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To: Members of the Executive Board

From: The Secretary

Subject: Malawi - Enhanced Structural Adjustment Facility - Policy Framework Paper 1989/90-1991/92

Attached for consideration by the Executive Directors is the policy framework paper under the enhanced structural adjustment facility for Malawi, which is tentatively scheduled for discussion on Wednesday, August 30, 1989.

Mr. Sharer (ext. 6515) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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Department Heads

INTERNATIONAL MONETARY FUND

MALAWI

Enhanced Structural Adjustment Facility

Policy Framework Paper 1989/90-1991/92 1/

Prepared by the Malawian authorities in collaboration
with the staffs of the Fund and the World Bank

August 2, 1989

I. Introduction

1. This paper, prepared by the Government of Malawi in collaboration with the staffs of the International Monetary Fund and the World Bank, updates the policy framework paper (PFP) 1988/89-1990/91 issued in June 1988, and extends its horizon to 1991/92. The updated PFP also reports on progress achieved to date in implementing the Government's structural adjustment program, and on recent economic and financial developments. In addition, the paper reviews the objectives, targets and measures, and the medium-term outlook for 1989/90-1991/92, together with the prospects for external assistance and financial requirements during that period. The basic objectives, targets, and policies, as well as the Government's overall development strategy, however, remain unchanged.

2. During 1964-1979, the Malawi economy recorded real per capita GDP growth of about 3 percent per annum, while maintaining financial and price stability and liberal economic policies. The economic situation began to weaken at the beginning of the 1980s and the Government implemented a broad-based structural adjustment effort during 1981-1986 supported by several successive arrangements with the Fund and the World Bank, comprehensive external debt reschedulings, and considerable external assistance. Substantial progress was made, but the situation deteriorated rapidly during 1985-1986, owing to a significant weakening in the terms of trade, continuing regional security problems--which disrupted normal transport routes and caused an influx of displaced persons--and rising public sector deficits. In February 1988, the authorities undertook a stabilization program supported by a 15-month stand-by arrangement from the Fund. In addition, the Government formulated a three-year structural adjustment program covering the period April 1988 to March 1991, supported by a three-year arrangement under the Enhanced Structural Adjustment Facility (ESAF), and the Bank's Industrial and Trade Policy Adjustment Credit (ITPAC). At the same time, the Government issued a Statement of Development Policies covering the period 1987-1996 (DEVPOL).

1/ Malawi's fiscal year runs from April 1 to March 31.

II. Program Implementation and Performance During 1988/89

3. The program's major objectives are to achieve and sustain a high rate of economic growth in the context of a viable medium-term balance of payments and price stability. The 1988/89 program aimed at raising the 1988 real growth rate to 1.5 percent and reducing inflation to 20 percent while building up external reserves and initiating or extending critical structural policy reforms. The program has promoted a greater role for the private sector and a return to Malawi's traditionally liberal economic policies.

4. Substantial progress was made during FY 1988/89 and all major performance criteria and structural benchmarks were met. An important achievement was the restoration of fiscal discipline resulting in a reduction of the overall deficit (excluding grants) to an estimated MK 256 million or 6.6 percent of GDP, substantially below the 8.1 percent specified in the program. This reflected a strong performance in almost all areas of tax revenue, and, in part, the introduction of improved budgetary management and monitoring measures. Total expenditures, relative to GDP, declined in 1988/89 by 1.6 percentage points to 27.0 percent. Total revenue increased sharply due to a broad-based rise in tax revenues related to improved GDP growth and the implementation of some revenue-generating features of the tax reform program; the latter included a shift in the payment of business income tax to a current-year income basis, a change from specific to ad valorem excise tax rates, and the merger of the import duty and levy tariff schedules. There were, however, some administrative delays in introducing a streamlined duty drawback and a surtax credit system. As a result of these developments and better-than-expected foreign grant receipts, the overall deficit (including grants) was MK 46 million in 1988/89. Therefore, with the somewhat higher-than-programmed nonbank financing, net domestic bank financing of the Government declined by the equivalent of about 2.6 percent of GDP.

5. For the parastatal sector, efforts were continued to improve financial performance and operational efficiency by implementing organizational reforms, streamlining and rationalizing employment levels, and setting realistic planning objectives. The financial targets established under the program, including that relating to the parastatals' recourse to bank credit, were observed, in part due to increases in tariffs and prices charged by the parastatals for goods and services. The Agricultural Development and Marketing Corporation (ADMARC) kept its overdraft position well below last year's level and the 1988/89 program target. ADMARC's asset divestiture program has proceeded smoothly, although with some delays due to legal difficulties and the need to maximize receipts. A few parastatals, however, are continuing to experience financial problems.

6. In trade policy, the liberalization of foreign exchange allocations for imports has proceeded well. The first and second stages of liberalization were implemented in February and August 1988, and as a

result, some 75 percent of imports 1/ of raw materials and spare parts and a significant proportion of intermediate goods are no longer subject to prior foreign exchange approval. Further, allocations were increased for many items not yet formally liberalized. This liberalization of imports resulted in improved private sector confidence and increased manufacturing output.

7. Monetary developments during 1988/89 have differed considerably from the program. Broad money increased by 27 percent, compared with 4 percent envisaged, associated chiefly with a higher-than-projected level of net foreign assets. However, net bank claims on both the Government and parastatals were kept well within the program ceilings. Credit to the private sector exhibited a greater-than-usual seasonal increase owing to high tobacco prices and the effect of import liberalization. Nevertheless, the overall credit ceilings were observed. Bank interest rates were completely liberalized in April 1988, although still influenced by collaboration between the Reserve Bank and commercial banks. These interest rates remained negative in real terms.

8. As a result of cautious demand management policies and better-than-projected terms of trade and capital inflows, the balance of payments outturn in 1988 was much stronger than envisaged. Export receipts, helped by a 9.5 percent improvement in (SDR) export prices, were 8.5 percent higher than projected despite a larger-than-forecasted decline in volume. Import volume rose by 28 percent, compared with the projected 5 percent. The current account deficit (excluding official grants), at SDR 89 million (8.3 percent of GDP), exceeded the program projection of SDR 75 million (7.3 percent of GDP), while the overall balance of payments surplus was sharply higher at SDR 62 million, compared with SDR 6 million envisaged. The capital account strength reflected a significantly higher level of grants and concessional loans than envisaged. The larger external surplus together with greater-than-anticipated debt relief were reflected in a higher-than-programmed increase in external reserves, which rose to the equivalent of 4.6 months of non-maize imports at end-1988, compared with 2.6 months envisaged and the end-1987 equivalent of 1.8 months. Following the conclusion of rescheduling agreements with Paris Club, London Club and Commonwealth Development Corporation (CDC) creditors, debt service was reduced in 1988 from the scheduled 44 percent of exports of goods and nonfactor services, to 30 percent. In accordance with the agreement, during 1988/89, CDC converted the equivalent of SDR 6.4 million of the consolidated principal to equity investments in export-oriented industries.

9. As a result of better weather conditions, increased import availability and improved private sector confidence, growth in real GDP (at factor cost) reached 3.6 percent in 1988 (against 1.5 percent originally

1/ Excluding petroleum, which was never subject to prior foreign exchange approval.

projected). Better weather conditions spurred higher agricultural production while the liberalization of imports permitted greater availability of inputs for the manufacturing sector which increased capacity utilization. The Government announced increased agricultural producer prices to be paid during the 1989 season, with the largest increases going to tobacco and maize. At the same time fertilizer prices were increased by an average of 13 percent. Despite a restrained fiscal policy, the average rate of inflation in 1988 was about 30 percent, which was much higher than the 20 percent expected. The high level of inflation reflected a substantially higher-than-programmed rate of monetary expansion; demand pressures on scarce resources, particularly on transport and other resources related to the substantial influx of displaced persons from Mozambique; the passthrough of the January 1988 depreciation; and also private sector hedging arising from uncertainties regarding further exchange rate changes and the import liberalization. To alleviate the impact on the lowest paid, the Government raised the rural minimum wage by 126 percent, the first increase since 1986.

III. Medium-Term Objectives, Strategy, and Policies

10. The broad objectives and strategy for the 1989/90-1991/92 period remain fundamentally unchanged from the first-year PFP. The principal objectives are to raise the rate of economic growth to sustainable positive per capita levels in the context of a viable medium-term balance of payments position and relative price stability. To achieve these objectives, the Government continues to be committed to a strategy of structural reform and macroeconomic stabilization and the restoration of an economy based on liberal policies with emphasis on private sector production. Policy will continue to focus on two elements of adjustment and development. First, policies to ensure a balanced macroeconomic environment on both the domestic and external fronts will be pursued, including constraint of the fiscal deficit following the sharp reductions of recent years, tight monetary and credit policies, and liberalization of trade. Second, policies to reduce structural impediments to growth will be implemented in each of the main sectors of the economy. Table 3 presents, in matrix form, a summary of the Government's structural adjustment program, and the timetable for its implementation.

11. Rapid reduction in the inflation rate is a major priority for the authorities to ensure a more stable business environment and maintain external competitiveness. With firm fiscal discipline, progress with structural reform (including improvements in the availability of transport equipment) and full and speedy implementation of import liberalization, much lower rates of inflation are expected. The new monetary instruments now available to the authorities will also assist in financial management.

12. On the basis of performance during 1988/89 and of external financing prospects in the medium term, several assumptions and macroeconomic targets in the original PFP have been revised. The first PFP

presented two medium-term scenarios, building on an identical projection for policy measures and targets for 1988/89. The first scenario was predicated on a cautious projection of external resources, while the second scenario envisaged a higher rate of economic growth on the basis of the availability of higher concessional grants and loans and accelerated structural policy implementation. With the Consultative Group meeting in June 1988 helping to clarify capital inflows, and building on the review of economic performance during 1988/89, a single scenario is being adopted for the second-year PFP, with the medium-term targets relating to the growth path and external financing falling between those contained in the two scenarios of last year's PFP. The fiscal targets before grants for 1990/91 and 1991/92 have also been adjusted to a position between those of the two scenarios in the original PFP.

13. The program's external projections are based on a cautious assessment of external financing and are consistent with medium-term balance of payments viability. Recent estimates indicate that the total financing requirement would average SDR 164 million per year for 1989-92, compared with the average of SDR 151 million for 1989-91 projected in the previous PFP's first scenario and the SDR 212 million in the second scenario. Increased external inflows may support a higher level of imports than assumed in the first scenario for 1989-92. Consistent with the program's growth objectives, non-maize import volume growth is now projected at 9.4 percent in 1989 and 6.2 percent in 1990, after 28 percent in 1988, as the impact of import liberalization gradually winds down. Thereafter, volume growth of about 4 percent per annum is anticipated. Following a decline of 5 percent during 1984-88, export volumes are expected to improve by about 6 percent annually in 1989-90 and about 4 percent per annum thereafter. Consequently, the current account deficit (excluding official transfers) as a percentage of GDP is now expected to average 8.4 percent during 1989-92, compared with an average for 1989-91 of 7.0 percent assumed in the original first scenario and 11.2 percent in the second scenario. The current account projections are consistent with the envisaged rapid progress in import liberalization and the maintenance of adequate external reserves. The debt service profile during 1989-92 is also expected to improve faster than earlier assumed, largely reflecting the increased share of grants and concessional inflows in external financing. Given the faster-than-programmed accumulation of external reserves during 1988/89, the external reserves target over 1989-92 will be to maintain the level at the annual equivalent of about 4 months of non-maize imports.

14. Consistent with the revised medium-term scenario, the real GDP growth targets have also been revised. The new targets significantly exceed those set out in the first scenario of last year's PFP but fall short of the targets of the second scenario. Real GDP is now projected to increase by 3.7 percent in 1989, reflecting an improved agricultural sector performance and increased output in manufacturing, utilities, and construction, as capacity utilization returns to the early 1980s levels under the import liberalization program. Growth performance is expected to improve to 4.1 percent for 1990, as agriculture continues to recover

from its poor performance over the past few years. Government policy reforms and initiatives are expected to begin to yield large productivity gains in the smallholder and estate sectors, and private sector investment is expected to lead to new growth in manufacturing. Finally, a growth rate of about 4.5 percent is projected for 1991-92 by which time macroeconomic policy reforms and sectoral investments will feed into sustained economic expansion and diversification. During this period, growth is expected to be spurred by a reduction in Malawi's external transport costs as a result of completion of the Northern Corridor Transport Project. The inflation rate, although considerably higher in 1988 than projected, is expected to decline in 1989 to about 15 percent, compared with 10 percent originally envisaged, and subsequently fall further to 12.5 percent in 1990, 7.5 percent in 1991, and 5 percent in 1992.

IV. Macroeconomic and Sectoral Policies

a. Macroeconomic policies

External sector policies

15. A flexible exchange rate policy has in recent years underpinned the Government's policies to promote an efficient allocation of foreign exchange, stimulate export growth and diversification, and efficient import substitution. The Government is committed to the continuation of a flexible exchange rate policy to maintain external competitiveness and to support the process of import liberalization.

16. The Government intends to broaden the process of import liberalization, building on the considerable progress made during 1988/89. The liberalization process will continue to focus on the removal of the requirement for prior approval of foreign exchange for current payments, with administrative controls limited to establishment of a small negative list of selected items for which the prior approval requirement will be maintained. The third stage of the import liberalization is being introduced in August 1989 and involves the removal of the prior-approval requirement for the balance of raw materials, spare parts, intermediate goods, and some consumer goods remaining subject to this control. A complete liberalization of the approval system is now planned to be accomplished by end-December 1989. While the liberalization has so far been targeted to end-users of the liberalized imports, future liberalization will broaden the coverage to include distributors of imports. The Government intends, during 1989/90, to review the existing tariff structure for imports with a view to implementation of an additional tariff reform program during 1990/91 (see paragraph 24 below).

17. The Government is committed to pursuing other measures to enhance Malawi's export competitiveness and to develop new nontraditional exports. To this end, the Government has passed legislation to permit

more favorable tax arrangements and will streamline the duty-drawback scheme for exporters.

18. The rescheduling agreements with Paris Club and CDC creditors covered periods to end-May 1989. The Government has not requested further rescheduling from these creditors at this time. Nevertheless, Malawi remains a poor and heavily indebted country, and in case of need the Government will wish to request the benefit of any future initiatives in the area of debt relief. The external debt rescheduling obtained in 1988 significantly eased the country's projected external debt service burden, reducing it to about 26 percent of exports of goods and nonfactor services by 1992. To improve the debt profile further over the medium term, the Government plans to rely almost entirely on external grants and concessional external borrowing to finance the current account deficits.

Public finances

19. The program continues to recognize the importance of maintaining strict fiscal discipline as a means of ensuring the availability of an adequate level of resources for the rest of the economy. Therefore, the deficit is to be reduced in 1989/90 to 6.3 percent of GDP, from 6.6 percent in 1988/89. The appropriate level of the fiscal deficit and government expenditures will continue to be reviewed during the program period taking into account the availability of foreign concessional inflows and the progress towards attaining the program's overall domestic and external objectives. The targets for the fiscal deficit (before grants) for 1990/91 and 1991/92 are somewhat above those of the first scenario of the first PFP; while they continue to support the anti-inflationary objective of the program, they will permit an expanded level of core expenditures in high priority sectors. Accordingly, while the targets for the fiscal deficit after grants included in the first scenario have been increased somewhat, the original targets for domestic bank financing of the Government over this period have been broadly maintained. Budgetary targets may have to be reviewed in light of the prospective requirements for budgetary onlending of external investment loans to the Electricity Supply Commission (ESCOM) envisaged for 1991-95, which could amount to 1 percent of government expenditure by 1991/92.

20. Achievement of the above fiscal targets will require that total expenditures of the Government be strictly contained. To this end, the overall ratio of expenditure to GDP will fall from an estimated 27.0 percent in 1988/89 to some 26 percent by 1991/92. Given programmed GDP growth, this implies an annual increase in expenditures in real terms of around 3 percent. The Government will continue to pursue a restrained wage and salary policy. Following the strict freeze on public sector wage rates in 1988/89, the program includes an increase in average wage rates of 17 percent during 1989/90. However, in order to redress the substantial disparity between public and private sector wage rates that has emerged in recent years, as well as the severe wage

compression within the civil service, the Government intends to raise real public sector wages in 1990/91 and 1991/92, subject to the program's overall fiscal targets. Net civil service employment will, after a freeze in 1988/89, be allowed to grow by at most 2 percent in each of the following three years, and the program to reduce the number of nonestablished positions will be continued.

21. Most direct costs associated with the significant influx of displaced persons in recent years are being borne through direct donor assistance. However, the Government will review the recent World Bank-UNDP analysis of the impact of the displaced persons on public expenditure and will seek additional donor grant assistance for any further outlays required. In addition, the Government is approaching donors for emergency relief to respond to the recent natural disasters.

22. To maximize the benefits of budget outlays in the tight fiscal environment, the Government has reviewed findings and expenditure options outlined in the Public Expenditure Review recently completed by the World Bank, and has adopted an action program to strengthen the budgetary allocation process. Specific measures to be implemented in 1989/90-1990/91 include development of proposals that facilitate a shift in donor financing toward recurrent development expenditures in key sectors, reactivation of the forward budget, and improvement of the consistency of sectoral budget planning with the underlying medium-term program. The Institutional Development Project is intended to finance the development of the institutional expertise and infrastructure necessary to implement these goals.

23. The Government recognizes the disincentives engendered by high levels of taxation; thus the burden of fiscal adjustment was placed primarily on expenditures. For 1988/89, revenues (excluding grants) amounted to 20.4 percent of GDP, and the objective during the program will be to maintain a revenue to GDP ratio of at least 19 percent. These revenue projections allow for the impact of the reform of the tax system aimed at improving incentives in the productive sector and enhancing the elasticity of the tax system. In this regard, following technical assistance from the World Bank, the Government began the process of a broadly revenue neutral tax reform in 1987/88 with three major objectives: (i) broadening the effective tax base; (ii) improving allocative efficiency while achieving greater equity; and (iii) simplifying and strengthening tax administration. In this latter regard, certain administrative improvements, including measures to improve the identification and monitoring of taxpayers, begun in 1987/88, will continue to be put in place during 1989/90.

24. Measures undertaken during 1988/89 to broaden the effective tax base included converting certain excise taxes from a specific to an ad valorem basis, expanding the surtax coverage to repackaging, merging the import duty and levy, and shifting the luxury tax from the import duty to the surtax schedule. With regard to the second objective of improving the allocative efficiency of the tax system, the Government

introduced a four-year phase-in of a current payment system for business income tax and increased in 1988/89 the Investment Allowance for certain assets placed in service after March 31, 1988 to 40 percent. The Government will review investment incentives with a view to the full merger of the Initial and Investment Allowance, initially foreseen for 1988/89, by 1990/91, combined with appropriate changes to the structure of depreciation rules for tax purposes. Additional actions to be taken in 1989/90 include: (i) the introduction of a tax allowance for export earnings and a more effective duty drawback system to help improve Malawian exporters' competitiveness in international markets; and (ii) the implementation of a surtax credit system to exempt payment of surtax on inputs, including spare parts and capital goods. During 1989/90, the Government will also review the scope for a reduction in overall levels of direct and indirect taxation, including income tax, surtax, and import duty rates, for implementation during 1990/91. To achieve the third objective of strengthening and simplifying tax administration the Government will continue its strategy of improving the income tax administration and the mechanism for collection of tax arrears. In addition, to facilitate these and subsequent reforms to the tax administration, the Government is also seeking to develop a Tax Analysis Unit within the Ministry of Finance during 1990/91.

25. In 1989/90 the overall deficit (before grants) is targeted to increase somewhat to MK 291 million, equivalent to 6.3 percent of GDP. Revenues are projected to fall slightly, as a percent of GDP, to 19.3 percent, while total expenditure will be reduced by 1.3 percentage points of GDP to 25.7 percent, or MK 1,180 million. To improve the balance between recurrent and capital expenditures, and to emphasize expenditures considered critical for promoting development, expenditure on the revenue account will rise by 18.1 percent to reach MK 868 million, representing an increase of some 4 percent in real terms and capital development is targeted to increase by 6.8 percent to MK 297 million. On the financing side, net foreign financing will rise, compared with original projections, reflecting higher levels of concessional inflows from structural adjustment lending operations. The budget provides for the full amount of the estimated debt service falling due, and the kwacha counterpart of government debt service payments subject to rescheduling will continue to be held in a blocked account at the Reserve Bank. Domestic financing will continue to be negative and net payments to the banking system are expected to be MK 212 million, or 4.6 percent of GDP.

26. Public investment will continue to be guided by the rolling three-year Public Sector Investment Program (PSIP), which includes all central government development projects and any investments of public enterprises involving government finance. Priorities and programs for development spending have been reviewed with the World Bank in the context of the 1989/90-1991/92 PSIP. In line with the expenditure priorities outlined in DEVPOL sectoral allocations for education and

health are projected to increase significantly, power and water increase moderately, agriculture and forestry remain relatively unchanged, and transport and buildings decline. To enhance the effectiveness of the PSIP and its coordination with the remainder of the budgetary process, the formal guidelines for public enterprises and ministries for submitting investment projects for approval have been improved for the preparation of the 1990/91-1992/93 PSIP. Infrastructural investments with low economic return will be avoided, and individual investment projects will be evaluated in terms of their contribution to economic growth and income distribution. The Government will improve the coordination between the development and recurrent budgets by updating recurrent cost coefficients and expanding the classification system of the PSIP in 1989/90. The expansion of the PSIP will also allow a better understanding of the links between the macro-economy and the development budget. The need for maintaining and strengthening recurrent expenditures in priority sectors will be taken into account when determining the size of the development budget, and likewise, the implications of projects for recurrent expenditures, including future debt service obligations, will be considered when making judgments on the appropriateness of the development budget.

27. For 1989/90, the Government's development budget consists primarily of on-going projects in the PSIP, with the exception of certain high priority infrastructure projects. In its annual review of the PSIP the Government will ensure its consistency with resource availability, assess its recurrent cost implications, and take into account the need to attain balance of payments viability; donor financing of priority expenditures will continue to be encouraged.

Monetary and credit policies

28. Monetary and credit policies will continue to be geared towards the goals of reducing the rate of inflation, encouraging domestic financial savings, and safeguarding external sector objectives. Interest rates, which were decontrolled during 1988, have since remained stable in nominal terms. Although the persistence of high inflation during 1988/89 led to continuing negative real interest rates, the Government believes that the rate of inflation will decelerate sharply and that there will be significant movement towards positive real interest rates. To ensure that lending rates are positive in real terms, effective August 1, 1989 the preferential lending rate for agriculture is being discontinued and the minimum lending rate is being raised by 3 percentage points to 18 percent. The Government has also been reviewing monetary policy instruments, and has initiated reforms with a view to increasing the scope for more market-related monetary and credit policies. In this regard, a revised Reserve Bank of Malawi Act was approved by Parliament in April 1989, and the Banking Act is being revised, with a view to being presented to Parliament in October 1989. The revision of the Reserve Bank of Malawi Act enables the authorities

to engage fully in traditional central banking functions, including open market operations, implementation of reserve requirements, enhanced supervision, and last resort lending to the banking system. A reserve requirement for commercial banks of 10 percent of average deposits was introduced in June 1989 to facilitate monetary management and lead to reduced reliance on credit ceilings. The revised Banking Act will include a wider definition of banking activity to increase competition and avoid distortions in the financial system. The Post Office Savings Bank (POSB) will be restructured to perform the normal functions of a commercial bank, thereby enhancing competition. Phased implementation of the above reforms should enable the monetary authorities to move eventually to a market-based system where monetary policy is conducted through controlling reserve money in an environment of flexible interest rates.

29. For the medium term, policy will focus on ensuring adequate availability of credit to the productive sectors while sharply curtailing monetary expansion to help reduce the rate of inflation. During 1989/90, net bank credit to the Government is programmed to decline further by MK 212 million, equivalent to 4.6 percent of GDP, reflecting higher projected levels of external financing of the deficit and continued improvement in the overall government financial position. Net credit to the parastatal sector is projected to rise by MK 37 million, while credit to the private sector is projected to increase by 36 percent reflecting the upturn in activity expected in that sector. Altogether, the net domestic assets of the banking system are targeted to fall by 15 percent. After allowing for the improvement in the net foreign assets position of the banking system, broad money is projected to remain essentially unchanged, which is consistent with the continued decline in excess liquidity in the banking system and in the private sector.

b. Sectoral policies

Agriculture

30. The development of the agriculture sector is of major importance to the Government. The primary objectives will be to: (i) ensure food security and improve rural incomes through increased smallholder production of food and cash crops, with emphasis on food deficit and female households; (ii) increase agricultural and agro-industrial exports through expansion and diversification; and (iii) stem the deterioration of natural resources through improved tobacco curing methods, increased fuelwood planting, and improved soil conservation practices, in conjunction with other environmental policies reviewed in paragraph 53 below. As reviewed during the Government's 1988 Agricultural Symposium, the Government is expanding its agricultural strategy to address more effectively the persistent problems of food security and malnutrition. The timing and scope of specific agricultural policy reforms will be agreed

under an Agriculture Sector Adjustment Credit (ASAC) funded by the World Bank and other donors.

31. In the smallholder sector, increases in food production will come through increased fertilizer use and adoption of higher-yielding maize varieties, to counter land scarcity and the narrow cropping base. To increase fertilizer use, the Government will: (i) expand and improve the seasonal credit system under the Smallholder Agricultural Credit Project; (ii) ensure adequate working capital financing for the Smallholder Fertilizer Revolving Fund; and (iii) review existing fertilizer procurement and distribution systems. To spur the development and adoption of higher-yielding maize varieties, the Government will: (i) continue research in appropriate technologies, with special emphasis on the development of a suitable flint maize variety; (ii) develop an implementation program for national research priorities based on the research master plan completed in 1988/89; (iii) improve research-extension linkages, which will include the operation of adaptive research teams in the field; and (iv) continue to develop and expand the extension system. In addition, the Government will also study the potential to raise smallholder production through irrigation and will review the scope for economically viable irrigation investments.

32. Government is targeting much of this increased production from farmers with plots less than one hectare who comprise more than one-half of the rural population and face seasonal food deficits and low nutrition levels. Some of these farmers have sufficient land to feed themselves and generate some surplus cash crops for sale, if given access to improved technologies, while many have land barely sufficient to meet their own food requirements. Therefore, Government will develop new programs to ensure that the smaller farmers have sufficient resources to procure fertilizer and other inputs. In addition, the Government will: (i) conduct pilot projects to test alternative mechanisms for providing credit and inputs to small farmers, including food/fertilizer-for-work schemes and targeted fertilizer subsidies; (ii) continue to expand the supply of fertilizer in small packets; (iii) relax crop restrictions and develop appropriate institutional arrangements for smallholder production of high-value crops; and (iv) identify additional measures during the program period to support the development of off-farm, rural income-generating activities.

33. In the estate sector, the Government's strategy will focus on productivity gains and more efficient resource use. To raise productivity, the Government will: (i) establish an estate extension service in 1989 to disseminate information on improved technology, which will be funded initially through external donor support and then become self-supporting through estate contributions; and (ii) expand estate access to medium-term credit. To improve the efficiency of resource use and address the problem of under-utilization of estate land, the Government will: (i) increase and improve collection of lease-rents; (ii) more

strictly enforce land-use covenants in leases; and (iii) enforce restrictions on estate expansion in areas of high land pressure, except in the case of experimental estates aimed at benefiting smallholders.

34. In line with its objective of encouraging private sector activity, the Government will continue the reform of the smallholder agricultural marketing system, including a review of the regulatory framework for private trading in 1989/90. With regard to pricing policies, the Government recognizes the importance of maintaining adequate smallholder producer incentives for both domestic and export crops. In order to encourage diversification and an appropriate crop mix, producer output and input prices will continue to be reviewed annually and adjusted if necessary, taking into account costs of production and marketing, border prices, and the level of domestic supply. For the medium term, the objective will be to move toward import or export parity prices while taking into account the other aforementioned factors. The World Bank and the Fund will be consulted on the proposed consumer and producer prices before they are announced.

35. With regard to input use and pricing, the Government's agriculture strategy largely depends on a significant increase in smallholder fertilizer consumption. However, since many smallholders lack adequate access to credit and alternative sources of income to pay the full cost of the fertilizer input, the Government recognizes that it will be necessary to continue to maintain the small budgetary subsidy on fertilizer in the short term to ensure wider uptake of this critical input. In 1989/90, this amount is expected to be no greater than 1 percent of total Government expenditure, or MK 12 million. While the Government is committed to the removal of the fertilizer subsidy in the medium term with the adoption of high yielding maize varieties, expansion of rural credit, and improved external transport, in the short term it will conduct a thorough review of fertilizer requirements, marketing, prices, and financing in connection with ASAC. This will include reforms to limit the leakage of subsidized fertilizer into the estate sector and better target the fertilizer subsidy to food deficit households.

Industry and energy

36. Industrial sector policy has remained relatively liberal since independence and a recent World Bank report indicated a low level of sectoral distortion and inefficiency. The Government's development strategy for the industrial sector will continue to emphasize private sector activity and the maintenance of a market-determined pricing system. The Government enacted a number of reforms in 1988, including reduction in the scope of industrial licensing, reduction of price controls to only four basic commodities, reduction in the scope of import and export licensing, and the introduction of import liberalization. These factors should ensure a more favorable environment for export growth and efficient import substitution.

37. As future industrial growth will be based largely on growth in domestic incomes, and because the domestic market is small, policies to ensure adequate opportunities for small- and medium-scale enterprises will be pursued. The Government aims to increase the effectiveness of institutions working with the small-scale sector, to expand the pool of funds available for lending, and to expand the guarantee scheme managed by the Small Enterprise Development Organization of Malawi (SEDOM). Government intends to complete a study of the institutional and regulatory framework for small enterprise development in 1989/90.

38. In the energy sector, the Government supports policies that protect the environment and are cost effective (forestry and environmental issues are reviewed below in Section VI). The Government recognizes the necessity of encouraging the most efficient use of power and petroleum products. After reviewing the results of the 1988 Least Cost Power Development Study, the Government has developed an appropriate expansion program for Malawi's electricity-generating capacity to meet the economy's future needs. ESCOM will begin expansion of the hydroelectric capacity at Tedzani in 1989/90, with complementary investments in distribution, transmission, and institutional strengthening, which will result in significant public sector investment expenditures beginning in 1991/92. The World Bank will be annually consulted on ESCOM's proposed investment program. In the area of pricing, Government will continue to follow the policy of adjusting electricity tariffs in a timely manner on the basis of long-run marginal costs, and allowing domestic prices of petroleum products to reflect a full pass-through of import and domestic distribution costs and taxes, consistent with budgetary requirements.

Infrastructure

39. A high priority of the Government is to alleviate the heavy burden that has been placed on the economy by the disruption of traditional routes through Mozambique. The improvement of the Northern Corridor transport route to Dar es Salaam, including handling facilities in Tanzania, lake terminals in Malawi, and upgrading of roads is expected to reduce the c.i.f. margin from 40 percent in 1989 to about 35 percent by 1993, leading to annual savings equivalent to about 1 percent of GDP. The Malawian authorities have also been working closely with the Mozambican authorities to reopen the traditional rail line to the port of Nacala, although progress is being hampered by continued uncertainty regarding the security situation. If the Nacala line were fully reopened savings up to SDR 25 million a year could be realized. The Government will re-evaluate on a yearly basis the progress on this project relative to its costs.

40. To help attenuate excess demand pressures and supply constraints in both the international and domestic haulage sectors, the Government intends to implement the following measures during 1989/90: (i) review

the scope for expansion of the Malawian-owned domestic and international road-haulage sectors; (ii) review the requirement providing for international truckers to off-load onto domestic vehicles, which was intended to protect Malawi Railways and the domestic trucking industry; (iii) continue institutional strengthening of Malawi Railways; and (iv) reduce duties on imported trucks. In the area of pricing, the Government will ensure maintenance of market-determined transport rates.

41. As regards the remainder of the infrastructure network, the Government recognizes the importance of maintenance and rehabilitation. It will continue its program of road maintenance covering all existing roads, upgrade the road network only where justified by projected traffic, and strengthen the maintenance capability for public buildings. Urban water supply will be expanded where financially viable. Borehole and gravity-fed water supplies will be expanded in line with national water access objectives and rehabilitation will be initiated. With regard to water tariffs, the Government will ensure that the District Water Supply Fund's tariffs are increased annually to reflect domestic inflation rates and the Water Boards' rates are increased annually to maintain financial viability. The Government's housing policy will be to widen the role of the private sector and local authorities in urban housing construction, through (i) expansion of the housing finance market; (ii) liberalization of New Building Society policies; (iii) progressive withdrawal from the provision of subsidized civil service housing; and (iv) transfer of management of traditional housing areas to local government. In the area of urban services, the Government will strengthen local government management capability and review measures to improve local government finances.

Public enterprise sector

42. The broad aim of the Government is to improve the financial control and performance of the parastatal sector to minimize budgetary transfers to subvented parastatals and ensure adequate financial return to commercial parastatals. Following a comprehensive review, in collaboration with the World Bank, the Government began a program of reorganization in 1987/88. The Government began the regularization of the cross debts and arrears between the Government and public enterprises in 1988/89, including Air Malawi, Malawi Railways, MDC, and ADMARC, and intends to ensure that future financial flows will be conducted in a more transparent and orderly fashion. Specific financial provisions to cover these flows consistent with the program's objectives have been incorporated in the 1989/90 budget. The Government will continue the institutional strengthening of the Department of Statutory Bodies (DSB) to enhance its capacity to monitor parastatals. DSB will continue to develop and implement evaluation criteria for reviewing parastatal investment plans and a performance monitoring system, which will enhance performance accountability while increasing autonomy in the operational management of commercially oriented parastatals. In

aggregate, the 12 major commercial parastatals are expected to show a profit of MK 32.2 million in 1989/90, compared with MK 24.4 million in 1988/89 and only MK 3.9 million in 1987/88.

43. Following ADMARC's large losses in 1985/86 and 1986/87, the Government embarked on broad structural reform of the enterprise in 1987. While ADMARC had been involved in a broad range of commercial and developmental functions, including smallholder marketing, agricultural development, and non-marketing investments, the reform program withdrew ADMARC from certain activities in favor of the private sector, as follows. First, ADMARC's dominant position in smallholder agricultural marketing was reduced, except for smallholder tobacco and cotton, and a multi-channel marketing system involving private traders was introduced. Private sector participation in marketing was supported by the introduction of a differential crop pricing system between ADMARC depots and primary buying points. Second, ADMARC reviewed its investment portfolio and began a comprehensive program of disposal of nonmarketing assets. These structural reforms were complemented with cost-cutting measures, including the closure of some seasonal markets and reduction in staff levels. Under the first year of the program, ADMARC initiated further reforms to improve its financial viability and operating efficiency, including the introduction of fuller cost recovery on the marketing of producer inputs, additional staff reductions, improved transport planning, improved cost-center accounting, reform of rice marketing, asset divestiture, and the development of a corporate plan. The actions taken during the past two years in conjunction with high tobacco prices and maize sales to the Strategic Grain Reserve have accounted for a sharp improvement in ADMARC's profitability, from a net loss (after depreciation and interest) of MK 2.3 million in 1987/88 to a net profit of MK 14.9 million in 1988/89.

44. The Government is committed to further reform during the program period to improve efficiency in the agriculture sector and to realize the medium-term objectives for ADMARC of market stabilization and financial viability. Based on the results of the recently completed ADMARC cost structure study, the Government is reviewing the financial costs and economic benefits arising from the commercial and development functions currently undertaken by ADMARC. The study has identified a number of ADMARC activities that are not financially viable but nonetheless play an important role in economic development. These include the operation of seasonal markets in areas with little marketed output, the role of residual buyer in surplus production years, the purchase of certain crops at prices mandated by Government that do not cover operating costs, and the provision of seeds and other production inputs below cost. To strengthen ADMARC efficiency and operating performance, subject to the program's overall fiscal objectives, the Government will assume responsibility to finance priority development functions that are not consistent with ADMARC financial viability directly out of the government budget. To this end, the Government will agree with ADMARC

by December 1989 on which development activities ADMARC will continue to undertake based on direct budget support and which activities will be dropped altogether from ADMARC operations. It is intended that the transfer of agreed development functions to Government will be reflected in the FY 1990/91 budget. The scope of specific policy and institutional measures to be implemented under the study will be agreed with the World Bank and the Fund.

45. In addition to delineating commercial and development functions, the Government will continue to strengthen ADMARC's financial position during the program period through the following revenue and cost measures: (i) the pricing policy to be implemented by ADMARC will ensure that each individual crop trading account will achieve, on average, a surplus during a reasonable time horizon as well as timely repayment of financial obligations; (ii) the asset divestiture program will continue, with a targeted disposal of three assets in 1989/90; (iii) staff levels will continue to be reduced; (iv) expenses arising from the operation of the strategic grain reserve and other food security activities will continue to be met directly from the budget; and (v) ADMARC's net use in any year of its seasonal commercial bank overdraft will be zero by end-year.

V. Social Development

46. The Government's efforts to restore macroeconomic balance and sectoral growth will be complemented by a comprehensive program to strengthen human resource development and alleviate poverty. With an estimated per capita income of US$170 Malawi remains one of the poorest countries in the world. While social indicators have improved since Independence, they remain low by African standards, particularly in nutrition, school enrollment, literacy, and infant and maternal mortality levels. In response to these problems, the Government will maintain and expand existing initiatives to support social development, particularly among the most vulnerable and disadvantaged groups, as reviewed below. This strategy will involve an increased allocation of public expenditures to the social sectors during the program period, ensuring that the fiscal policy of strict containment of public expenditures does not erode the provision of essential services. These efforts to raise education, health and nutrition levels will be supported by studies underway by the World Bank designed to identify new policy and investment measures, including an integrated human resource development study, a country economic memorandum highlighting poverty issues, and a food security report.

Food security

47. The Government will continue to pursue a number of studies and trial projects to strengthen domestic production and nutrition levels.

At the national level, a food security monitoring and reporting system, set up in 1987, is now fully operational. The Government is following up the 1988 study of food security strategy and restocking the strategic grain reserve. The Government purchased 60,000 metric tons of surplus maize from ADMARC's reserves and an additional amount of some 40,000 metric tons from a private farm in 1988/89 and expects to continue the restocking in 1989/90 from additional domestic purchases and donor maize grants.

48. Food security at the household level is a critical factor in improving nutrition. It is estimated that almost 55 percent of all smallholders are unable to meet minimum caloric requirements from their own farms, due to growing land pressures and declining soil fertility, and face seasonal food deficits. As a result, many smallholders sell their labor to larger farmers or estates at key points in the growing season to provide supplementary food, depriving their own plots of sufficient labor and exacerbating the problem of declining agricultural yields. As reviewed in paragraph 32, the Government is expanding the scope of agricultural interventions to ensure that farmers with less than one hectare of land gain access to credit, inputs and extension services. Likewise, it is reorienting the research and extension program to make it more appropriate for smaller farmers.

Education

49. The Government will build upon its Second Ten-Year Education Plan for 1985-95 with the support of the World Bank, AfDB, and other donors critical for its full implementation. The emphasis will be on expansion and quality enhancement of primary education to contribute to spreading the benefits of economic growth. The Government's program will include less focus on secondary boarding schools in favor of day schools, more attention to the sciences and technical skills, improved teacher training and provision of teaching materials, curriculum reform, and a reduction in primary school dropout rates. Special attention will be paid to increased access and retention rates for girls. Government will continue to review fees at post-primary levels of education and restructure the fee schedule to ensure an equitable distribution and adequate level of cost recovery.

Health

50. The Government is implementing its National Health Program for the period 1986-95 and the support of the World Bank and other donors will ensure wider implementation. Specific policy measures (excluding population issues, which are described below) include: improved staffing of the Primary Health Care facilities of the community-based health system, increased allocation of resources for maternal and child care services, and expansion of family health concepts through educational programs and family health services. The Government will begin a phased program in

1989/90 to strengthen the local supply of doctors, with the introduction of the final year of clinical training in Malawi and the awarding of the medical degree by the University of Malawi. The timing and content of subsequent phases of medical training will be reviewed with the World Bank in the context of the program's fiscal objectives. The manpower development, planning, and evaluation capacity of the Ministry of Health will be strengthened.

VI. Long-Term Development Issues

51. In addition to pursuing policies and programs designed to ameliorate structural constraints to growth in the short and medium term, the Government is also taking steps to address longer-term developmental problems.

Population

52. Malawi is one of the most densely populated countries in Sub-Saharan Africa, with a population growth rate estimated by the Government at 3.2 percent in the 1987 census (this rate excludes the significant increase in displaced persons). This rapid population growth threatens to exhaust the country's land resources and create a massive and unsustainable demand for food, energy, and social services. Malawi's long-term prospects for sustained development and per capita income increases depend heavily on immediate and effective action to slow population growth. Thus, the Government has begun to implement new policies and programs including: (i) expansion of child-spacing services in the Maternal and Child Health Program; (ii) introduction of social marketing and community based distribution of contraceptives; (iii) support to a new nongovernment initiative to establish a Family Welfare Association, which will disseminate information on family planning concepts; (iv) continuation of voluntary surgical contraception programs; and (v) expansion of education programs on the impact of population growth on economic development. Population policy issues and additional project interventions will be reviewed in a Bank Population Study, to be completed in 1990, and a new Health and Population Project, scheduled for implementation in 1991.

Environment

53. Given the central role of agriculture in the economy, the Government has become increasingly concerned about environmental problems and protection of the natural resource base. The growing population pressure, combined with limited arable resources, have resulted in increasing degradation of the soils and forests, which carries far-reaching implications for agricultural productivity and Malawi's growth prospects. Other environmental problems include degradation of water resources, depletion of fisheries due to over-fishing, and loss of

wildlife as a result of poaching and encroachment. Government has developed a relatively strong institutional and policy framework in response to these environmental problems and existing programs support improved cultivation and livestock practices, social forestry, and improved charcoal production and tobacco curing. Additional environmental policy measures that will be undertaken during the program period include the following: (i) introduction of incentive bonus payments in the smallholder tree-planting program in 1989/90; (ii) increases in stumpage fees in order to reach a full cost recovery stumpage rate by 1994; (iii) improvements in the system for wood revenue collection and forest management; and (iv) stricter enforcement of land use covenants in estate land leases. Government plans to develop an Environmental Action Plan in 1990/91 that will map out a long-term investment and policy reform program for environmental protection. This will be supported by a World Bank economic report on environmental issues in 1990.

VII. External Financing Requirements

54. Despite the considerable adjustment effort envisaged in the medium term, the pace of structural reform and of economic growth will continue to be constrained by the amount of concessional external resources forthcoming to support the authorities' adjustment program. The revised scenario updates projections of external resource inflows during 1989-1992 and merges the two scenarios incorporated in the first year PFP. On the basis of performance during 1988/89 and more up-to-date information, the revised base scenario envisages higher concessional external assistance and a higher average rate of economic growth than the original first scenario, although both are still lower than the second scenario projections of the first year PFP.

55. During 1989-92, it is expected that the current account deficit (excluding official transfers) will decline from the equivalent of 8.4 percent of GDP to 6.9 percent. At the same time, external reserves will not decline below 4 months of non-maize imports. Malawi's debt service profile has improved markedly relative to the original assumptions in the program, as capital inflows are now projected to be more concessional than assumed in the initial PFP. As a result, Malawi's debt service and debt service ratio are expected to decline at a faster pace and to remain within manageable limits. The revised projection of total financing requirements for 1989-92 comprising the current account deficit, public sector debt service payments (including to the Fund) and the maintenance of the external reserves level at the equivalent of 4 months of non-maize imports, amounts to SDR 656 million over the period 1989-92 (Table 2). Disbursements from existing commitments as of early 1989--including project loans of SDR 166 million, disbursements of SDR 46.5 million under the ESAF, and SDR 28 million from the World Bank's ITPAC--are estimated at SDR 435 million. Disbursements from

expected new commitments are projected at SDR 207 million, including SDR 95 million from the World Bank through the ASAC and other adjustment lending. The balance of SDR 14 million is expected to come from debt relief already obtained by Malawi for 1989.

56. Total financing requirements during 1989 are estimated at SDR 200 million. Of this amount, SDR 150 million is expected to be met from existing commitments, including project loans of SDR 38 million; ESAF disbursements of SDR 19 million; and World Bank Adjustment lending under ITPAC of SDR 28 million. Disbursements from new commitments, primarily of ITPAC cofinancing, are projected at SDR 36 million.

Table 1. Malawi: Key Macroeconomic Indicators, 1985-92

	1985	1986	1987	1988	1989	1990	1991	1992
	Actual				Projected			
	(Annual percentage change)							
GDP growth rate	4.5	1.1	1.4	3.6	3.7	4.1	4.3	4.5
GDY growth rate	3.7	-2.1	0.5	6.7	3.7	3.5	4.9	5.8
GDY/per capita growth rate	0.5	-5.3	-2.7	3.5	0.5	0.3	1.7	2.5
Consumption/per capita growth rate	-1.3	-0.6	-5.9	5.7	1.2	0.1	0.1	0.5
	(In percent, unless otherwise specified)							
Debt service (SDR millions) 1/	121.2	132.5	109.3	107.0	100.1	80.2	81.5	83.4
Debt service/XGS	44.5	57.3	46.9	43.9	37.5	27.6	25.9	24.3
Debt service/GDP	10.9	13.0	11.3	10.0	8.0	7.0	6.7	6.3
Gross investment/GDP	18.5	11.3	14.1	16.1	17.3	15.0	15.8	16.5
Fixed investment/GDP	13.3	11.1	12.3	13.0	14.2	14.5	15.0	15.7
Stockbuilding/GDP	5.2	0.2	1.8	3.1	3.1	0.5	0.8	0.8
Government investment/GDP	6.8	7.8	5.6	5.2	5.3	5.7	5.8	5.8
Private investment/GDP 2/	11.7	3.5	8.5	10.9	12.0	9.3	10.0	10.7
Government/private investment	0.58	2.23	0.66	0.48	0.44	0.62	0.58	0.54
Domestic saving/GDP	13.1	9.2	11.9	7.6	6.9	7.0	8.5	10.4
National saving/GDP 3/	9.4	5.6	9.2	7.8	8.9	5.1	7.4	9.6
Government saving/GDP	-2.8	-4.5	-4.5	-1.8	-1.1	-1.0	-1.0	-1.0
Private saving/GDP	12.2	10.1	13.7	9.6	9.9	6.2	8.4	10.7
Marginal national saving rate 3/	-0.06	-0.25	0.24	-0.39	0.25	-0.80	0.49	0.47
Government revenue/GDP 4/	21.9	21.1	19.5	20.3	19.3	19.6	19.3	...
Government expenditure/GDP 4/	31.9	34.2	28.6	26.9	25.6	26.5	26.2	...
Fiscal deficit/GDP 4/	-10.0	-13.1	-9.1	-6.6	-6.3	-6.9	-6.9	...
Fiscal deficit incl. grants/GDP 4/	-7.8	-9.6	-6.6	-1.2	-0.4	-1.3	-3.8	...
CPI change	14.9	14.8	26.8	31.4	15.0	12.5	7.5	5.0
GDP deflator change	9.2	12.6	22.7	29.9	15.6	10.2	8.2	6.4
Real exchange rate (Index, 1980 = 100)	96.9	85.6	77.8	82.3	...	...	...	...
Export volume growth (merchandise)	-2.3	3.0	-0.7	-4.9	4.4	7.7	4.3	4.2
Exports/GDP	24.4	22.7	24.1	22.7	21.3	25.6	25.7	26.1
Import volume growth (merchandise) 5/	14.5	-14.7	-2.1	27.6	9.4	6.2	4.5	4.2
Imports/GDP	29.2	24.7	26.3	31.2	31.0	34.4	33.7	32.5
Current account (SDR millions) 6/	-95.2	-57.9	-46.0	-89.4	-105.7	-112.5	-103.1	-90.8
Current account/GDP 6/	-8.6	-5.7	-4.8	-8.3	-8.4	-9.9	-8.4	-6.9
Current account incl. grants/GDP	-6.4	-3.3	-2.4	-2.0	-2.6	-4.8	-5.5	-4.3
External reserves (SDR millions)	39.8	16.4	34.4	107.4	115.8	129.1	133.7	129.6
In months of non-maize imports	1.7	0.9	1.8	4.6	4.3	4.3	4.2	4.0

Sources: Data provided by the Malawian authorities; and staff estimates and projections.

1/ Before debt relief; excluding debt conversion; including interest on short-term debt.
2/ Statutory bodies that are not included in the central government budget and stockbuilding are included in private sector investment.
3/ National saving rate in 1988-90 is affected by emergency grants for displaced persons.
4/ Fiscal year basis; i.e., beginning in April of the year indicated.
5/ Excluding emergency imports for displaced persons.
6/ Excluding official transfers.

Table 2. Malawi: External Financing Requirements, 1985-92

(In millions of SDRs)

	1985	1986	1987	1988 Est.	1989 Projected	1990 Projected	1991 Projected	1992 Projected
Total financing requirement	136.0	51.9	133.0	265.1	200.3	169.0	152.4	134.6
Current account	-95.2	-57.9	-46.0	-89.4	-105.7	-112.5	-103.1	-90.8
Amortization (public sector)	-56.8	-58.6	-42.6	-48.1	-45.3	-28.9	-29.4	-34.3
Change in arrears (increase +)	—	43.8	-9.7	-34.1	—	—	—	—
Change in gross official reserves (increase -)	18.2	24.1	-18.7	-73.0	-8.4	-13.3	-4.7	4.1
IMF repurchases	-16.0	-20.6	-23.6	-19.9	-19.0	-13.8	-15.2	-13.6
Change in other Reserve Bank liabilities (net)	13.8	17.3	7.5	-0.6	-21.9	-0.5	—	—
Disbursements (existing commitment) 1/	129.3	49.5	132.6	218.4	150.5	102.0	96.5	86.5
Net official transfers	24.1	24.5	23.2	67.4	56.7	36.4	31.9	34.3
Of which: SAL-related grants	(—)	(9.3)	(6.4)	(44.3)	(25.1)	(7.6)	(—)	(—)
Borrowing by the public sector	69.0	89.8	95.2	95.9	75.2	47.0	55.3	52.2
Bilateral creditors	16.1	10.4	22.8	28.8	22.6	14.1	16.6	15.7
Of which: adjustment lending	(—)	(6.8)	(6.4)	(5.3)	(—)	(—)	(—)	(—)
Multilateral creditors	50.2	72.4	71.4	66.2	51.9	32.4	38.2	36.0
Of which: adjustment lending (World Bank)	(7.4)	(47.8)	(28.1)	(23.0)	(31.8)	(3.8)	(3.8)	(—)
Private creditors	2.7	7.0	1.0	1.0	0.8	0.5	0.6	0.5
IMF (stand-by purchases)	23.0	—	—	9.3	—	—	—	—
ESAF credit	—	—	—	9.3	18.6	18.6	9.3	—
Other capital (net) 2/	13.2	-64.8	14.2	36.6	—	—	—	—
Disbursements (expected commitments)	—	—	—	—	35.9	67.0	55.9	48.1
Net official transfers	—	—	—	—	16.2	21.0	4.1	—
Of which: SAL-related grants	(—)	(—)	(—)	(—)	(16.2)	(21.0)	(4.1)	(—)
Borrowing by the public sector	—	—	—	—	14.2	44.6	49.4	41.8
Bilateral creditors	—	—	—	—	7.6	15.2	11.4	11.4
Multilateral creditors	—	—	—	—	6.6	29.4	38.0	30.4
Of which: World Bank	(—)	(—)	(—)	(—)	(—)	(22.8)	(38.0)	(30.4)
Other capital (net) 2/	—	—	—	—	5.5	1.4	2.4	6.3
Debt rescheduling	6.7 3/	2.4 3/	0.4 3/	46.7	13.9	—	—	—
Financing gap	—	—	—	—	—	—	—	—

Sources: Data provided by the Malawian authorities; and staff estimates and projections.

1/ All project loans and grants are included under "existing commitments." The amounts for 1989-92 are SDR 72 million, SDR 70 million, SDR 79 million and SDR 82 million.

2/ Includes net private long- and short-term inflows and, for the historical data, errors and omissions.

3/ Rescheduling of Dwangwa Sugar Corporations debt.

Malawi: Summary and Timeframe for Adjustment Policies, 1989/90-1991/92

Sector	Objectives and targets	Strategies and measures	Timing
1. External sector			
a. Exchange and trade system	Promote efficient resource allocation.	Manage exchange rate flexibly.	1989/90-1991/92
	Reduce efficiency losses associated with administrative controls on foreign exchange allocation.	Progressively liberalize imports.	Complete liberalization by December 1989.
	Simplify and rationalize system of trade taxes.	Rationalize import duties toward more uniform rates of domestic protection at lower average levels.	1989/90-1990/91
	Rationalize treatment of exports.	Reduce scope of export licensing.	Completed.
b. External debt	Improve profile of external public debt.	Observe limits on contraction of nonconcessional debt.	1989/90-1991/92
2. Public Finance			
a. Central government budget	Adjust fiscal position.	Maintain overall deficit at non-inflationary and sustainable level.	1989/90-1991/92
b. Revenue	Broaden effective tax base.	Move from specific to ad valorem rates for excise tax.	Completed.
	Improve allocative efficiency while achieving greater equity.	Introduce a tax allowance for export earnings and a more effective duty drawback system for exporters.	1989/90
		Introduce new surtax credit system tax; exempt payment of surtax on inputs by producers.	Completed.

Malawi: Summary and Timeframe for Adjustment Policies, 1989/90-1991/92 (continued)

Sector	Objectives and targets	Strategies and measures	Timing
	Strengthen and simplify tax administration.	Implement phase-in of current payment system for company taxes.	Completed.
c. Expenditures	Improve expenditure allocation decision-making process.	Develop proposals to shift donor financing to recurrent expenditures.	1989/90.
		Activate and strengthen three-year forward budget.	1989/90-1991/92
	Strengthen assessment of public sector investment program (PSIP).	Continue to consult with World Bank on three-year rolling PSIP.	1989/90-1991/92
		Develop and implement formal guidelines for submissions to PSIP.	1989/90
		Expand PSIP classification system.	1989/90
	Strengthen expenditure control and monitoring procedures.	Introduce breakdown by expenditure program of Ministries' accounts at Reserve Bank of Malawi.	1989/90
3. Monetary and financial policies	Promote efficiency in the allocation of financial resources and implementation of monetary policy.	Revise Reserve Bank of Malawi Act.	Completed.
		Revise Banking Act.	October 1989.
		Introduce reserve requirement.	Completed.
		Develop capital markets.	1989/90-1990/91.
4. Agriculture			
a. Smallholder production	Increase smallholder productivity through increased use of fertilizer.	Agree with World Bank and IMF on medium-term fertilizer subsidy policy.	1989/90
		Expand supply of fertilizer in small packets.	1989/90
		Expand seasonal credit system.	1989/90-1991/92

Malawi: Summary and Timeframe for Adjustment Policies, 1989/90-1991/92 (continued)

Sector	Objectives and targets	Strategies and measures	Timing
	Increase smallholder productivity through adoption of high-yielding maize varieties.	Develop implementation program for development of maize technologies.	1989/90
		Train and set up adaptive research teams and improve extension methodology.	1990/91
		Develop Research Master Plan.	Completed
b. Estate production	Increase estate productivity through more efficient resource use.	Establish estate extension service.	1989/90
		Increase land-lease charges.	1989/90
		Stricter enforcement of land use covenants in leases.	1989/90-1991/92
c. Land policy	Reorient land policy to promote equitable and efficient use of land.	Enforce restrictions on estate expansion in areas of high land pressure.	1989/90-1991/92
d. Food security	Strengthen domestic food security, particularly for smaller farmers.	Rebuild strategic grain reserve.	1989/90-1990/91
		Conduct pilot projects to test alternative mechanisms for providing credit and inputs to food deficit farmers.	1989/90-1990/91
		Relax crop restrictions on smallholder production of high-value crops.	1989/90
e. Pricing and marketing	Maintain producer incentives to encourage efficient production.	Consult with the World Bank and the Fund on annual producer price review.	1989/90-1990/91
	Maintain multichannel marketing system.	Review regulatory framework for private trading.	1989/90.
5. Industry/Energy			
a. Industry	Ensure adequate opportunities for small- and medium-scale enterprises.	Review institutional and regulatory framework for small enterprises.	1989/90
b. Energy	Promote efficient investment and consumption of power.	Continue to base power investment program on least-cost power development study.	1989/90-1991/92
		Continue to set prices based on long-run marginal cost.	1989/90-1991/92

Malawi: Summary and Timeframe for Adjustment Policies, 1989/90-1991/92 (continued)

Sector	Objectives and targets	Strategies and measures	Timing
	Promote efficient consumption of petroleum.	Prices to reflect full pass-through of import and distribution costs.	1989/90-1991/92
6. Infrastructure			
a. Transport	Reduce external transport cost burden.	Continue to improve Northern Corridor transport route.	1989/90-1991/92
		Review scope for expansion of Malawian-owned international and domestic road haulage.	1989/90
	Liberalize transport regulatory framework.	Review international off-loading requirement.	1989/90
	Strengthen road maintenance and rehabilitation.	Strengthen program of road maintenance.	1989/90-1991/92
b. Water	Ensure financially viable expansion of water supply.	Increase water board rates to ensure financial viability.	1989/90-1991/92
		Increase District Water Supply Fund's rates to adjust for domestic inflation.	1989/90-1991/92
		Continue water supply maintenance program.	1989/90-1991/92
c. Housing	Encourage development of private housing market.	Expand housing finance market.	1990/91-1991/92
		Liberalize NBS policies.	1990/91-1991/92
		Initiate divestiture of subsidized civil service housing.	1990/91-1991/92
		Transfer management of traditional housing areas to local government.	1990/91
d. Urban services	Strengthen local government.	Strengthen management capability and local finances.	1990/91-1991/92
7. Public enterprises			
a. Monitoring	Improve efficiency and financial performance of public enterprises.	Develop and implement evaluation criteria for parastatal investment plans.	1989/90
		Implement performance monitoring system.	1989/90-1991/92
b. ADMARC	Improve ADMARC's operating efficiency and financial viability.	Review costs of ADMARC's development and commercial functions.	1989/90

Malawi: Summary and Timeframe for Adjustment Policies, 1989/90-1991/92 (concluded)

Sector	Objectives and targets	Strategies and measures	Timing
		Agree with ADMARC on functions to be transferred to government budget or discontinued.	1989/90
		Continue asset divestiture program.	1989/90-1990/91
8. Human resources			
a. Education	Expansion and quality enhancement of primary school education and intensified usage of secondary schools.	Limit construction of boarding schools and emphasize development of secondary day schools.	1989/90-1991/92
		Provide adequate allocation in recurrent budget for textbooks and other teaching materials.	1989/90-1991/92
		Improve teacher training.	1990/91
		Develop program for curriculum reform.	Completed
	Increase supply of technical and management skills in the economy.	Develop Malawi Institute of Management.	1989/90-1991/92
	Expand services through cost-recovery measures.	Restructure post-primary fee schedule towards cost recovery.	1989/90-1991/92
b. Health	Expand community-based health services.	Ensure adequate staffing for Primary Health Care facilities.	1990/91
		Increase allocation of resources to maternal and child care services.	1990/91
9. Population	Reduce population pressures.	Expand child-spacing services in MCH Program.	1989/90-1991/92
		Introduce social marketing and community-based distribution of contraceptives.	1989/90-1991/92
		Support Family Welfare Association.	1989/90-1991/92
		Expand population education program.	1989/90-1991/92
10. Environment	Support environmental protection and improve land use.	Introduce incentive payments for tree planting.	1989/90
		Increase stumpage fees.	1989/90-1991/92
		Improve wood revenue collection and forest management.	1989/90-1991/92