

THE INTERNATIONAL MONETARY FUND AND
THE INTERNATIONAL DEVELOPMENT ASSOCIATION

MALAWI

POVERTY REDUCTION STRATEGY PAPER
Joint Staff Assessment

Prepared by the Staffs of the International Monetary Fund
and the International Development Association

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I. OVERVIEW

1. The attached poverty reduction strategy paper (PRSP) of the Government of Malawi builds upon the interim poverty reduction strategy paper (I-PRSP) presented to the Boards of the International Monetary Fund (IMF) and International Development Association (IDA) in December 2000. Developed through a highly participatory process, the PRSP presents the available knowledge on poverty and details Malawi's multisectoral approach to reducing poverty.
2. **The staffs consider the Malawi PRSP a well-developed and sound strategy. The PRSP's main strengths are** (i) a highly participatory process involving government, civil society, the private sector, and donors; (ii) an appropriate macroeconomic framework and financing plan; (iii) a balanced approach to public policy designed to create the necessary conditions to generate growth, improve social sector outcomes, protect the vulnerable, and improve governance; (iv) a detailed action plan linked to strategic goals; and (v) an adequate institutional structure for monitoring the PRSP. The staffs believe that Malawi's PRSP provides a credible framework for reducing poverty in Malawi and is a sound basis for IDA and Fund concessional assistance.
3. **Successful implementation of the PRSP will, however, require further work in specific areas.** In particular, the link between the PRSP and the central government budget needs to be further strengthened. This will give policymakers greater guidance on how to translate the PRSP priorities into the budget, a task that will need to be undertaken as part of the annual budgetary preparations. In order for the PRSP's growth and poverty reduction objectives to be met, it is also essential that the structural reform agenda does not falter. During implementation of the PRSP, a clear capacity building program needs to be developed to redress the impact of HIV/AIDS, which is rapidly taking its toll on both the private and public sector. In addition, further refinement of the indicators and timeframe for attaining the PRSP targets requires immediate attention.

II. THE PARTICIPATORY PROCESS

4. **One of the strongest features of the Malawi PRSP is the participatory process, which has helped develop a relatively high degree of national ownership over the strategy.** The PRSP also builds on the groundwork for Malawi's poverty reduction policies as formulated in the "Vision 2020" document. The participatory nature of the PRSP process also resulted in the emergence of the Malawi Economic Justice Network (MEJN) as an umbrella organization for civil society groups. This greater involvement of civil society in the public sphere is an important step forward in Malawi's nascent democracy.
5. As described in Annex 6a of the PRSP document, the development of the PRSP involved three stages: mobilization, preparation, and validation. The "mobilization" phase consisted of forming three PRSP committees (ministerial, principal secretaries, and technical) and drafting an issues paper. During the official launch of the PRSP—attended by a wide variety of stakeholders—the rationale and objectives of the exercise were discussed. A media campaign was also launched to disseminate the purpose and road map of the PRSP.
6. The "preparation" phase of the PRSP development consisted of contributions from 19 thematic working groups and extensive "bottom-up" consultations. The working groups were composed of relevant government officials and representatives from the donor community, academics, nongovernmental organizations (NGOs), religious bodies, and the private sector. Several thematic contributions were based on existing sector strategies, such as the Policy and Investment Framework for education. Consultations were held in all 27 districts and included traditional authorities, village headmen, ward councilors, members of parliament, local politicians, local NGOs, and ordinary citizens. Annex 6b in the PRSP summarizes the common themes, such as the importance of law and order and access to credit, that emerged from the district consultations and were fed into the priority-setting at the national level.
7. The final PRSP drafting team comprised members of the government technical committee and civil society representatives. The drafting was carried out through an iterative process in which comments from all stakeholders were solicited at various stages and fed into subsequent drafts. This "validation" phase concluded with the official launch on April 24, 2002, attended by the President of Malawi, members of parliament, government officials, civil society groups and donors.
8. Civil society groups are expected to have an active role in the monitoring and evaluation of the PRSP targets. As described in the PRSP, a monitoring committee will be formed, and the technical committee will include academics, NGO representatives and the media, in addition to government officials and members of parliament.

III. POVERTY DIAGNOSIS

9. The PRSP benefited from Malawi's 1997/98 Integrated Household Survey, multiple demographic and health surveys, and qualitative studies on poverty. The new household survey, to be launched in late 2002, will provide a rich source of data to assess the dynamics

and trends in poverty. In general, there is relatively free access to the data, but capacity constraints have limited their extensive use in public policymaking.

10. **The PRSP presents a good summary of the profile of poverty, although it focuses primarily on quantitative aspects.** The 1997/98 national household survey was used to develop a comprehensive poverty profile disaggregated by gender, household demographics, and physical, financial, and human assets. However, there is little discussion of environmental degradation as a cause of poverty and only scant use is made of qualitative sources of information to provide a more in-depth analysis of both the profile and determinants of poverty.

11. **Further analysis is needed of the government's past policies and programs.** The PRSP candidly states that government policies have not yet made a significant dent in poverty. The main reasons presented are spells of macroeconomic mismanagement, vulnerability to exogenous shocks, growing population pressure, the high prevalence of HIV/AIDS, and weak institutional capacity. However, while the description of recent reforms is accurate, the analysis of their impact requires further work. The shortcomings of the assessment reinforce the importance of having a strong monitoring and evaluation system for the PRSP. Donor support for capacity building in the area of policy impact analysis can be channeled through the PRSP implementation unit.

IV. THE POVERTY REDUCTION STRATEGY

12. **The PRSP is a comprehensive and policy-focused framework designed to reduce poverty.** The overall approach is to promote growth and diversification of the economy, improve the delivery of social services, create safety nets, improve governance, and integrate policies on HIV/AIDS, gender, environment, and science and technology across the main sectors. The overall goals are translated into broad programs and activities that are costed and presented both in the main text and in Annex 2 of the PRSP. The staffs concur that the strategy presented in the PRSP is an appropriate framework for poverty reduction in Malawi.

A. Targets, Indicators, and Monitoring

13. **The PRSP targets are generally well specified, although they focus primarily on the medium term (2005-07).** The choice of indicators is appropriate for the goals and actions identified by the strategy and the proposed monitoring system would collect the relevant data. Annex 4 of the PRSP lists the main overall targets, as well as the key sector specific indicators. These targets relate primarily to 2005 as the PRSP will be revised after three years following annual reviews of the targets. However, the PRSP monitoring and evaluation process should establish the baseline for targets, where they do not exist, as well as targets for 2003-04, where they can be appropriately monitored.

14. **While most indicators are in line with the Millennium Development Goals (MDG), the PRSP's targets are less ambitious.** Further work is required to develop longer-term targets that relate directly to the 2015 goals. However, extrapolating the targets set in the PRSP for 2005 suggests that Malawi will fall short of meeting the 2015 MDG goals. The

staffs believe that these PRSP targets are more realistic and reflect Malawi's current socioeconomic conditions. For instance, the targeted reduction in income poverty from 65 percent in 1998 to 59 percent in 2005 is not at a rate that would halve poverty by 2015 but is realistic given medium term growth projections. Similarly, the 20 percent targeted reduction in the infant mortality rate by 2007 also falls short of the MDG's goal (reduction in infant mortality by two-thirds by 2015).

15. **The staffs endorse the new cross-sectoral monitoring and evaluation structure with civil society participation. The institutional arrangements are well designed.** At the political level, the cabinet committee on the economy will provide overall guidance to the monitoring and evaluation system. In addition, a committee of principal secretaries will provide leadership in the exercise, supported by a technical committee. Civil society groups, academics, district representatives, the media, and donor representatives will be part of the technical committee along with line ministry and parliamentary representatives. The challenge will be in implementing this coordinated effort across sectors and different stakeholders.

16. **The data collection activities are well sequenced.** The National Statistical Office will collect annual socioeconomic data using the Core Welfare Indicator Questionnaire (CWIQ), as well as conduct a full-fledged Integrated Household Survey and a Demographic and Health Survey (DHS) every five years. Moreover, an annual public expenditure review (PER) will also be carried out to strengthen the linkage between the PRSP and the budget. Community-based expenditure tracking and output-monitoring exercises, involving civil society organizations, will complement these efforts. In addition, the PRSP appropriately identifies specific institutions for monitoring of targets.

17. **However, significant capacity building is necessary to improve the quality of economic data, to allow for effective monitoring of progress toward achieving the PRSP targets.** Whereas the poverty-related data appear satisfactory, agricultural data have been found to be grossly inaccurate; in fact, flawed crop estimates thwarted a timely response to the recent food crisis. Moreover, national accounts and trade statistics, as well as fiscal data, are weak and hamper economic analyses.

B. Macroeconomic Framework

18. **The PRSP appropriately places emphasis on implementing sound macroeconomic policies in order to achieve the country's growth and poverty reduction goals.** High and volatile inflation has been imposing a considerable burden on the poor and high real interest rates have severely constrained private sector activity and depressed economic growth. The PRSP acknowledges that achieving macroeconomic stability is imperative to accelerating growth.

19. **The medium-term macroeconomic framework, developed in consultation with IMF staff in late 2001, is appropriate but will need to be updated to take into account recent developments, including the availability of foreign financing and the response to**

the food crisis (paragraph 27). The staffs believe that—based on recent performance and future prospects—the growth projections for 2003-05 in the PRSP are reasonable. The acceleration of the growth rate to above 5 percent by 2004 is achievable and necessary to attain the poverty reduction target of 59 percent by 2005. The macroeconomic analysis in the PRSP should be expanded to include monetary and external sector developments.

20. The PRSP recognizes that at the heart of Malawi's macroeconomic stabilization problems lie its past failures to control and limit the size of its fiscal deficits. The PRSP correctly points out that achieving fiscal restraint requires effective monitoring and control of public spending and the prevention of budgetary arrears. Continued political commitment will be necessary to ensure that the budget is not undermined by extrabudgetary spending.

21. **The emphasis on agriculture as the main source of pro-poor growth is sound, and the staffs fully endorse the PRSP's main focus on promoting small-scale private sector employment in agriculture to achieve both food security and enhance the income of the poor.** The strategy correctly places significant emphasis on strengthening access to inputs, improving the relevance of extension and research, promoting small-scale irrigation, improving access to markets, and reducing land degradation. This approach will be important to generating off-farm employment, which the poverty analysis highlights as a critical source of income for the rural poor. These actions gain further urgency in light of the present food crisis and the need to reduce the country's vulnerability to further crisis in the future.

22. **While identifying and analyzing certain sectors in terms of their growth potential is useful, the growth strategy has to focus on eliminating obstacles to growth on an economy-wide basis.** Furthermore, the strategy could have provided an analytical justification for identifying macroeconomic stability, access to credit, and the development of rural infrastructure and other "enabling infrastructure" as the key factors for creating an enabling environment for pro-poor growth. Issues such as government intervention in the economy, governance, investment in human resources, the legal framework, land policy, and security are discussed in the PRSP, but their links with the overall framework for generating growth could have been strengthened.

C. Public Expenditure Program and Financing

23. **The PRSP projects a realistic resource envelope for the period 2002-05.** It rightly points out that it is essential that the government stay within its financial envelope to avoid further crowding out of the private sector. This will require clear prioritization of expenditure in the spirit of the PRSP, imply cuts in nonessential spending, and entail measures to increase revenue.

24. **However, while the staffs are encouraged by the proposed re-prioritization of spending allocations reflecting strategic priorities, further prioritization and better linkage to the budget are needed to provide greater guidance to policy makers.** In particular, staffs are encouraged by the commitment to reduce statutory and statehood expenditures in favor of PRSP prioritized activities over time. However, as statutory and

statehood expenditures have repeatedly diverted funds from priority areas in the past, and since all other non-interest expenditures are defined as PRSP-related spending, the PRSP should have been explicit as to which pro-poor expenditures are protected should shocks require adjustments to the budget. This is a critical issue that should be addressed during implementation of the PRSP and articulated in the annual progress reports. Also, in moving forward it could become necessary to further prioritize spending based on outcomes achieved. The staffs are encouraged that the 2002/03 budget, which was approved by parliament in July 2002, explicitly identifies priority pro-poor expenditure that will be protected.

25. **The detailed program classification of the budget and several years of experience in developing medium-term estimates have facilitated the costing of the PRSP.** However, the PRSP should have presented the methodology and established the 2001/02 baseline, thus linking proposed pro-poor programs with budget programs. Translating the PRSP's commitments to certain strategic priorities will therefore need to be undertaken as part of the annual budgetary preparations. The staffs are encouraged that the Ministry of Finance will continue its prebudget consultations, which will give stakeholders an opportunity to be involved in incorporating PRSP priorities into the budget (see paragraph 27).

26. **Moreover, it will be critical that expenditure programs are subsequently monitored through a transparent expenditure-tracking system.** It is absolutely essential that this system become fully operational so that stakeholders can monitor budget implementation and thus, hold the government accountable in implementing the PRSP.

27. **The government reports in letters sent to the World Bank and the IMF (and attached as an addendum to the PRSP) the latest revisions to the macroeconomic framework and lays out its approach to adjusting the PRSP accordingly.** The 2002/03 budget law broadly reflects the priorities of the PRSP and includes higher expenditure, following upward revisions to external grants and loans from the time the PRSP was finalized. Moreover, after preparing the 2002/03 budget, government decided to provide imported maize to the population at a subsidized price, which the staffs believe is an appropriate response to address the lack of purchasing power of the poor that are not benefiting from food aid under humanitarian programs. The subsidy has increased the fiscal deficit by about 1 percent of GDP, which it expects to finance through donor support. These revisions of the macroeconomic framework, as shown in tables 1 and 2 of the authorities' letters, will provide the basis for consultations with stakeholders on updating the PRSP (specifically tables 5.2 and 5.4). Moreover, in their table 3, the authorities identify the priority pro-poor expenditure that were included in the budget. The staffs welcome the authorities' commitment to adjust the macroeconomic framework underlying the PRSP in the forthcoming consultations with stakeholders.

D. Governance

28. **The open discussion in the PRSP of the lack of good governance undermining development efforts is refreshing.** The section on "Good Governance, Political Will and

Mindset” is a very perceptive and frank assessment of obstacles to development and poverty alleviation. The "depoliticization of development" message and the discussion of the links between human rights, democracy, and development are well cast.

29. **The PRSP reaffirms the need to improve governance by addressing certain legislative weaknesses for prosecuting corruption cases and the need to strengthen the Anti-Corruption Bureau’s (ACB) investigative capacity.** It is, therefore, important that the government submit the draft amendments to the Corrupt Practices Act to parliament by end-2002. Efforts to build capacity by establishing a program to train magistrates in interpreting the revised act, and to increase staffing levels of the ACB substantially, particularly in the investigative branch, are also under way.

30. **The staffs fully share the concern that the losses incurred by parastatals are diverting resources meant for priority areas.** This highlights the need for improved public expenditure management and adherence to established guidelines on transparency, both of which will require strong political commitment. The ongoing efforts to increase the transparency in parastatal operations will make explicit the trade-off between financing parastatal activity and pro-poor expenditure. It is thus important that the parastatal reform agenda is accelerated as outlined in the PRSP, to prevent further bailouts of parastatals.

E. Structural, Sectoral and Cross-Cutting Policies

31. **The recent progress on the structural reform agenda needs to be maintained over the medium term in order for growth to rebound.** The poverty reduction strategy proposes solutions to key structural constraints inhibiting private sector development such as (i) improving the provision of basic infrastructure; (ii) promoting competition by reducing the domination of the formal sector by large oligopolies; and (iii) deepening financial services to enable widespread access to credit and saving mechanisms.

32. **Private sector development is considered critical for achieving the objectives of the PRSP, but the role of the private sector in specific areas is not clearly identified.** The activities to be undertaken by the private sector, civil society and the government (central and local) will need to be further clarified during PRSP implementation. The PRSP states that the private sector will be the engine of growth, but there is ambiguity regarding the government’s role as a facilitator, financier or implementing agency.

33. **The PRSP’s focus on the financial sector is narrow.** While the overall strategy behind supporting the growth of micro-finance appears sound, it is also critical that capacity-building support for microfinance institutions be included. Moreover, it will be important to make the financial sector more competitive and to explore alternative ways of strengthening linkages between the formal, semiformal, and informal financial sector. The PRSP could have linked the discussion on the operational and financial independence of the Reserve Bank of Malawi with the objective of achieving macroeconomic stability.

34. **The recommendation in the PRSP to improve disaster management is commendable, but, given the gravity of the present food crisis in Malawi, the strategy**

should have clearly spelled out improvements to the national food security policy. The PRSP addresses issues of increasing crop production and providing a safety net for the vulnerable, but lacks a coherent discussion on improving crop estimates and on managing the food grain reserve.

35. **Considerable efforts have been undertaken to develop an extensive safety net strategy.** The four components of the safety net program are conceptually sound and are aimed at different groups of vulnerable households, depending on the extent of their land and physical constraints. However, given the current food crisis, the costing of some aspects of the safety net strategy might have to be reworked. Furthermore, because targeted inputs schemes in Malawi have a mixed record of reaching the intended recipients, the challenge will be to develop mechanisms for targeting, preferably through self-selection. The implementation of the safety net strategy should be closely coordinated with the ongoing decentralization process.

36. **The PRSP provides some insights into the challenge of improving the quality of education.** The policies in the education sector are based on the existing sector strategy document, and the emphasis on improving the quality of basic education and teacher training while increasing access to higher education is an appropriate strategy. However, policies to ensure effective deployment and management of qualified staff, coupled with improvements in procurement of basic supplies (e.g., teaching materials) are not adequately discussed. It will also be necessary to clarify the respective roles of central and local government in the provision of education services during the ongoing decentralization process.

37. **The strategy for fighting HIV/AIDS in the PRSP has to be strengthened and there needs to be a recognition that the scale of the AIDS crisis requires that it be tackled head-on.** As the HIV/AIDS pandemic is undermining Malawi's development efforts, the PRSP should have been more explicit on the overarching strategy. The setting of strategic indicators and targets is essential in such a critical area. Furthermore, the importance of a multisectoral approach and the involvement of the civil society, including the private sector and NGOs, need to be highlighted. As noted in the PRSP, HIV/AIDS is not only a health issue; it also erodes growth, as morbidity and mortality of the working-age population increases.

38. **The health section of the PRSP appears to be more focused on the delivery of health services, with less emphasis placed on a multi-sectoral approach.** The importance of improving nutrition, especially of children, is recognized, but the role of maintaining a healthy environment is given relatively little attention despite references to providing latrines at schools and use of bed nets against malaria. Moreover, the staffs feel that there should be greater emphasis on service provision by local community groups and other proven delivery agents during implementation.

F. Risks to the strategy

39. **There are several risks that could derail the poverty reduction strategy laid out in the PRSP.** These include: a failure to create a stable macroeconomic environment; a crowding out in the central government's budget of pro-poor spending by nonessential spending; the impact of HIV/AIDS, and already weak economic databases that do not provide a good basis for sound policy decisions; weak governance and pressures on the budget in the run-up to the presidential elections, scheduled for 2004.

40. **The poverty reduction efforts could be derailed if the macroeconomic program is not steadfastly implemented.** A lack of spending discipline by government could result in the reemergence of excessive government borrowing, and therefore further increase already high real interest rates. Strict adherence to fiscal targets is thus critical to the success of this strategy. Also, exogenous shocks (droughts, floods, and commodity prices) could threaten macroeconomic stability.

41. **The PRSP does not clearly specify the pro-poor programs that will be protected should shocks require adjustments to the budget.** This shortcoming, together with capacity constraints and the weaknesses in public expenditure management, pose a major risk. To mitigate this risk, it is important that the authorities develop a specific timetable for the envisaged improvements in public expenditure management, including tracking budget execution.

42. **The generally weak implementation and absorption capacity is being exacerbated by the high rate of HIV/AIDS, which is rapidly taking its toll on both the public and private sector.** This will remain the main challenge to Malawi's development efforts in the foreseeable future. During implementation of the PRSP, it is therefore essential that a clear capacity-building program be developed in order for the PRSP's goals to be met. In addition, Malawi's economic databases are weak and significant capacity building is necessary to improve the quality of economic data and the consequent public policy decisions.

43. **The election cycle could also jeopardize implementation of the PRSP.** In the run-up to elections in 2004, budgetary pressures could reemerge, efforts to improve transparency and accountability could be hampered, and the structural reform program could easily be derailed.

G. Conclusions

44. **The strategy set out in the PRSP is an important step forward in Malawi's poverty reduction efforts.** The PRSP is derived from a highly consultative, country-owned process. The strategy is coherent, comprehensive, and refreshingly frank. The PRSP lays out strategic goals and specific actions to accomplish them. However, as the risk assessment has highlighted, the success of the PRSP process is contingent on sustaining political commitment, establishing macroeconomic stability, protecting pro-poor expenditures, and relieving capacity constraints within the public sector.

45. **The staffs of the World Bank and IMF consider that this PRSP provides a credible poverty reduction strategy and is a sound basis for IDA and Fund concessional assistance.** The staffs recommend that the Executive Directors of the World Bank and IMF reach the same conclusion.