-106	-157	-143	-105	-110	-117	-113	-114
Monetary authorities	14,158	14,632	12,739	7,546	3,998	7,194	1,531	-3,558	-4,467	-330	-1,210	1,455	698	-8
NFA of the monetary authorities (In millions of U.S. dollars)	183	197	206	111	51	94	19	-41	-49	-4	-11	13	6	0
Gross foreign assets	280	273	283	185	125	167	114	103	85	90	81	116	106	94
Foreign liabilities	-98	-75	-77	-74	-74	-73	-95	-144	-134	-93	-92	-102	-100	-94
Commercial banks	2,570	4,061	2,479	4,106	3,210	4,197	3,691	3,178	3,978	4,213	4,532	4,011	5,429	6,593
NFA of the commercial banks (In millions of U.S. dollars)	30	49	33	45	43	55	46	36	43	47	42	37	50	61
Gross foreign assets	41	63	46	60	55	70	57	49	53	59	60	52	63	81
Foreign liabilities	-11	-14	-13	-15	-12	-15	-11	-13	-9	-12	-18	-15	-14	-21
Net domestic assets (NDA)	223	3,388	5,756	10,073	12,851	12,892	20,180	27,590	27,130	27,638	30,547	29,717	29,649	36,156
Credit to government (net)	-3,838	-1,862	892	5,829	7,372	5,520	9,218	15,626	17,995	19,458	20,410	18,694	19,068	27,023
Credit to statutory bodies (net)	683	738	113	-109	367	482	152	-120	-588	-698	-266	-352	-222	-720
Credit to private sector	5,478	5,289	6,016	6,454	6,998	6,838	6,916	7,363	7,341	9,665	8,888	9,809	9,544	10,459
Other items (net)	-2,100	-777	-1,263	-2,100	-1,886	-2,47	3,894	4,721	2,182	-787	1,515	1,566	1,259	-607
RBM's revaluation accounts	-38	-185	-325	-49	198	254	451	-4	170	-337	-119	0	10	0
Open market operations	-826	-1,375	-4,015	-6,312	-4,961	-5,746	-5,991	-4,508	-5,395	-8,056	-4,080	-2,574	-4,565	-5,039
Encumbered reserves	1,522	1,300	1,169	1,229	1,306	2,001	6,513	5,105	2,998	1,784	1,989	759	761	305
Others	-2,757	-518	1,908	3,032	1,571	3,243	2,921	4,128	4,409	5,822	3,725	3,381	5,053	4,127
Memorandum items:														
Money and quasi money	39.2	52.8	21.4	21.2	18.3	8.6	21.1	25.2	32.8	31.4	33.3	29.3	34.3	35.6
Net foreign assets	68.2	61.0	21.0	-8.0	-56.2	-33.1	-47.7	-55.4	-38.4	-31.3	-7.5	21.5	24.8	8.6
Net domestic assets	-28.7	-8.2	0.3	29.2	74.5	41.7	68.8	80.6	71.2	62.7	40.8	7.8	9.5	27.0
Credit to the government	-28.9	-1.4	-1.4	29.4	66.1	33.4	39.7	45.1	53.0	58.1	44.1	11.3	4.0	24.0
Credit to statutory bodies	-2.2	-1.0	-4.6	-6.4	-1.9	-1.2	0.2	-0.1	-4.8	-4.9	-1.6	-0.9	1.4	-0.1
Credit to the private sector	5.4	-1.2	3.8	3.6	9.0	7.0	4.3	4.2	4.7	11.8	7.8	9.0	7.5	2.5
Other assets (net)	-3.1	-3.6	2.5	2.7	1.3	2.4	24.6	31.4	20.3	-2.3	-9.4	-11.6	-3.5	0.6

Source: Reserve Bank of Malawi, and IMF staff estimates.

1/ Includes 4 commercial banks (NBM, Starbic, FBM, and FMB) and the RBM

2/ Excluding encumbered reserves

Table 12. Malawi: Summary Accounts of Monetary Authorities, March 2001-June 2004
(In millions of Malawi kwacha; end of period)

	2001			2002			2003			2004				
	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.
Reserve money	6,102	7,844	8,537	8,165	7,245	8,877	9,879	10,682	8,717	9,836	12,846	13,743	12,058	18,723
Currency outside banks	3,820	5,299	4,672	4,066	4,306	6,067	6,226	5,964	5,558	7,827	8,160	7,838	7,211	11,072
Cash in vault	447	494	526	924	509	683	852	1,101	909	1,079	1,173	1,449	1,382	1,418
Commercial bank deposits with RBM	1,835	2,050	3,339	3,174	2,430	2,128	2,801	3,617	2,250	930	3,512	4,455	3,465	6,233
Net foreign assets (NFA)	14,158	14,632	12,739	7,546	3,998	7,194	1,531	-3,558	-4,467	-330	-1,210	1,455	698	-8
NFA (in millions of U.S. dollars)	183	197	206	111	51	94	19	-41	-49	-4	-11	13	6	0
Gross foreign assets	280	273	283	185	125	167	114	103	85	90	81	116	106	94
Foreign liabilities	-98	-75	-77	-74	-74	-73	-95	-144	-134	-93	-92	-102	-100	-94
Net domestic assets	-8,057	-6,789	-4,201	618	3,247	1,683	8,348	14,239	13,184	10,166	14,056	12,288	11,360	18,731
Credit to government (net)	-5,620	-3,498	-957	3,830	4,313	1,386	4,661	9,666	11,334	10,613	10,487	8,245	9,323	17,215
Credit to statutory bodies (net)	296	296	292	166	314	314	314	0	0	0	0	0	0	0
Credit to domestic banks	4	4	15	4	3	6	3	3	118	3	138	3	3	2
Other items (net)	-2,737	-3,591	-3,552	-3,381	-1,383	-22	3,370	4,570	1,731	-450	3,431	4,039	2,034	1,514
Revaluation accounts	-38	-185	-325	-49	198	254	451	-4	170	-337	-119	0	10	0
Open market operations	-1,706	-3,801	-6,911	-7,746	-5,908	-6,621	-7,201	-5,850	-7,018	-9,212	-4,566	-2,914	-5,233	-5,199
Encumbered reserves	1,522	1,300	1,169	1,229	1,306	2,001	6,513	5,105	2,998	1,784	1,989	759	761	305
Others	-2,515	-905	2,515	3,185	3,021	4,344	3,608	5,319	5,581	7,315	6,127	6,194	6,495	6,408

Source: Reserve Bank of Malawi, and IMF staff estimates.

Table 13. Malawi: Summary Accounts of Commercial Banks, March 2001-June 2004
(In millions of Malawi kwacha, unless otherwise indicated; end of period)

	2001			2002			2003			2004				
	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.
Deposits of the private sector	13,131	16,782	16,302	17,659	15,752	17,916	19,176	21,246	21,083	23,694	25,709	27,344	28,565	31,669
Demand deposits	5,056	6,455	6,342	6,277	5,406	6,724	6,987	7,476	7,863	9,328	9,848	9,626	9,801	12,431
Foreign currency deposits	5,533.3	7,092.0	7,671.1	8,232.7	7,252.0	7,631.8	8,533.8	9,265.8	8,671.0	9,594.7	9,975.3	12,356.1	11,529.4	11,518.7
Time and saving deposits	2,541.3	3,234.5	2,288.7	3,149.4	3,094.2	3,560.4	3,655.0	4,504.6	4,549.0	4,772.1	5,885.7	5,362.4	7,234.4	7,719.1
Net foreign assets	2,570	4,061	2,479	4,106	3,210	4,197	3,691	3,178	3,978	4,213	4,532	4,011	5,429	6,593
Foreign assets	3,431	5,078	3,282	5,121	4,124	5,359	4,601	4,296	4,839	5,263	6,446	5,614	6,908	8,831
Foreign liabilities	-861	-1,017	-803	-1,016	-914	-1,162	-909	-1,118	-861	-1,050	-1,914	-1,603	-1,478	-2,238
Cash and reserves	2,172	2,279	3,590	4,159	3,106	2,666	3,470	4,838	3,027	2,183	4,526	5,350	5,061	6,910
Cash	447	494	526	924	509	683	852	1,101	909	1,079	1,173	1,449	1,382	1,418
Deposits with Reserve Bank of Malawi	1,726	1,785	3,064	3,234	2,596	1,984	2,618	3,737	2,118	1,104	3,352	3,901	3,679	5,492
Net domestic assets	8,388	10,442	10,225	9,395	9,437	11,053	12,015	13,230	14,078	17,299	16,651	17,984	18,075	18,166
Domestic credit (net)	7,943	7,663	7,976	8,344	10,424	11,454	11,625	13,203	13,614	17,813	18,545	19,905	19,067	19,548
Credit to the government (net)	2,079	1,932	2,140	2,166	3,372	4,448	4,870	5,960	6,661	8,846	9,922	10,449	9,746	9,808
Credit to statutory bodies (net)	386	442	-180	-276	54	168	-162	-120	-588	-698	-266	-352	-222	-720
Credit to the private sector	5,478	5,289	6,016	6,454	6,998	6,838	6,916	7,363	7,541	9,665	8,888	9,809	9,544	10,459
Other assets (net)	445	2,779	2,249	1,051	-987	-401	390	28	464	-514	-1,894	-1,922	-992	-1,381
Claims on other banks	821	1,315	908	1,611	241	951	399	1,205	954	1,966	1,477	1,226	791	1,231
Premises and other equipment	1,677	1,805	1,866	1,769	1,760	1,841	1,939	2,278	2,397	2,528	2,897	2,851	3,141	3,363
Other assets	3,080	4,101	3,176	3,287	3,303	3,962	4,910	4,607	4,928	4,679	4,084	4,898	5,948	5,830
Liabilities to other banks	-101	-351	-174	-151	-300	-424	-149	-402	-448	-86	-59	-75	-122	-98
Capital accounts	-3,308	-3,635	-3,549	-3,730	-4,178	-4,309	-4,577	-4,903	-5,484	-5,880	-6,082	-6,564	-6,962	-6,927
Reserve Bank of Malawi bills	880	2,426	2,895	1,434	947	875	1,210	1,342	1,622	1,156	486	340	668	160
Nonperforming debts	-1,142.7	-870.2	-1,103.1	-900.8	-906.0	-1,259.9	-1,568.8	-1,662.0	-1,136.3	-1,225.8	-598.0	-991.8	-1,098.9	-1,308.0
Other liabilities	-1,460	-2,012	-1,770	-2,268	-1,854	-2,038	-1,774	-2,438	-2,369	-3,651	-4,100	-3,605	-3,356	-3,633
Memorandum item:														
Reserve/deposit ratio (in percent)	13.1	10.6	18.8	18.3	16.5	11.1	13.7	17.6	10.0	4.7	13.0	14.3	12.9	17.3

Source: Reserve Bank of Malawi.

Table 14. Malawi: Commercial Banks' Advances by Sector, 1999-2003 1/

	1999	2000	2001	2002	2003
(In millions of kwacha, end of period)					
Agriculture	617	499	566	128	1,059
Mining and quarrying	6	9	37	9	1
Manufacturing	914	1,229	2,207	1,141	2,066
Electricity, water, and gas	4	195	456	491	132
Construction and civil engineering	151	378	490	141	810
Wholesale and retail trade	1,260	1,120	939	858	1,653
Transport, storage, and communications	93	1,192	269	149	746
Finance, insurance, real estate, and business services	688	507	272	111	682
Community, social, and personal services	153	849	149	941	645
Personal accounts	342	633	1,166	2	1,848
Total	4,229	6,611	6,549	3,971	9,640
(In percent of total)					
Agriculture	14.6	7.5	8.6	3.2	11.0
Mining and quarrying	0.1	0.1	0.6	0.2	0.0
Manufacturing	21.6	18.6	33.7	28.7	21.4
Electricity, water, and gas	0.1	3.0	7.0	12.4	1.4
Construction and civil engineering	3.6	5.7	7.5	3.5	8.4
Wholesale and retail trade	29.8	16.9	14.3	21.6	17.1
Transport, storage, and communications	2.2	18.0	4.1	3.7	7.7
Finance, insurance, real estate, and business services	16.3	7.7	4.2	2.8	7.1
Community, social, and personal services	3.6	12.8	2.3	23.7	6.7
Personal accounts	8.1	9.6	17.8	0.1	19.2

Sources: Reserve Bank of Malawi, Financial and Economic Review; and Malawian authorities.

1/ From December 1999 onward, includes Finance Bank of Malawi, First Merchant Bank, and Malawi Savings Bank.

Table 15. Malawi: Summary Accounts of Nonbank Financial Institutions, March 2000-June 2004 1/
(In millions of Malawi kwacha, end of period)

	2000			2001			2002			2003			2004	
	Mar.	Jun.	Dec.	Mar.	Jun.	Dec.	Mar.	Jun.	Dec.	Mar.	Jun.	Dec.	Mar.	Jun.
Cash deposits with monetary authorities	12	48	26	35	119	788	539	250	1,181	1,675	1,228	1,159	948	133
Domestic assets (net)	5,194	5,613	7,170	6,799	7,438	6,669	4,190	4,768	5,039	3,559	4,290	6,020	5,861	6,346
Credit to the government	574	727	1,255	1,283	1,738	1,782	1,478	1,936	2,169	1,560	2,137	3,865	3,582	3,960
Credit to statutory bodies	75	76	30	23	80	48	21	28	32	27	39	40	38	9
Credit to the private sector	2,428	2,813	2,983	2,979	2,903	2,940	1,884	1,834	1,980	1,194	1,174	1,188	1,334	1,387
Other assets (net)	2,117	1,998	2,902	2,514	2,718	1,898	807	971	858	778	940	927	907	991
Other assets (gross) 2/	1,164	1,013	1,305	1,199	1,414	1,133	448	525	419	451	495	517	627	687
Other liabilities (gross) 3/	953	985	1,597	1,315	1,304	765	359	446	439	327	445	410	280	304
Deposits	2,955	3,228	3,788	3,580	4,406	4,755	3,645	4,116	4,234	3,636	4,605	5,416	5,724	6,529
Share capital	504	517	830	763	723	1,027	591	664	932	797	1,099	1,284	1,190	1,242
Liabilities to banks 4/	63	59	212	65	77	34	66	0	27	14	16	42	39	2
Insurance and assurance companies														
Credit to the government	708	...	...	271	322	393	417	474	447	545	571	547	725	...
Credit to the private sector	220	...	...	44	45	158	34	34	44	45	38	25	56	...
Credit to banks	50	...	...	69	145	115	207	137	245	214	169	309	3,062	...
Demand deposits	-35	...	...	0	0	0	0	0	0	0	0	0	0	...
Time and savings deposits	85	...	...	69	145	115	207	137	245	214	169	309	3,062	...
Other assets	399	...	...	166	150	136	96	95	81	171	152	97	1,306	...
Total assets	1,377	...	...	550	662	801	754	741	817	976	930	978	5,149	...
Premiums received	1,061	...	...	...	...	...	...	...	...	...	...	...	...	...
Expenses, commissions, and claims paid	66	...	...	...	...	...	...	...	...	...	...	...	...	...
Premiums (net)	995	...	...	...	...	...	...	...	...	...	...	...	...	...
Investment income	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Miscellaneous income	...	...	...	...	...	...	...	...	...	...	...	...	...	...

Sources: Reserve Bank of Malawi, Financial and Economic Review; and other data provided by the Reserve Bank of Malawi.

1/ Malawi Savings Bank (MSB), New Building Society (NSB), Mercantile Credit Bank (MCB), and Investment Development Bank (Indebank); from May 1999 onward, includes also Leasing and Finance (LFC), Finance Corporation of Malawi (FINCOM), Indefinance, and CBM Finance.

2/ From March 1999 onward, other assets of all other financial institutions, excluding LFC, FINCOM, Indefinance, and CBM Finance.

3/ From March 1999 onward, other liabilities of all other financial institutions, excluding LFC, FINCOM, Indefinance, and CBM Finance.

4/ Liabilities to banks of all other financial institutions put together.

Table 16. Malawi: Balance of Payments, 1999-2003
(In millions of U.S. dollars, unless otherwise indicated)

	1999	2000	2001	2002	2003
Current account balance (incl. grants)	-147.5	-91.5	-116.5	-221.2	-149.8
Trade balance	-226.4	-161.4	-157.9	-305.7	-227.5
Exports	447.1	401.8	426.6	421.1	402.1
<i>Of which: tobacco</i>	274.6	246.8	254.5	232.7	211.9
Imports	-673.5	-563.2	-584.5	-726.8	-629.6
Services balance	-86.5	-85.8	-66.3	-165.1	-88.7
Interest public sector (net)	-21.3	-20.6	-17.8	-20.2	-25.5
Receipts	8.8	12.1	8.7	2.5	1.5
Payments	-30.2	-32.7	-26.5	-22.7	-27.0
Other factor payments	-20.4	-15.8	-15.3	-24.5	-15.1
Nonfactor (net)	-44.8	-49.4	-33.1	-120.4	-48.1
Receipts	50.6	44.5	54.8	50.6	36.9
Payments	-95.3	-93.9	-87.9	-171.1	-85.0
Unrequited transfers (net)	165.4	155.6	107.7	249.6	166.4
Private (net)	8.9	7.8	9.9	14.3	12.4
Receipts	21.8	21.8	21.8	27.7	27.7
Payments	-12.9	-13.9	-11.8	-13.4	-15.3
Official	156.5	147.8	97.7	235.3	154.0
Receipts	157.9	148.4	98.3	235.3	154.0
Payments	-1.3	-0.6	-0.6	0.0	0.0
Capital account balance (incl. errors and omissions)	163.3	80.7	85.0	64.7	102.0
Medium- and long-term flows	89.9	65.0	59.8	23.8	29.5
Disbursements	128.9	124.9	127.0	81.0	98.1
Amortization (public sector)	-39.0	-59.9	-67.2	-57.2	-68.6
Foreign direct investment and other inflows	39.4	27.0	28.0	37.6	43.2
Short-term capital and errors and omissions	34.0	-11.3	-2.8	3.3	29.3
Overall balance	15.8	-10.8	-31.5	-156.5	-47.7
Financing	-15.8	10.8	31.5	156.5	47.8
Central bank	-30.8	16.6	11.8	111.4	7.0
Reserves (-increase)	13.6	1.7	40.7	40.8	41.4
Liabilities	-44.4	14.9	-28.9	70.6	-34.4
<i>Of which: IMF (net)</i>	-12.8	-1.8	-7.8	15.6	-1.0
Purchases/drawings	10.6	8.4	0.0	23.0	9.3
Repurchases/repayments	-23.5	-10.2	-7.8	-7.4	-10.2
Commercial banks	15.0	-5.7	-7.7	14.5	-6.7
Arrears	0.0	0.0	0.0	0.0	0.0
Debt relief	0.0	0.0	27.4	30.6	47.5
Memorandum items:					
Gross official reserves					
In millions of U.S. dollars	246.0	243.6	202.9	162.1	120.7
In months of imports 1/	4.5	4.3	3.0	2.7	1.8
Current account balance (percent of GDP)					
Excluding official transfers	-16.9	-14.1	-12.6	-24.5	-17.8
Including official transfers	-8.2	-5.4	-6.8	-11.9	-8.8
Malawi kwacha per U.S. dollar (end year)	44.1	59.5	72.2	76.7	97.4
Terms of trade	-13.4	1.1	-0.3	-7.5	-7.9

Sources: Malawian authorities; and staff estimates.

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

Table 17. Export Volumes, Values and Prices, 1999- 2003
(Volume in million kilogrammes, value in millions of Kwacha and average prices in Kwacha per kilogramme)

	1999	2000	2001	2002	2003
Average export prices					
Tobacco	100.7	137.6	148.0	155.7	200.7
Tea	36.9	55.0	66.8	66.8	65.8
Sugar	18.0	28.3	26.5	27.0	38.9
Cotton	47.0	49.3	52.1	62.9	97.7
Rice	32.4	14.7	22.9	36.3	36.3
Coffee	89.1	84.4	74.3	67.1	90.9
Pulses	14.5	15.6	26.0	29.4	30.8
Export volume					
Tobacco	120.3	106.8	124.2	114.7	100.0
Tea	47.0	40.0	38.5	38.4	38.0
Sugar	56.7	82.3	94.2	126.0	119.2
Cotton	5.0	8.5	6.1	4.1	5.0
Rice	3.4	6.6	3.8	1.5	5.4
Coffee	4.4	3.7	3.8	2.8	2.9
Pulses	19.6	8.5	2.6	7.6	15.1
Export value					
Tobacco	12,109.1	14,696.4	18,376.2	17,851.1	20,072.3
Tea	1,734.6	2,200.0	2,570.6	2,563.8	2,500.0
Sugar	1,019.5	2,334.1	2,500.0	3,396.2	4,635.1
Cotton	235.0	420.2	317.9	260.8	483.9
Rice	110.1	96.6	86.8	54.5	195.2
Coffee	392.2	312.0	282.2	187.9	266.7
Pulses	284.9	132.2	66.7	222.5	466.5
Other exports					
Skins and hides	13.9	21.1	33.5	32.1	25.7
Flowers and Live Trees	22.4	20.6	32.2	33.7	11.3
Edible nuts	158.0	212.5	336.5	378.1	1,011.6
Spices	58.1	85.6	78.3	224.1	123.4
Beverage, Spirits and Vinegar	51.9	81.0	15.2	9.9	6.1
Natural Rubber	54.0	73.7	170.7	152.9	240.9
Wood Products	18.1	34.3	57.4	62.7	164.3
Cotton Fabrics	44.8	3.2	32.2	18.7	23.8
Woven Fabric	5.9	8.6	0.2	10.8	13.7
Knitted Apparel	372.3	405.0	550.2	742.7	1,009.8
Unknitted Apparel	330.3	381.0	1,467.8	1,721.9	2,365.3
Other	1,345.8	1,851.9	2,938.6	1,482.4	4,158.9
Domestic Exports	18,360.9	23,370.0	29,913.2	29,406.6	37,774.5
Re Exports	1,351.6	555.1	884.8	2,306.4	847.9
Merchandise Exports	19,712.5	23,925.1	30,798.0	31,713.1	38,622.4
Memorandum items					
Export unit price	22.5	36.7	7.7	4.5	27.9
Export quantum	-6.1	-7.0	11.2	-3.0	-8.8
Period average exchange rate (K/USD)	44.1	59.5	72.2	76.7	97.5

Source: Malawi, National Statistical Office

Table 18. Malawi: Tobacco Exports, 1996-2001

(Values in millions of U.S. dollars; volumes in thousands of tons; and prices in U.S dollars per kilogram)

	1996	1997	1998	1999	2000	2001
Flue cured						
Value	51.3	64.9	28.3	32.7	21.1	13.1
Volume	16.4	17.9	11.4	16.3	9.5	7.3
Unit value	3.1	3.6	2.5	2.0	2.2	1.8
Burley						
Value	203.4	246.8	179.5	208.7	206.3	188.0
Volume	73.1	86.2	69.3	78.6	88.7	94.0
Unit value	2.8	2.9	2.6	2.7	2.3	2.0
NDDF						
Value	...	...	...	11.3	4.9	9.1
Volume	...	...	...	7.8	6.2	4.9
Unit value	...	...	...	1.5	0.8	1.9
Fire cured (northern division)						
Value	14.8	18.2	30.1	...	...	...
Volume	4.9	6.3	11.7	...	...	...
Unit value	3.0	2.9	2.6	...	...	...
Fire cured (southern division)						
Value	0.7	0.3	93.8	...	...	...
Volume	0.3	0.8	34.1	...	...	...
Unit value	2.3	0.4	2.8	...	...	...
Sun/air-cured						
Value	0.7	1.5	2.8	0.7	0.9	0.1
Volume	0.3	0.5	1.4	0.3	0.4	0.1
Unit value	2.3	3.0	2.0	2.7	2.2	1.3
Other (commercial)						
Value	1.6	1.0	3.1	18.6	18.7	10.8
Volume	0.6	0.3	1.3	7.2	8.2	5.6
Unit value	2.7	3.3	2.4	2.6	2.3	1.9
Total						
Value	272.5	332.7	337.6	260.5	246.8	212.0
Volume	95.6	112.0	129.2	102.3	106.8	107.0
Unit value	2.9	3.0	2.6	2.5	2.3	2.0

Source: Tobacco Control Commission (TCC).

Table 19. Malawi: Direction of Trade, 1999-2003

	Exports					Imports				
	1999	2000	2001	2002	2003	1999	2000	2001	2002	2003
(In millions of U.S. dollars)										
<i>DOTS</i> World total	482.3	423.8	473.5	466.2	558.8	635.2	568.0	447.5	546.3	617.8
Industrial	290.7	243.5	274.3	245.2	297.5	129.8	92.2	90.4	142.0	110.9
France	8.6	8.8	11.3	8.9	7.6	10.0	5.1	6.1	11.2	9.8
Germany	72.1	29.3	55.9	56.6	62.7	30.1	13.0	17.3	14.4	11.0
Japan	21.1	46.5	32.7	23.9	25.5	16.6	12.7	13.0	16.9	21.2
Netherlands	43.0	28.6	27.0	22.1	23.4	4.0	7.4	3.8	3.5	3.1
United Kingdom	16.0	15.3	19.6	17.3	17.5	31.2	18.1	13.0	22.1	18.3
United States	69.1	53.8	76.5	69.5	75.3	9.5	14.4	16.3	33.0	18.4
Other	60.9	61.2	51.2	47.1	85.6	28.4	21.5	21.0	41.0	29.1
Developing countries	191.6	180.3	199.2	221.0	261.3	505.5	475.8	357.1	404.2	506.9
Africa	95.5	105.8	113.1	121.0	159.5	435.6	416.5	308.9	348.7	429.7
Botswana	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Mozambique	2.5	0.5	2.9	2.6	3.3	5.3	12.1	12.9	11.4	13.8
South Africa	74.7	85.9	94.8	102.9	130.3	258.2	260.2	252.3	273.8	331.9
Tanzania	3.2	1.7	1.9	1.3	1.7	10.9	12.1	6.5	19.5	23.7
Zambia	2.6	2.2	3.1	3.3	8.6	66.1	62.8	10.6	13.1	22.3
Zimbabwe	7.0	6.0	2.6	2.9	3.6	80.3	52.4	9.6	10.4	12.6
Other	5.5	9.5	7.8	8.0	12.1	14.9	16.9	17.1	20.4	25.4
Other developing countries	96.2	74.5	86.1	100.0	101.8	69.9	59.3	48.2	55.5	77.2
(In percent of total, unless otherwise indicated)										
<i>DOTS</i> World total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Industrial	60.3	57.5	57.9	52.6	53.2	20.4	16.2	20.2	26.0	17.9
France	1.8	2.1	2.4	1.9	1.4	1.6	0.9	1.4	2.1	1.6
Germany	15.0	6.9	11.8	12.1	11.2	4.7	2.3	3.9	2.6	1.8
Japan	4.4	11.0	6.9	5.1	4.6	2.6	2.2	2.9	3.1	3.4
Netherlands	8.9	6.8	5.7	4.7	4.2	0.6	1.3	0.9	0.6	0.5
United Kingdom	3.3	3.6	4.1	3.7	3.1	4.9	3.2	2.9	4.0	3.0
United States	14.3	12.7	16.2	14.9	13.5	1.5	2.5	3.6	6.0	3.0
Other	12.6	14.4	10.8	10.1	15.3	4.5	3.8	4.7	7.5	4.7
Developing countries	39.7	42.5	42.1	47.4	46.8	79.6	83.8	79.8	74.0	82.1
Africa	19.8	25.0	23.9	26.0	28.5	68.6	73.3	69.0	63.8	69.6
Botswana	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Mozambique	0.5	0.1	0.6	0.6	0.6	0.8	2.1	2.9	2.1	2.2
South Africa	15.5	20.3	20.0	22.1	23.3	40.6	45.8	56.4	50.1	53.7
Tanzania	0.7	0.4	0.4	0.3	0.3	1.7	2.1	1.4	3.6	3.8
Zambia	0.5	0.5	0.6	0.7	1.5	10.4	11.0	2.4	2.4	3.6
Zimbabwe	1.5	1.4	0.6	0.6	0.6	12.6	9.2	2.1	1.9	2.0
Other	1.1	2.2	1.6	1.7	2.2	2.3	3.0	3.8	3.7	4.1
Other developing countries	19.9	17.6	18.2	21.4	18.2	11.0	10.4	10.8	10.2	12.5
Memorandum items:										
Group of countries										
(in millions of U.S. dollars)										
European Union	188.9	130.1	151.6	139.4	180.1	98.3	58.9	54.6	73.0	65.7
Cross-Border Initiative countries 1/	14.4	14.9	16.4	...	...	165.1	176.1	194.0	...	...
Group of countries										
(in percent of total)										
European Union	39.2	30.7	32.0	29.9	32.2	15.5	10.4	12.2	13.4	10.6
Cross-Border Initiative countries 1/	3.0	3.5	3.5	...	...	26.0	31.0	43.4	...	...

Source: IMF, Direction of Trade Statistics (DOTS).

1/ Now Regional Integration Facilitation Forum.

Table 20. Malawi: Public Sector External Debt and Debt Service, 1999-2003
(In millions of U.S. dollars, unless otherwise indicated)

	1999	2000	2001	2002	2003
Total debt stock	2,608	2,674	2,736	2,773	2,831
Multilateral	2,187	2,275	2,356	2,414	2,485
IMF	88	83	73	92	99
Other	2,099	2,110	2,112	2,291	2,487
Bilateral	382	364	347	327	315
Paris Club	342	328	309	279	263
Non-Paris Club	40	36	38	48	52
Other (commercial)	39	35	32	32	31
Total scheduled debt service	87	98	96	95	103
Principal obligations due	61	67	66	66	74
Multilateral	48	45	43	43	50
IMF	21	10	8	8	11
Others	27	36	35	36	39
Bilateral	13	19	22	22	22
Paris Club	12	16	20	17	17
Non-Paris Club	1	3	2	5	5
Other	0	3	1	1	2
Interest obligations due	26	31	30	29	29
Multilateral	19	21	20	20	21
IMF	1	0	0	0	0
Others	18	20	20	20	20
Bilateral	7	11	10	9	8
Paris Club	6	7	8	8	6
Non-Paris Club	1	4	2	1	2
Other (commercial)	0	1	1	0	0
Memorandum items:					
Debt-service scheduled/ exports ratio (in percent)	17.5	22.0	19.9	20.2	23.5
Debt-service scheduled/government revenue (in percent)	26.6	30.0	29.3	29.1	31.4

Sources: Malawian authorities; and staff estimates.

Table 21. Malawi: Summary of the Tax System
(As of July 2004)

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates
1. Profit Taxes			
1.1 Taxation of business income <i>Taxation Act</i> (Cap. 41.01)			
	Taxable Persons	Exemptions	General Tax Rates
	Income tax is payable on the net income of all corporations, companies and other operating entities unless explicitly exempted.	Income from the following is exempt: (a) income of a public character from ecclesiastical, charitable and educational entities; (b) approved provident funds, building societies and friendly societies; (c) local authorities; (d) employees' saving schemes; (e) clubs, societies and bodies conducted for social welfare or civic improvement; (f) non-commercial income of statutory corporations; (g) land and agricultural banks; and (h) investments attributable to pension provident and annuity funds	Corporations 30 percent Foreign branches 35 percent Export enterprises in EPZs 0 percent Priority industries - for 10 years or - unlimited 0 percent Taxable income of ecclesiastical, charitable or educational institutions 25 percent
	Concept of income	Deductible Expenses	
	Income includes all receipts and accruals, in cash or otherwise, if these arise from a source within Malawi. The following are specifically included in the definition of income: (a) rental income;	Expenditure incurred for the purpose of trade or in the production of income is allowed as a deduction. The following are specifically allowed under the Act (a) bad and doubtful debts	Discretionary trusts and life assurance businesses 21 percent Dividend Withholding tax 10 percent Minimum tax A minimum tax is payable by companies with very low profitability or in a loss-making situation at following amounts:

Taxes	Tax Base	Exemptions, Allowances and Deductions	Annual gross income (MK)	Tax Rates
<p>(b) interest and royalties; (c) fees received in respect of services rendered; (d) premiums for the right to use or occupy land and buildings, plant and machinery or industrial property rights; (e) capital gains from the sale of property; (f) income from investments other than equities in life assurance businesses; (g) lump-sum payments under a contract of employment or service; (h) amounts received from timber sales if growing costs have been claimed as deductions; and (i) foreign exchange gains and losses which arise from a source in Malawi.</p>	<p>(b) contributions up to certain limits to approved pension and provident funds; (c) interest incurred in the production of income; (d) any deductible expenditure incurred in the 18 months before setting up a 'manufacturing' business; (e) premiums paid for the use of land, buildings or industrial property rights, plant and machinery; (f) non-capital expenditure on experiments and research; (g) contributions to scientific or educational institutions connected with the taxpayer's trade; (h) grants or scholarships for technical education; (i) donations to specific charities; (j) insurance premiums for insuring normal business risk; (k) legal fees incurred in production of income; and (l) contributions to the training funds set up under the TEVET Act</p>	<p>0 – 250,000 250,000 – 500,000 500,000 – 2,000,000 2,000,000 – 5,000,000 Over 5,000,000</p>	<p>5,000 25,000 50,000 100,000 200,000</p>	
<p>Benefits in kind</p>	<p>The value of benefits (e.g., housing, Motor vehicles, use of furniture) Provided by an employer, other than Government, to an employee with Taxable income in excess of MK 5,000 Results in a fringe benefit tax liability at The standard corporate tax rate on the employer and is not included in the employee's taxable income. (e) expenses incurred on exempt income;</p>	<p>Nondeductible expenses</p> <p>The following are specifically disallowed expenses: (a) domestic or private expenses; (b) losses or expenses recoverable under insurance policies; (c) any income tax or interest payable thereon; (d) income transferred to a reserve fund or capitalised;</p>		

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates
<p>The value of each benefit is generally calculated at cost though standard rates apply to certain specific items including the provisions of housing, a car and children's education.</p>		<p>(f) contributions to non-approved pension, sickness, accident or unemployment funds; (g) rent or cost of repairs to premises not occupied for the purpose of generating income; and (h) expenses in respect of which a subsidy is received</p>	
<p>Depreciation allowances</p>	<p>Annual allowances are available for qualifying assets on a declining balance basis at the following rates:</p>	<p>(i) buildings, farm improvements, hotels 5% (ii) industrial fencing 5% (iii) farm fencing 10% (vi) heavy machinery and installations 15% (v) light machinery 10% (vi) trucks and tractors 33.33% (vii) light commercial vehicles 25% (viii) motor vehicles 20%</p>	
<p>Other allowances</p>	<p>(a) <i>Initial allowance</i></p>	<p>Available on capital expenditure during the year of acquisition at the following rates:</p>	<p>(i) buildings, farm improvements, hotels 10% (ii) farm fencing 33.33% (iii) heavy machinery and installations 20% (iv) light machinery 20% (v) trucks and tractors 20%</p>

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates
<p>1.2 Taxation of individual income Taxation Act (Cap. 41:01)</p>	<p>Income tax is payable on all income which arises within Malawi</p>	<p>(vi) automobiles forming part of a commercial hire fleet 20%</p> <p>(b) <i>Investment allowance</i> An additional deduction of 40 percent of Expenditure on fixed assets including industrial buildings, plant and machinery, and farm improvements. A 20 percent deduction is also allowed for used industrial buildings, plant and machinery.</p> <p>(c) <i>Training allowance</i> An allowance may be granted of 150 percent of the costs of training employees.</p> <p>(d) <i>Transport allowance</i> An allowance may be granted of 125 percent of the international outward Transport costs for exports.</p> <p>(e) <i>Export promotion</i> Under the <i>Export Incentives Act</i>, a registered exporter will be entitled to an income tax allowance of 4 percent of taxable income derived from exports. Under the Investment Promotion Act, certain exporters will be entitled to a tax allowance of 12 percent of export revenues for non-traditional exports.</p>	<p>Annual income (MK) Rate (%)</p>

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates																
		<p>(o) up to MK 50,000 of any amount paid to an employee who has been made redundant, as well as an amount paid for voluntary termination.</p>																	
		<p>Deductible expenses In addition to deduction of expenses where applicable, individuals are entitled to the following deductions: than from employment or pension at the following amounts: fund up to a maximum of 8 percent of annual emoluments or MK 3,000 whichever is less; and (c) other expenses incurred to carry out a job.</p>																	
I.	professional subscription;																		
II.	contributions to an approved pension																		
			<p>Minimum tax A minimum tax is payable by individuals in receipt of income other</p>																
			<table border="1"> <thead> <tr> <th data-bbox="609 546 633 745">Annual income (MK)</th> <th data-bbox="609 451 633 493">Tax (MK)</th> </tr> </thead> <tbody> <tr> <td data-bbox="641 546 665 745">0 – 100,000</td> <td data-bbox="641 451 665 493">0</td> </tr> <tr> <td data-bbox="673 546 698 745">100,000 – 500,000</td> <td data-bbox="673 451 698 493">5,000</td> </tr> <tr> <td data-bbox="706 546 730 745">500,000 – 1,000,000</td> <td data-bbox="706 451 730 493">7,500</td> </tr> <tr> <td data-bbox="738 546 763 745">Over 1,000,000</td> <td data-bbox="738 451 763 493">10,000</td> </tr> </tbody> </table>	Annual income (MK)	Tax (MK)	0 – 100,000	0	100,000 – 500,000	5,000	500,000 – 1,000,000	7,500	Over 1,000,000	10,000						
Annual income (MK)	Tax (MK)																		
0 – 100,000	0																		
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Over 1,000,000	10,000																		
Payroll tax	A payroll tax has been introduced to fund training costs (TEVET levy). Claims for reimbursements of eligible Costs can be made against the TEVET Funds.	A reduced rate of 1 percent applies to the Government and statutory corporations.	2 percent payroll levy																
1.3 Taxation of Capital	An estate duty is levied on the estate in Malawi of every deceased person and in respect of foreign movable property in the case of those domiciled in Malawi.	No tax is levied on estate valued at MK 30,000 or less.	The rates of estate duty are as follows:																
	The duty is levied on market value after deduction of debts due at the date of death		<table border="1"> <thead> <tr> <th data-bbox="885 546 909 745">Value of estate (MK)</th> <th data-bbox="885 451 909 493">Rate (%)</th> </tr> </thead> <tbody> <tr> <td data-bbox="917 546 941 745">0 – 30,000</td> <td data-bbox="917 451 941 493">0</td> </tr> <tr> <td data-bbox="950 546 974 745">30,000 – 40,000</td> <td data-bbox="950 451 974 493">4</td> </tr> <tr> <td data-bbox="982 546 1006 745">40,000 – 80,000</td> <td data-bbox="982 451 1006 493">5</td> </tr> <tr> <td data-bbox="1015 546 1039 745">80,000 – 140,000</td> <td data-bbox="1015 451 1039 493">6</td> </tr> <tr> <td data-bbox="1047 546 1071 745">140,000 – 200,000</td> <td data-bbox="1047 451 1071 493">7</td> </tr> <tr> <td data-bbox="1079 546 1104 745">200,000 – 400,000</td> <td data-bbox="1079 451 1104 493">8</td> </tr> <tr> <td data-bbox="1112 546 1136 745">400,000 – 600,000</td> <td data-bbox="1112 451 1136 493">9</td> </tr> </tbody> </table>	Value of estate (MK)	Rate (%)	0 – 30,000	0	30,000 – 40,000	4	40,000 – 80,000	5	80,000 – 140,000	6	140,000 – 200,000	7	200,000 – 400,000	8	400,000 – 600,000	9
Value of estate (MK)	Rate (%)																		
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Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates
<p>2. Taxes on goods and Services 2.1 Surtax <i>Customs and Excise Act (Cap. 42:02)</i></p>	<p>Taxable Persons All businesses involved in importing, manufacturing or the provision of prescribed services must register as surtax payers if the turnover in the current or ensuing 12 months will exceed MK 2,000,000</p> <p>Other businesses may register at the discretion of the authorities.</p>	<p>Exemptions The main exemptions are:</p> <p>(a) maize and many other unprocessed foodstuffs; and (b) petroleum, diesel and paraffin;</p> <p>Many services are implicitly exempt (by the omission from the list of taxed services) including education, health and financial services.</p>	<p>Tax rates There are two statutory rates: (i) 17.5 percent applies to most taxed commodities, including electricity supplied to commercial premises; (ii) Zero rating applies to exports and other zero rated goods</p>
<p>Taxable transactions</p>	<p>Surtax applies on goods imported into or Manufactured in Malawi and on the Following prescribed services: (b) fertilizers and insecticides; (c) some goods for the use of government; (d) animal feed; (e) many working vehicles; (f) black tea; (g) broken rice and grain sorghum; (h) laundry soap; (i) mosquito nets; (j) fresh and processed milk; and (k) capital goods and machinery used for manufacturing goods</p>	<p>Zero-rated goods In addition to exports, the following goods are zero rated: (a) pharmaceuticals;</p>	
<p>I. professional services; II. computer services; III. services supplied by agents and brokers, excluding insurance and agricultural produce for export; (d) repairs of domestic appliances, vehicles and machinery (e) building, electrical and plumbing contractors; (f) commercial and domestic electricity supply and telecommunication services; (g) hairdressing and beauty treatment, dry cleaning and laundry services;</p>			

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates
I. secretarial agencies;	(h) landscaping and gardening services;		
1.	(j) advertising		
	(l) courier and security services;		
	(m) public entertainment;		
	(n) services provided by processing goods;		
	(o) accommodation and catering services		
	(p) satellite and cable television		
	(q) commercial transporters (excluding mimi buses		
2.2 Excise duties	Tax base		
<i>Customs and Excise Act (Cap. 42:02)</i>	Excise duty is levied on specific manufactured goods on the ex-factory value (on domestically manufactured goods) or c.i.f. (on imports).		
	Tax rate	Rate (%)	
	Excisable goods		
	Alcoholic beverages	65	
	Opague beer	15	
	Powers No. 1	45	
	Cigarettes	60	
	Other tobacco products	80	
	Petroleum	20	
	Diesel	30	
	Kerosene	10	
	Jet fuel	10	
	Other fuels	20	
	Paraffin	15	
	Petroleum jelly	20	
	Passenger cars;		
	- up to 1,000 cc	10	
	- 1,000 – 1,500 cc	20	
	- 1,500 – 3,000 cc	20	
	- above 3,000 cc	80	
	-exceeding 3999 cc	100	
	Four wheel drive	20	
	Double cabin pick-up	10	
	Trucks	5	

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates

2.3 Customs duties
Customs and Excise Act (Cap. 42:02)

Tax Base

Customs duties are levied on goods imported into Malawi calculated on the c.i.f. value. Malawi uses the Harmonized Tariff System.

Preferential duty rates

The tariff schedule allows for preferential tariff rates for imports originating in ACP States and COMESA countries. (SADC Preferential treatment effective only in 2006?)

General duty rates

All general customs duties are imposed in the form of ad valorem rates and can be summarized in the following broad categories:
(i) low rates of 5 and 10 percent;
(ii) an intermediate rate of 15 percent
(iii) a high rate of 30 percent

Duty drawback

There is duty drawback system in place
Many products are exempt from customs duty

Taxes	Tax Base	Exemptions, Allowances and Deductions	Tax Rates
<p>3.0 Other Taxes 3.1 Stamp duty <i>Stamp Duty Act (Cap. 43:01)</i></p>	<p>Stamp duty is levied on a number of Instruments, including agreements, bills of exchange, [bonds], leases and licenses, mortgages, and insurance policies</p>	<p>for specified goods manufactured or processed in Malawi allowing a drawback of duty paid on materials and components used (either all or specified).</p> <p>Exemptions The law provides for suspensions, rebates, remissions, and refunds of duty in certain circumstances, and general exemptions from duty including inter alia goods imported for the use of the President.</p>	<p>Rates of stamp duty vary depending on the nature of the instrument and the Value thereof.</p>
<p>3.2 Motor vehicle taxes</p>	<p>Registration fees are levied at specific rates according to type of vehicle and weight.</p>	<p>No stamp duty is payable on instruments executed by the government and on all forms of securities.</p>	<p>MK [400]</p>
<p>3.3 Road levy</p>	<p>The road levy is for road construction and maintenance carried out by the National Road Authority.</p>	<p></p>	<p>MK 3.75 per litre</p>