EXECUTIVE BOARD MEETING

EBS/18/96

November 6, 2018

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Malawi—First Review Under the Three-Year Extended Credit Facility Arrangement and Requests for Modification and Waivers of Nonobservance of Performance Criteria**

Board Action:	Executive Directors' **consideration** (Formal)
Tentative Board Date:	**Wednesday, November 21, 2018**
Proposed Decisions:	Pages 17–20
Publication:	Yes*
Questions:	Ms. Mitra, AFR (ext. 39523) Ms. Farahbaksh, AFR (ext. 39957) Ms. Pant, AFR (ext. 35974)
Document Transmittal in the Absence of an Objection and in accordance with Board policy:	Wednesday, November 14, 2018—WTO After Board Consideration—African Development Bank, European Commission

***The authorities have indicated that they consent to the Fund's publication of this paper.**

INTERNATIONAL MONETARY FUND

MALAWI

November 5, 2018

FIRST REVIEW UNDER THE THREE-YEAR EXTENDED CREDIT FACILITY ARRANGEMENT AND REQUESTS FOR MODIFICATION AND WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA

KEY ISSUES

Context. Malawi's economic growth remains moderate, reflecting a weak agricultural harvest and continued electricity shortages. Fiscal deficits continue to be financed domestically, as donor funding remains constrained by governance concerns since the 2013 cashgate scandal, resulting in an increasing public debt burden. Presidential elections are scheduled for mid-2019.

Program performance. Most quantitative performance criteria (QPC) were met at end-June 2018, with significant overperformance on international reserves and the reduction in Reserve Bank of Malawi (RBM) holdings of government securities. The QPC on the primary fiscal balance was missed by 0.9 percent of GDP due to expenditure overruns. The continuous QPC on new non-concessional external debt was missed due to a technical oversight in the Technical Memorandum of Understanding. Based on corrective measures, the authorities request waivers of non-observance. Two structural benchmarks were observed and most of the rest have been completed with delay.

Program strategy. Entrenching macroeconomic stability and enhancing poverty-reducing and resilient growth continue to be the authorities' goal. Program fiscal targets have been strengthened to preserve debt sustainability, including a tightening of the FY 2018/19 target to correct for the FY 2017/18 slippage and partially adjust for postponed budget support. Governance reforms span debt management, commitment control, bank reconciliation, investment spending efficiency, and monitoring of state-owned enterprises. Tight monetary policy will contain inflation. Greater exchange rate flexibility is needed to buffer shocks, preserve competitiveness, and strengthen financial sector resilience. Advancing structural reforms will support private sector development.

Staff views. Staff supports the authorities' request for completion of the first review under the ECF arrangement and for waivers of non-observance for the missed QPCs, given the authorities commitment to corrective measures. This would result in the disbursement of SDR 11.15 million and help catalyze donor support.

Approved By
David Robinson (AFR) and Nathan Porter (SPR)

Discussions on the first review under the ECF arrangement were held on September 25-October 5, 2018 in Lilongwe and Blantyre. The staff team comprised Ms. Mitra (head), Ms. Farahbaksh, Ms. Pant, Mr. Ree (all AFR), Ms. Lin (SPR), Mr. Swistak (FAD), and Mr. Banda (local economist). Mr. Hettinger (World Bank) joined the technical meetings. Mr. Almeida and Ms. Vibar assisted in the preparation of the staff report. The mission held discussions with Mr. Goodall E. Gondwe, Minister of Finance; Mr. Dalitso Kabambe, Governor of the Reserve Bank of Malawi; and other senior officials. The mission also met representatives of the private sector, civil society, and development partners and held a press conference.

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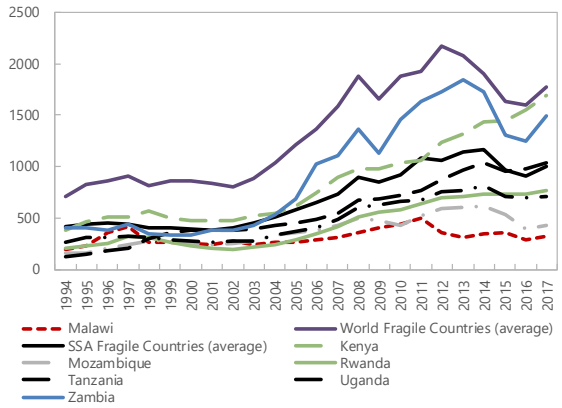
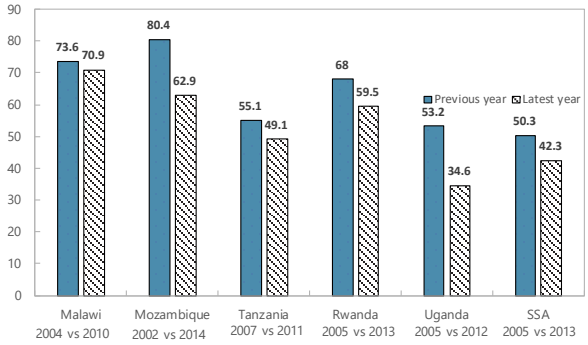
CONTEXT

1. Malawi is a fragile country facing pervasive poverty and severe vulnerabilities to climate shocks. Economic growth, averaging 3.7 percent during 2012–17, is barely above population growth (2.9 percent in 2017). As a result, Malawi's per capita GDP ($322 in 2017) is falling further behind that of its regional peers and other fragile states and its poverty incidence is among the highest in sub-Saharan Africa (Text Figures 1 and 2). Two thirds of the population are employed in agriculture (primarily maize farming) which is vulnerable to frequent droughts given the low coverage of engineered irrigation systems and a single harvest per year.

Text Figure 1. GDP per Capita: Malawi vs. Fragile Countries and Regional Peers
(US$)



Text Figure 2. Poverty Rate: Malawi and Peer Countries
(Poverty headcount ratio at US$1.90 a day, Percent of population)



Sources: Malawian authorities; IMF staff estimates.

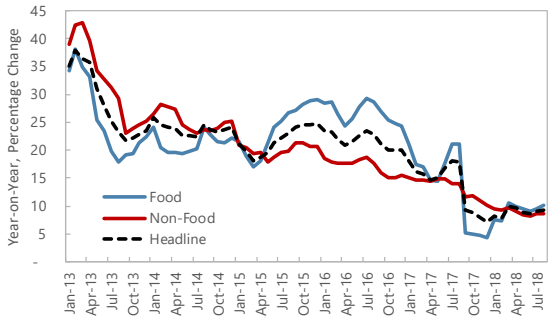
2. The May 2019 presidential and parliamentary elections are expected to be closely fought, with a focus on governance. Candidates include the incumbent President Mutharika, Vice President Chilma, and former President Banda. Governance issues and electricity shortages are at the center of most political discussions.

3. Despite the approval of a new three-year ECF arrangement, donor funding for the budget remains low. Reflecting continued governance concerns after the 2013 cashgate scandal and slow reform implementation, most donors limit support to off-budget projects and the World Bank may delay disbursement of $80 million (1.1 percent of GDP) of budget support until FY 2019/20. Absent a substantial increase in on-budget donor financing, fiscal space will remain limited, constraining the authorities' ability to progress towards the Sustainable Development Goals (SDGs).

RECENT DEVELOPMENTS

4. Malawi's economic growth moderated this year—declining from 4 percent in 2017 to 3.2 percent in 2018. Agriculture, especially maize, is suffering from insufficient rain and insect infestations. As a result, one sixth of the population is at risk of food insecurity. Manufacturing and wholesale and retail trade remain challenged by electricity shortages (despite deployment of diesel generators). Inflation rose from 7.1 percent at end-2017 to 9.3 percent in August 2018 and is expected to end the year at 9.5 percent (Text Figure 3)—reflecting higher maize prices and cumulative increases of 45 percent in electricity tariffs in February/July/October and 15 percent in fuel prices in July/October.

Text Figure 3. Inflation
(Year-on-year percentage changes)



Sources: Malawian authorities; IMF staff estimates.

5. The fiscal balance deteriorated in FY 2017/18. The overall deficit was 1.3 percent of GDP larger than programmed. The primary deficit, after adjusting for large shortfalls in budget support and dedicated grants, widened by 0.8 percent of GDP. These shortfalls—largely due to capacity constraints—along with lower project loans were reflected in lower foreign-financed capital spending. Tax revenue was broadly in line with the program while non-tax revenue overperformed owing to a one-off remittance of stamp duty.[1] However, there were expenditure overruns—mainly from increased spending to ensure safety during elections as well as additional maize purchases to ensure food security for the most vulnerable in light of poor maize harvests and payment of arrears arising from court rulings.[2] These overruns were larger than the decline in domestically-financed

Text Table 1. Central Government Operations
(FY 2017/18, percent of GDP)[1]

	Prog.	Est.	Change
Revenue			
Tax revenue	17.6	17.5	-0.1
Non-tax revenue	1.9	2.3	0.3
Budget support and dedicated grants	1.0	0.5	-0.5
Project grants	1.8	0.9	-0.9
Spending			
Generic goods and services	2.7	2.7	0.0
Elections	0.2	0.6	0.4
Maize	0.5	0.7	0.2
Social spending	1.8	1.9	0.1
Arrears payments	1.3	1.6	0.3
Transfers to public entities	2.3	2.2	-0.1
Interest	4.0	4.0	0.0
Other current spending	10.1	10.5	0.4
Development spending			
Foreign financed	4.8	3.1	-1.6
Domestically financed	1.9	1.7	-0.2
Discrepancy	0.3	-0.4	-0.7
Overall balance	-7.0	-8.4	-1.3
Primary balance (excluding budget support and dedicated grants)	**-4.0**	**-4.9**	**-0.8**
Nominal GDP (in MK billions)	4764	4735	-29

[1]Due to rounding, the difference between figures in the "Est." and "Prog." can differ from "Change" by one decimal place.

Sources: Malawian authorities; IMF staff estimates.

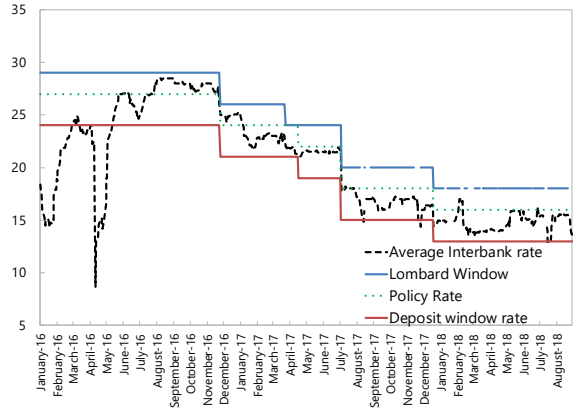
[1] In FY 2017/18, in contrast to past years, the existing stamp duty was collected and accounted for in the budget.

[2] Some of the arrears accrued during FY 2012/13—2016/17 that were verified and rejected by the Accountant General were contested in court. Recently, the court-ruled on some of these cases, requiring the government to pay the plaintiffs (totaling 0.3 percent of GDP).

capital spending cuts. The deficit was financed domestically by banks and non-banks.

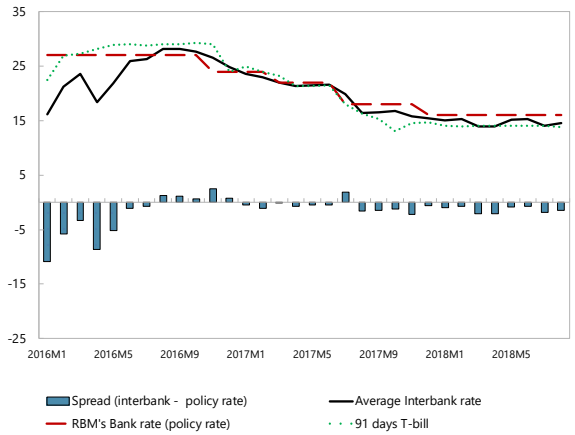
6. Tight monetary policy is containing inflation. Responding to inflationary pressures, the Reserve Bank of Malawi (RBM) has maintained the policy rate at 16 percent. The interbank rate continued to align with the policy rate (Text Figures 4 and 5). Average real bank lending rates have declined but tighter lending conditions and weak credit demand (reflecting electricity shortages weighing on business activity) has stalled credit growth. Weak credit demand as well as low intermediation and banks' increased holding of government securities has led to a reduction in loans and advances (in percent of assets) from 51 percent in 2012 to 32 percent in August 2018.

Text Figure 4. Interest Rate Corridor
(Percent, Jan.2016–Aug.2018)



Sources: Malawian authorities; IMF staff estimates.

Text Figure 5. Policy, Interbank and Treasury Bill Interest Rates
(Percent, Jan.2016–Aug.2018)

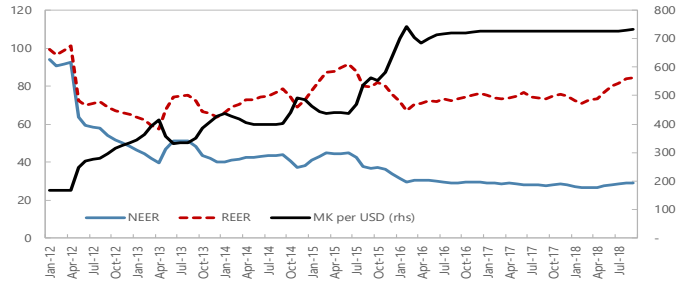


7. Banking system resilience has improved. The system is well capitalized and profitable. Non-performing loans (NPLs) declined from 15.7 percent at end-2017 to 9.3 percent in August 2018 mainly due to write offs and loan recovery. Over the same period, provisions almost doubled with the adoption of IFRS9 requirements. The situations of two small banks that were at the borderline of the minimum core capital requirement in December 2017 have improved significantly through capital injection, asset recovery, and write-offs. Nevertheless, the RBM's June 2018 stress test showed that some individual banks remain vulnerable to credit, liquidity, and interest rate shocks.

8. The current account deficit continued to improve, declining from 11.1 percent of GDP in 2017 to a projected 9.3 percent of GDP in 2018. Solid global tobacco demand and growth in other commodities (such as edible ground nuts) are supporting exports. This, combined with a reduction in commercial banks' net foreign assets, resulted in an overperformance of the end-June reserves target. The impact of higher global fuel prices on the import bill was mitigated by a decline in project-related imports. For the year as a whole, lower grants, reflecting lower-than-expected implementation capacity, weigh on reserves with coverage in months of prospective imports expected to decline from 3.4 at end-2017 to 2.9 at end-2018.

9. The nominal exchange rate has been stable against the U.S. dollar for two years (Text Figure 6). The IMF's 2017 Annual Report on Exchange Rate Arrangements and Exchange Rate Restrictions (AREAER) reclassified Malawi's *de facto* arrangement from floating to stabilized. The stability reflects tight monetary policy and limited price discovery in a shallow interbank FX market. Most FX transactions take place in the retail market and directly with the RBM—neither of which contribute to price formation in the interbank market (Box 1). The REER appreciated nearly 5 percent during the first nine months of 2018 relative to the same period in 2017, as inflation differentials more than offset the nominal depreciation (about 2 percent) against trading partners.

Text Figure 6. Malawi: REER, NEER, and U.S. Dollar Exchange Rates



Sources: Malawian authorities; IMF staff estimates.

MACROECONOMIC OUTLOOK AND RISKS

10. The outlook is positive. Growth is expected to rebound to 4.0 percent in 2019 reflecting increased electricity generation and growing infrastructure investment. Over the medium term, growth is projected to reach around 6.5 percent assuming improved irrigation infrastructure and cropping techniques (including diversification to cassava and sweet potatoes), enhanced electricity generation, better road and telecommunications networks, increased donor assistance, and greater access to finance for the private sector.

11. Inflation is anticipated to remain in single digits while the current account gradually improves. Inflation is projected to moderate to 8.9 percent in 2019 in line with a gradual reduction in food prices and to around 5 percent over the medium term owing to tight fiscal and monetary policies and further declines in food prices as well as reduced international fuel prices. The current account deficit is expected to gradually narrow towards 7.5 percent of GDP and international reserves rise to around 4.5 months of prospective imports supported by strengthened competitiveness, export diversification, and fiscal restraint.

12. Risks are tilted to the downside. In the election run-up, political pressures could weaken policy and reform implementation. Intensified governance challenges could further postpone donor support. These risks, combined with adverse weather, infestations, and worsened terms of trade, could weigh on growth, raise inflation, and increase balance of payments pressures. Tighter global financial conditions and weak global growth could depress export growth and reduce donor financing (Annex I: Risk Assessment Matrix). On the upside, faster reform implementation and higher export prices could boost medium-term growth.

PERFORMANCE UNDER THE PROGRAM

13. Most quantitative performance criteria (QPC) for end-June 2018 were met (Table 10). The QPC on net international reserves significantly overperformed (by $119 million) as did the QPC on RBM holdings of government securities—which were reduced by MK 43 billion whereas the program permitted an increase of MK 69 billion. The stock of reserve money was within the programmed upper bound. The continuous QPC on the non-accumulation of external payment arrears was observed. The QPC on the primary fiscal balance (after adjusting for deviations in budget support, dedicated grants, and debt service payments relative to program request) was missed by 0.9 percent of GDP due to expenditure overruns. The continuous QPC on not contracting new non-concessional external debt was missed by about 2 percent of GDP.[3] The indicative target (IT) of a zero ceiling on new domestic arrears was missed by about MK 1 billion due to arrears incurred by universities, which are gradually being settled out of each university's own budget (with no impact on the central government budget or the government's contingent liabilities). The IT on social spending overperformed.

14. Program-supported reforms advanced although only two structural benchmarks (SBs) were met on time (Table 11a). The RBM developed a monetary policy communication strategy ahead of the end-June target date. Monthly cash forecasts for FY 2018/19 were completed for end-June. The new RBM Act 2018 (in lieu of an amended act) was not submitted to Parliament by end-October but the submission will be completed as a prior action. SBs covering reforms to reconcile debt and improve commitment control were completed with delays. Only two of the five reports by Ministries, Departments, and Agencies (MDAs) for March-June 2018 were published on the Ministry of Finance (MoF) website. The remaining three will be published as a prior action (Table 12). Bank account reconciliation (July 2017-May 2018) was completed by the end-July 2018 target date except for salary accounts, which will be incorporated in phases by June 2019. From FY 2019/20, the reconciliation of all accounts will be automated. The forensic audit for FY 2013/14-14/15 is complete and the report has been submitted to the Anti-Corruption Bureau for criminal investigation. However, it will only be available once related criminal investigations are concluded, after which the opening and closing balances of FY 2015/16 can be adjusted.

15. Corrective measures have been agreed for the missed QPCs and the authorities request waivers of nonobservance on this basis. The primary balance for FY 2018/19 has been tightened to correct for the FY 2017/18 slippage and partially adjust for postponement of budget support. The authorities have identified non-priority spending items, in particular, limiting external travel and deferral of non-priority maintenance (0.2 percent of GDP, Memorandum of Economic and Financial Policies (MEFP) ¶21) that can be cut to partially compensate for any future shortfalls in grants and other revenues. The authorities are committed to working with donors to improve the accuracy of

[3] A nonresident bank purchased Treasury Notes of MK 92 billion in the domestic market, which constitutes contracting of new non-concessional external debt according to the Technical Memorandum of Understanding (TMU). This is due to an oversight in the TMU which excluded Treasury Bills but not Treasury Notes from the items subject to the QPC. The definition of the external debt QPC in the TMU has been modified going forward to exclude both Treasury Notes and Treasury Bills from the QPC on new non-concessional external debt.

information on donor flows, especially the timing of disbursements (MEFP ¶20)—including enhanced use of the aid management platform and joint portfolio reviews. They are also steadily working towards raising project implementation capacity, including through improvements in public investment management (MEFP ¶19). In relation to the non-observance of the continuous PC on non-concessional external debt, the authorities have already taken and are committed to continue taking measures to strengthen debt management capacity.

POLICY DISCUSSIONS

Policies will continue to be anchored on entrenching macroeconomic stability, strengthening governance, and attaining higher, more inclusive and resilient growth. The fiscal path has been strengthened to preserve debt sustainability. Governance reforms are being stepped up to catalyze donor support and span commitment control, bank reconciliation, investment spending efficiency, monitoring of state-owned enterprises, and debt management. Tight monetary policy will continue to contain inflation. Greater exchange rate flexibility and advances in financial sector resilience and structural reforms will support broad-based private sector development.

A. Sustaining Macroeconomic Stability

Fiscal Policy

16. The authorities are committed to tightening the fiscal stance in FY 2018/19 (MEFP ¶17)**.** The primary deficit excluding budget support and dedicated grants will be reined in by 1.1 percent of GDP in FY 2018/19 (relative to program request, Text Table 2). Most of this adjustment corrects for the previous year's spending overruns and the rest adjusts for the postponement of World Bank budget support (now assumed to be disbursed in FY 2019/20). The end-December 2018 and end-June 2019 fiscal targets have been revised accordingly (Table 10). Key measures include:

- On the revenue side, tax measures announced in the FY 2018/19 budget will be expeditiously implemented. These include the VAT reverse charge mechanism on imported services, use of VAT withholding, and widening the corporate income tax base by applying a debt-to-equity ratio (adding almost 0.3 percent of GDP relative to the outturn in FY 2017/18). Tax administration will be ramped up by making better use of risk analysis, progress in cleansing the tax registry, and better use of penalties (adding about 0.1 percent of GDP relative to the outturn in FY 2017/18). Dividends (especially from state-owned enterprises (SOEs) and statutory bodies) will be reinforced and fees and charges will be raised to maintain their real values and progress toward marginal cost pricing (adding about 0.2 percent of GDP relative to the outturn in FY 2017/18).

- On the spending side, cuts to goods and services will target non-priority spending (mostly internal travel, motor vehicle purchases, and office supplies). Domestically-financed capital spending will be better aligned with implementation capacity. Efforts will also be made to raise its efficiency. Subsidies to SOEs and statutory bodies will be reduced in tandem with

improvements in their revenue generating capacity. Current social assistance programs and the two-tier electricity tariff structure are expected to mitigate the impact of electricity and fuel price increases on the most vulnerable.[4] The authorities are also considering a freeze on replacement hiring.

- In addition to tightening the deficit, the approved FY 2018/19 budget introduced measures to benefit low income earners through an increase in the income tax threshold for the lowest tax bracket, increased spending on goods and services to ensure safety during elections, more student loans, an additional 5 percent wage increase (relative to the program request which already incorporated a 15 percent increase) for government employees in the bottom half of the wage scale, and hiring of new medical workers.

- The risk of food insecurity will be addressed through increased FISP spending—budgeted to rise in line with the number of vulnerable households—and ADMARC's strategic grain reserves (which have no impact on the budget).

Text Table 2. Central Government Operations
(FY 2017/18-2019/20, Percent of GDP)[1]

	FY 2017/18			FY 2018/19			FY 2019/20		
	Prog.	Est.	Change	Prog.	Proj.	Change	Prog.	Proj.	Change
Revenue									
Tax and nontax revenue	19.5	19.8	0.3	19.5	20.2	0.8	19.5	20.0	0.6
Budget support and dedicated grants	1.0	0.5	-0.5	2.2	1.1	-1.2	1.1	2.1	1.1
Project grants	1.8	0.9	-0.9	0.9	1.3	0.4	1.6	1.4	-0.2
Spending									
Wages	6.6	6.7	0.1	7.0	7.4	0.4	7.0	7.4	0.4
Generic goods and services	2.7	2.7	0.0	2.4	2.3	-0.2	2.4	2.4	0.1
Elections	0.2	0.6	0.4	0.6	1.0	0.3	0.1	0.0	0.0
Social spending & FISP	2.4	2.6	0.2	2.3	2.4	0.2	2.3	2.5	0.2
Transfers to public entities	2.3	2.2	-0.1	1.3	1.2	-0.1	1.3	1.3	-0.1
Arrears	1.3	1.6	0.3	0.1	0.1	0.0	0.1	0.1	0.0
Interest	4.0	4.0	0.0	3.5	3.9	0.5	2.8	3.8	1.1
Other current spending	3.5	3.9	0.4	3.0	3.1	0.1	3.0	3.1	0.1
Development spending									
Foreign financed	4.8	3.1	-1.6	4.1	3.7	-0.4	3.8	3.7	-0.1
Domestically financed	1.9	1.7	-0.2	1.7	1.4	-0.3	2.0	2.0	0.0
Discrepancy	0.3	-0.4	-0.7	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-7.0	-8.4	-1.3	-3.4	-3.9	-0.5	-2.6	-2.7	-0.2
Primary balance (excluding budget support and dedicated grants)	**-4.0**	**-4.9**	**-0.8**	**-2.2**	**-1.1**	**1.1**	**-0.9**	**-1.0**	**-0.2**

[1]Due to rounding, the difference between figures in "Est." vs. "Prog." Or "Proj." vs "Prog." can differ from "Change" by one decimal place.

Sources: Malawian authorities; IMF staff estimates.

[4] The most vulnerable households use minimal fuel and electricity. For example, less than 5 percent of the rural population and less than half the urban population have access to electricity (World Development Indicators, 2018). Public transport costs remain broadly unchanged.

17. Over the medium term, the fiscal path will be strengthened to secure debt sustainability (MEFP ¶16, ¶30-31).

- The new Low-Income Country Debt Sustainability Framework (LIC DSF), carried out jointly by the staffs of the IMF and World Bank (Annex II: Debt Sustainability Analysis), indicates Malawi is at moderate risk of external debt distress and high overall risk of debt distress—driven by its growing public domestic debt.[5] Stress tests highlight vulnerabilities of total public debt to exogenous shocks, especially export revenues, exchange rate, weather-related, and contingent liabilities. This reflects the country's narrow export base, heavy reliance on rain-fed irrigation, as well as currently limited coverage of public debt arising from weak SOE oversight and monitoring.

- To ensure progress toward debt sustainability, future primary balances (excluding budget support and dedicated grants) will be tightened by an average of 0.2 percent of GDP relative to program request—reducing public debt from 55 percent of GDP to below 40 percent of GDP by 2028.

- The authorities have suspended the contracting of new non-concessional external debt. To maintain debt sustainability, the authorities prefer that under the program, exceptions only be considered in the context of later reviews on a case-by-case basis for new loans backing priority growth-enhancing projects—accompanied by independent third-party feasibility studies (including cost-benefit analysis) and fiscal measures, such as strengthened debt and project management, and that would be consistent with maintaining a moderate risk of external debt distress and the programmed fiscal path.

18. The authorities are seeking to balance the composition of the medium-term fiscal adjustment across spending and revenues. It was agreed that it in order to maintain, or even expand, space for growth-enhancing spending, that revenue efforts should be stepped up (MEFP ¶20). To this end, the authorities are considering a mix of tax policy measures (streamlining various tax incentives, expanding the VAT base and improving SME taxation) and tax administration measures (rollout of the Integrated Tax Administration System, and improving tax compliance). These measures, if implemented, should increase the tax-to-GDP ratio by about 1 percent of GDP by FY 2022/23 and will support a better business environment through strengthened transparency and reduced corruption.

19. The automatic fuel pricing mechanism should be implemented more forcefully to contain fiscal risks (MEFP ¶33-35)**.** Under this mechanism, which eliminated government subsidies, import price changes outside a ±5 percent threshold trigger domestic price changes. Any changes within the threshold are absorbed by the Price Stabilization Fund (PSF). However, since October 2016, the PSF has been subsidizing fuel distributors for almost all price changes. To safeguard the PSF, petroleum and diesel prices were increased this year. Staff urged the authorities to regularly

[5] Under the previous framework and reflecting staff judgement, Malawi was assessed to be at moderate risk of external debt distress, augmented by significant risks stemming from elevated domestic public debt.

implement the automatic pricing mechanism and to increase transparency by disclosing the PSF's financial statement. Staff and the authorities agreed that changes to the fuel import regime should also be transparent and include stakeholder consultations.

20. Enhanced SOE oversight will also be critical to containing fiscal risks (MEFP ¶18). Following last year's large bailout of ADMARC (agricultural developer and marketer), other SOEs are asking for the same. Weak oversight and poor financial reporting prevent proper analysis of SOE risks to public debt. To improve oversight and reporting, the authorities will issue regulations, policies, and guidelines for SOE monitoring (including their financial positions) and develop a prototype SOE database. A pilot audit of the largest SOEs will be submitted to Parliament as well as a published consolidated annual report on SOEs.

21. The authorities are committed to raising the efficiency and effectiveness of public investment (MEFP ¶19). Investment efficiency and higher project returns are impeded by weaknesses in cost-benefit analysis, project management and implementation, project monitoring and evaluation, cash management, procurement transparency, and data publication. To begin addressing these challenges, the authorities will undertake a pilot ex-post review/performance audit of some major capital projects in collaboration with the National Audit Office (NAO). The usefulness of the Public-Sector Investment Program (PSIP) database as a platform for the oversight and monitoring of investment projects will also be assessed—including an audit of the PSIP database's coverage and the efficiency and timeliness of its processes.

Monetary, Exchange Rate, and Financial Sector Policies

22. Preserving a declining inflation trajectory requires a tight monetary policy stance (MEFP ¶9, 10). Given current inflationary pressures, staff and the authorities agreed that continuing a tight monetary policy stance is appropriate. Operationally, the introduction of a band around the upper limit of reserve money is serving the RBM well. The band's flexibility supports better targeting of interbank rates. The authorities continue to expand capacity in developing high frequency data, liquidity forecasting, and the forecasting and policy analysis system (FPAS) modeling to support an eventual transition toward inflation targeting. The RBM views publication of their communication strategy as a positive step toward enhancing transparency.

23. Greater exchange rate flexibility will be critical to cushioning shocks and enhancing competitiveness (MEFP ¶15)**.** The authorities stressed that their intervention[6] is not intended to stabilize the exchange rate but mainly for accumulating reserves and smoothing the seasonality of FX supply. They pointed to the shallowness of the interbank market as the reason banks prefer to transact with the RBM or their own clients. Staff recommended developing a well-sequenced action plan that aims to deepen the interbank market and moderate the RBM's role to dampening excess volatility and accumulating reserves when needed (Box 1). This includes enhanced communication of the RBM's FX intervention objectives and strategies, more timely publication of information on

[6] During the first seven months of the year, the RBM's FX purchases (sales) were nearly 50 percent (40 percent) of total sales (purchases) of authorized dealer banks.

interbank transactions, and more prudent risk management and oversight. The authorities added that a more transparent auction-based system of FX intervention will also be developed.

24. The authorities are committed to strengthening banking resilience and financial sector oversight (MEFP ¶12-14).

- The authorities closely monitor and enforce compliance with prudential norms. The RBM is working with banks to improve their business models and reduce most banks' NPLs to around 5 percent by end-2018 through recovery or write-offs. Staff stressed the importance of improving banks' risk management and analysis of collateral quality. The RBM will continue close monitoring and surveillance of large borrowers and enforcement of the single borrower exposure limit as loan concentration remains a major banking system risk. Regulations aimed at enhancing the consolidated and Domestic Systemically Important Banks supervision will take effect as of end-March 2019. Higher FX lending (from 8 percent in 2012 to 25 percent in August 2018) is being closely monitored and a directive was issued in April 2018 limiting FX lending to borrowers with FX generating activities and to banks' FX deposit balance. The RBM will also ensure that banks meet the net open position requirement.

- The RBM is actively engaging with commercial banks to improve credit to small and medium size enterprises (SMEs) and to develop a roadmap for increasing access to finance. Staff emphasized the importance of simultaneously developing skills in the banking sector, increasing financial literacy, and improving banking system efficiency. By July 2019, the authorities will re-submit to Parliament amendments to the Banking Act of 2010 and Financial Services Act of 2010. The authorities plan to gazette and enact regulations related to the revised AML/CFT framework, enacted in 2017, and have committed to strengthening their asset declaration system and use of AML/CFT tools to improve governance.

B. Advancing Governance Reforms

25. Improving governance and transparency and reducing corruption remains critical to strengthening economic outcomes and bolstering donor confidence. Key areas the authorities are currently advancing include:

- **Bolstering the RBM's independence** by unwinding the RBM's significant holdings of government securities (MEFP ¶11). To this end, the RBM (i) will be submitting to Parliament a new RBM Act 2018 that enhances its autonomy and eliminates avenues for monetization of deficits (ii) has already reduced its holdings of the government's domestic debt by 13 percent between end-2017 and end-August 2018; and (iii) is developing a multi-year unwinding strategy which will be clearly communicated to smooth market reactions.

- **Deepening the domestic debt market** will eliminate the need for monetizing deficits and strengthen the government's debt management framework (MEFP ¶32). Important steps the authorities are undertaking include greater emphasis on developing domestic debt

management and policies in collaboration with the RBM and improving debt and liquidity management coordination.

- **Public Financial Management (PFM)** reforms aim to raise fiscal discipline, transparency, and integrity (MEFP ¶23-27), ultimately helping address the weaknesses in budget control that led to the cashgate scandal. These reforms focus on routinizing fiscal reporting and bank reconciliation, reconciling debt data between the MoF and RBM, strengthening the quality control of monthly fiscal reporting, strengthening cash management and the medium-term budgetary framework, preventing further accumulation of arrears including closing out all transactions pertaining to past arrears, broadening coverage of the current IFMIS, and implementing plans for acquiring a new IFMIS.

PROGRAM MODALITIES AND SAFEGUARDS

26. Malawi's capacity to repay the Fund remains strong (Table 8). Financing assurances are in place for the remainder of the program and Malawi has a solid track record in meeting its obligations to the Fund.

27. Modifications to the program and monitoring. To reflect corrections for the fiscal slippage in FY 2017/18, the updated profile of budget support, and lower than expected growth for 2018, modification of the end-December 2018 PCs for the primary fiscal balance, net international reserves, and reserve money are proposed. To better align IFMIS-related SBs with the budget cycle, these SBs are proposed for the third review instead of the second. New SBs on developing a strategy for the unwinding of RBM holdings of government securities, reforming oversight of SOEs, and improving public investment management are proposed for the second, third and fourth reviews. The program will continue to be reviewed semi-annually based on performance criteria, indicative targets (Table 10), structural benchmarks (Tables 11a, b, and c), and prior actions (Table 12). All prior actions are expected to be met prior to the Board discussion. Targeted technical assistance remains critical to achieving program objectives.

28. An updated safeguards assessment of the RBM was completed in July 2018. It found that the RBM's financial reporting and audit mechanisms continue to adhere to international practices. Nevertheless, risks in the area of foreign reserves management remain elevated due to lapses in oversight and departures from leading practices. Moreover, the RBM's governance arrangements and autonomy are undermined by weak legal provisions, and significant outstanding credit to the government. The key safeguards recommendation to strengthen the RBM's legal framework is a structural benchmark for the first review.

STAFF APPRAISAL

29. Malawi's macroeconomic outlook is positive but downside risks dominate. Growth is expected to rebound next year and strengthen over the medium term, assuming improved infrastructure, better cropping techniques, and increased donor assistance. Single-digit inflation is

anticipated to continue in line with prudent policies and declines in food and international fuel prices. The current account deficit is expected to narrow supported by strengthened competitiveness and fiscal restraint. However, political pressures ahead of elections could weaken reform implementation, governance challenges could further postpone donor support, and adverse weather could harm agriculture.

30. The fiscal position needs to be strengthened to preserve debt sustainability. The program's primary balance target for FY 2018/19 has been tightened to correct for the FY 2017/18 slippage and partially adjust for the postponement of World Bank budget support. The following year's target will be loosened with the arrival of the postponed budget support. Medium-term primary balances need to be tightened to rein in Malawi's growing public debt. Under the new LIC-DSF, Malawi's overall risk of debt distress is assessed as high, while the risk of external debt distress remains medium.

31. Advancing reforms in public investment management and SOE oversight will be critical to containing fiscal risks. Increasing project returns and investment efficiency will also create more space for building growth-enhancing infrastructure. The authorities plan to audit the performance of major capital projects and improve their oversight and monitoring. To begin addressing large contingent liabilities from SOEs, the authorities are formalizing a structure for monitoring them and submitting to Parliament audits of the largest SOEs and an annual report on all SOEs. Staff stressed regular implementation of the automatic fuel pricing mechanism to avoid government subsidies.

32. Improving governance and transparency and reducing vulnerabilities to corruption, especially in PFM, are paramount to improved economic outcomes and catalyzing donor support. Staff welcomes advances in routinizing bank reconciliation but quickly incorporating the salary accounts will be critical. More progress in improving commitment control, cash management, enlarging IFMIS coverage, and a stronger debt management framework are essential for improving fiscal reporting and integrity as well as transparency. A clearly communicated strategy for unwinding RBM holdings of government securities will bolster the RBM's independence. Effective use of AML/CFT tools and an enhanced asset disclosure system would support the authorities' efforts to improve governance.

33. Tight monetary policy is appropriate but greater exchange rate flexibility is needed. Given current inflationary pressures, continued tight monetary policy will preserve the declining inflation trajectory. Greater exchange rate flexibility will be critical to cushioning shocks and enhancing competitiveness. To this end, it will be important to deepen the interbank market, moderate the RBM's role in the market, and develop a more transparent auction-based FX intervention system.

34. Important steps have been taken to improve the resilience of the banking system. The adoption of IFRS9 requirements, RBM's vigilance, and regular stress testing of banks' balance sheets have significantly reduced NPLs and increased provisioning. Looking ahead, it will be important to maintain this momentum and ensure further increases in provisioning from the still low levels. The

RBM should also seek to further improve banks' risk management, analysis of collateral quality, business models, and closely monitor large borrowers and foreign currency lending developments. Efforts to align the AML/CFT framework with international standards should be accelerated.

35. Staff supports the completion of the first review under the ECF and the request for waivers of non-observance for the end-June 2018 QPC on the primary balance and the continuous QPC on not contracting new non-concessional external debt. This recommendation is based on the authorities' commitment to corrective fiscal and debt management measures, strong policy implementation during the second half of 2018, the completion of prior actions for this review, and on the strength of the reform agenda articulated by the authorities in their MEFP.

Proposed Decision

1. Malawi has consulted with the Fund in accordance with paragraph 4(b) of the arrangement for Malawi under the Extended Credit Facility ("ECF") (EBS/18/28, 04/17/18) (the "ECF Arrangement") to review program implementation and to reach understandings regarding the conditions for further disbursements.

2. The letter dated October 30, 2018 from the Minister of Finance, Economic Planning and Development and the Governor of the Reserve Bank of Malawi ("RBM") (the "October 2018 Letter") together with its Memorandum of Economic and Financial Policies (the "October 2018 MEFP") and the Technical Memorandum of Understanding (the "October 2018 TMU") shall be attached to the ECF Arrangement, and the letter dated April 13, 2018 from the Minister of Finance, Economic Planning and Development and the Governor of the RBM, together with all of its attachments, shall be read as supplemented and modified by the October 2018 Letter and its attachments.

3. Accordingly, the ECF Arrangement for Malawi shall be amended as follows:

   a. A new paragraph 2(c) shall be included in the ECF Arrangement to read as follows:

      "2(c) the third disbursement, in an amount equivalent to SDR 11.15 million, will be available on or after April 15, 2019, at the request of Malawi and subject to paragraphs 4 and 5 below."

b. A new paragraph 2(d) shall be included in the ECF Arrangement to read as follows:

"2(d) the fourth disbursement, in an amount equivalent to SDR 11.15 million, will be available on or after October 15, 2019, at the request of Malawi and subject to paragraphs 4 and 5 below."

c. Paragraph 4 of the ECF Arrangement shall be renumbered as "4.A" and paragraph 4.A(a) shall be amended to replace the numbering of (iv) and (v) with (iii) and (iv) respectively, and paragraph 4.A(b) shall be amended to read as follows: "until the Trustee has determined that the first program review referred to in paragraph 42 of the MEFP, has been completed."

d. A new paragraph 4.B of the ECF Arrangement shall be inserted to read as follows:

"B. Malawi will not request the third disbursement under this arrangement specified in paragraph 2(c) above:

(a) if the Managing Director of the Trustee finds that, with respect to the third disbursement, the data as of December 31, 2018 indicate that:

i. the ceiling on reserve money (upper bound);

ii. the floor on the primary balance;

iii. the ceiling on central bank financing of the central government;

iv. the floor on the net international reserves of the central bank,

as set out in Table 1 of the October 2018 MEFP and further specified in the October 2018 TMU was not observed; or

(b) until the Trustee has determined that the second program review referred to in paragraph 38 of the October 2018 MEFP has been completed."

e. A new paragraph 4.C of the ECF Arrangement shall be inserted to read as follows:

"C. Malawi will not request the fourth disbursement under this arrangement specified in paragraph 2(d) above:

(a) if the Managing Director of the Trustee finds that, with respect to the fourth disbursement, the data as of June 30, 2019 indicate that:

i. the ceiling on reserve money (upper bound);

ii. the floor on the primary balance;

iii. the ceiling on central bank financing of the central government;

iv. the floor on the net international reserves of the central bank,

as set out in Table 1 of the October 2018 MEFP and further specified in the October 2018 TMU was not observed; or

(b) until the Trustee has determined that the third program review referred to in paragraph 38 of the October 2018 MEFP has been completed."

f. Paragraph 5 shall be amended to replace the words "Table 1 of the MEFP and further specified in the TMU" with "Table 1 of the October 2018 MEFP and further specified in the October 2018 TMU".

g. Paragraph 7 shall be amended to replace the words "Paragraph 6 of the Letter" with "Paragraph 8 of the October 2018 Letter".

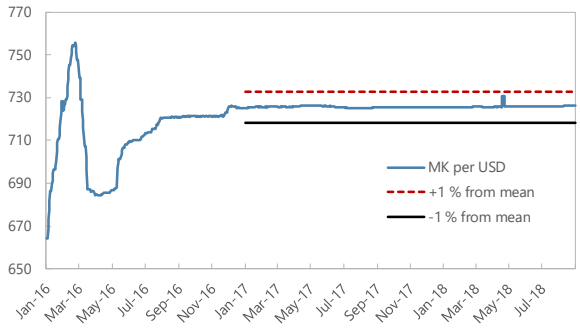
4. The Fund decides that the first review specified in paragraph 4.A(b) is completed, and that Malawi may request the second disbursement referred to in paragraph 2(b) of the ECF

Arrangement, notwithstanding the nonobservance of the end-June performance criterion on the primary balance, and of the continuous performance criterion on the ceiling on contracting new non-concessional external debt, specified in paragraphs 4.A(a)(ii) and 5(b) of the ECF Arrangement, respectively, on the condition that the information provided by Malawi on the performance under these criteria is accurate, and on the further condition that the information provided by Malawi on the implementation of the measures specified as prior actions in Table 2 of the October 2018 MEFP is accurate (EBS/18/96, 11/6/18).

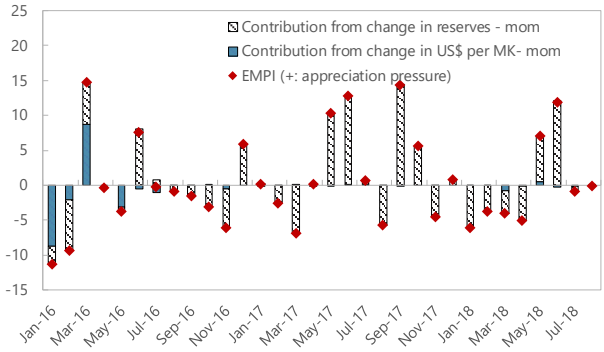
Box. 1 Exchange Rate Super-Stability in Malawi

The super-stability of the Kwacha against the U.S. Dollar can be explained by limited price discovery in Malawi's interbank FX market. Since August 2016, the exchange rate fluctuated within a narrow band of +/- 1 percent with market pressures fully borne by reserve changes (text figures). This is due to pricing being determined in the segmented and underdeveloped interbank FX market. In contrast, most transactions occur in the retail market as well as directly with the RBM—neither of which contribute to price formation in the interbank market. Activity in the retail FX market reflects the concentration of FX liquidity among a handful of corporate clients who trade directly with commercial banks. The RBM also intervenes by accumulating reserves when FX inflows peak and supplying FX to commercial banks during the lean season to limit market speculation.

Daily Exchange rate (Malawi Kwacha per USD)



Exchange Market Pressure Index (EMPI)



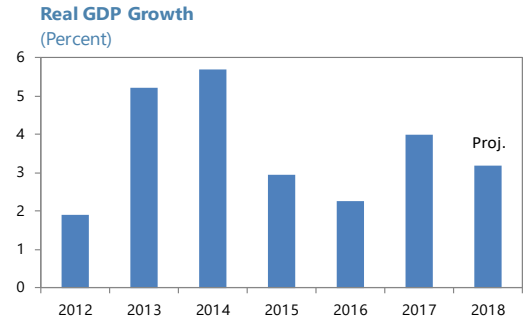
Sources: Malawian authorities and IMF staff calculations.

Promoting a more active interbank FX market would support greater exchange rate flexibility. To this end, the market should be gradually developed and the RBM's role moderated by addressing the following challenges. First, frequent RBM interventions on both sides obscures the objectives and strategy of the RBM's FX intervention, which could confuse market players and demotivate trade amongst themselves. Second, the interbank market relies on the previous day's traded prices and phone calls for guidance on the intraday market quotes with limited visibility of same-day transaction prices or volumes.[1] Third, the market is severely segmented between large and small banks, foreign and local banks, with FX liquidity trapped in different pockets—reducing trust among commercial banks to trade with each other.

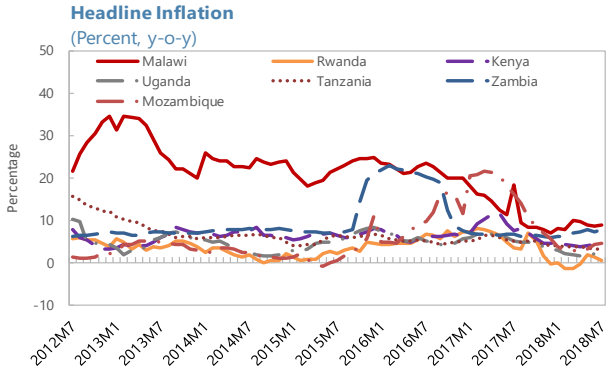
[1] Aide-Memoire, Malawi monetary and foreign exchange operations and repo market development, East AFRITAC, July 2017.

Figure 1. Malawi: Recent Economic Developments, 2012–18

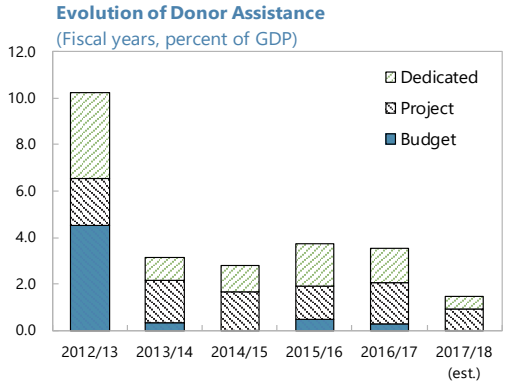
Real GDP growth is expected to moderate to 3.2 percent in 2018 after a rebound in 2017.



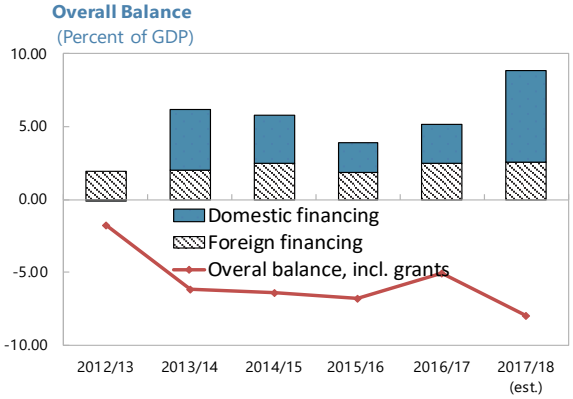
Headline inflation picked up slightly in 2018H1, and remains high compared to neighboring countries.



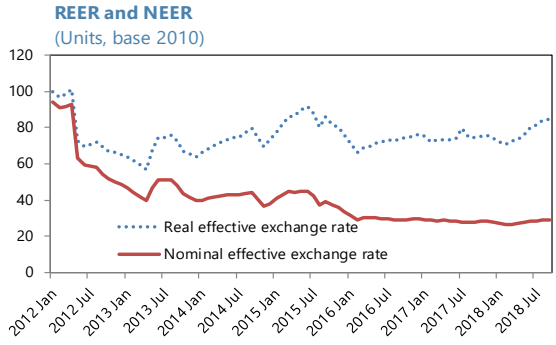
Donor assistance has been affected by the cashgate scandal since 2013/14, and was particularly low for 2017/18.



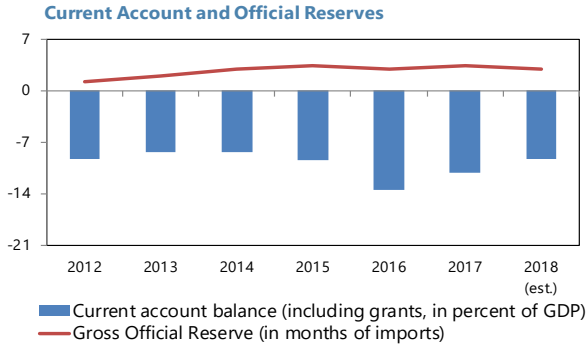
Fiscal stance became expansionary in second half of 2017/18.



The REER has remained broadly stable since 2016 reflecting stability of the NEER.



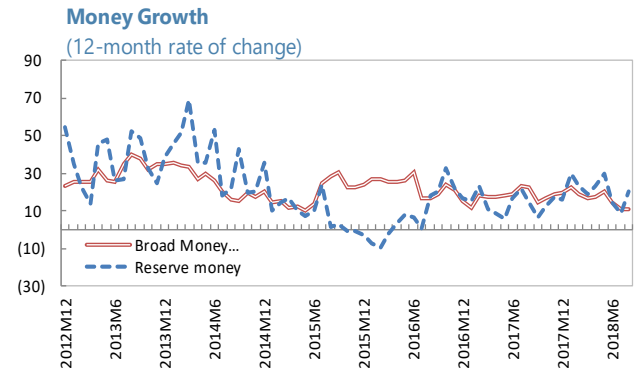
The current account deficit improved somewhat due to lower project-related imports.



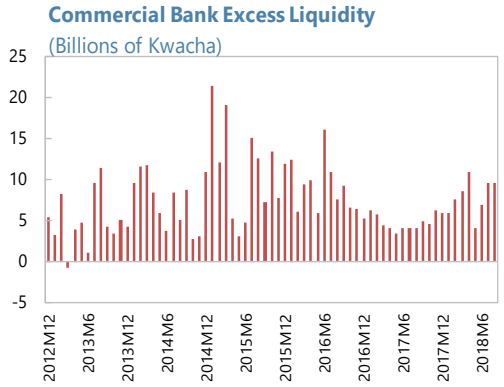
Sources: Malawian authorities; IMF staff estimates.

Figure 2. Malawi: Recent Monetary Developments, 2012–18

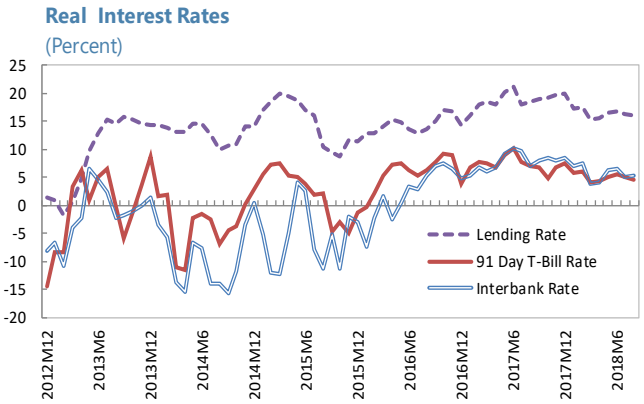
The broad money growth trend was reversed in mid-2015, mostly due to the valuation effect of a depreciating Kwacha.



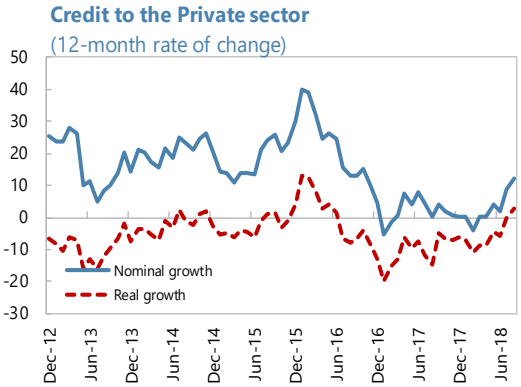
Active liquidity management has succeeded in reducing excess liquidity in the banking system since mid-2016.



Average real prime lending rate has remained elevated...



...which contributed to keeping credit growth weak in real terms since mid-2012.



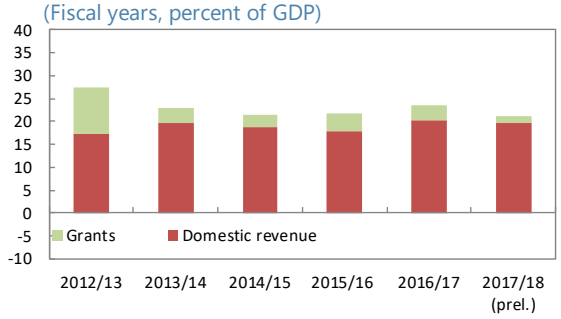
Sources: Malawian authorities; IMF staff estimates.

Figure 3. Fiscal Developments and Outlook, 2012–18

In 2018, domestic revenue remained high while grants received were lower than previous years.

Total Government Revenue

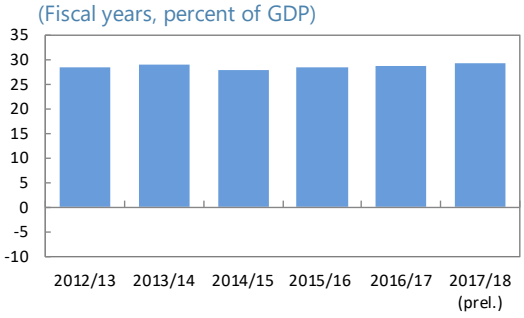
(Fiscal years, percent of GDP)



Total spending in 2017/18 was higher than previous years, despite lower development spending...

Total Government Expenditure

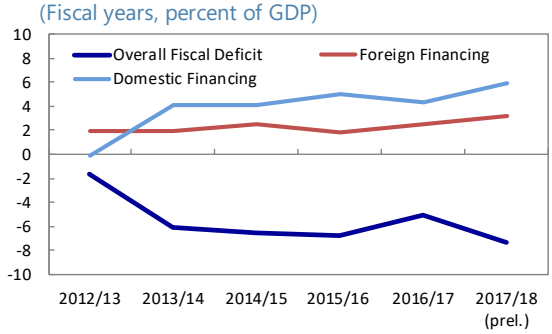
(Fiscal years, percent of GDP)



...which increased fiscal finnacing needs met by foreign and private domestic financing...

Central Government Financing

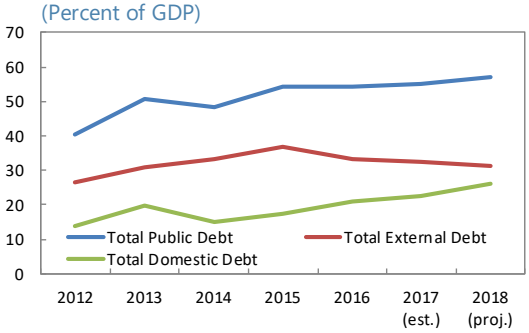
(Fiscal years, percent of GDP)



...and increased domestic public debt.

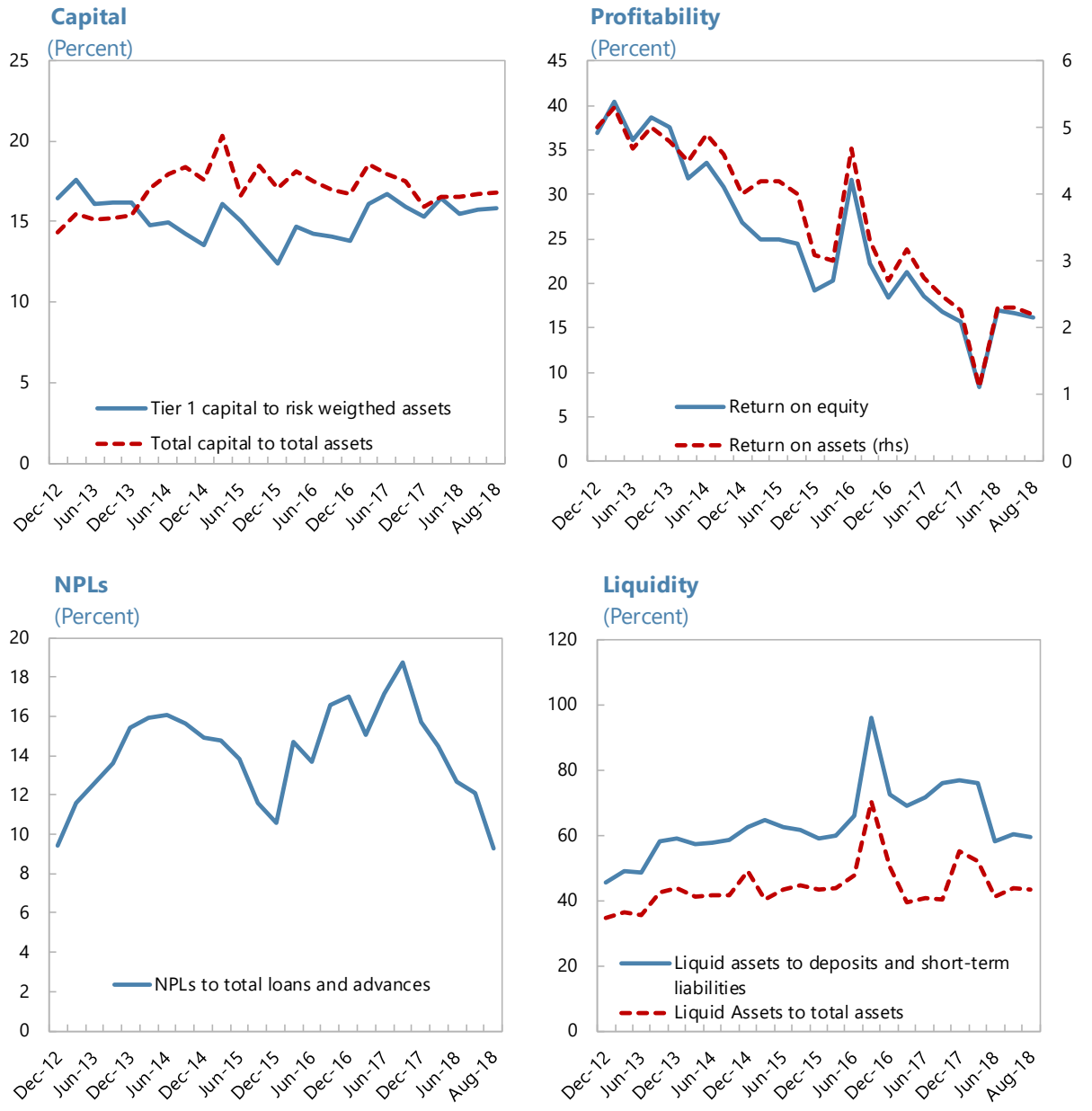
Public Debt

(Percent of GDP)



Sources: Malawian authorities; IMF staff estimates.

Figure 4. Malawi: Selected Financial Stability Indicators, 2012–18



Sources: Malawian authorities; IMF staff estimates.

Table 1. Malawi: Selected Economic Indicators, 2016–23

	2016	2017	2018		2019		2020	2021	2022	2023
	Est.		Prog.	Proj.	Prog.	Proj.	Proj.			
National accounts and prices (percent change, unless otherwise indicated)										
GDP at constant market prices	2.3	4.0	3.5	3.2	4.5	4.0	5.0	5.5	6.0	6.5
Nominal GDP (billions of Kwacha)	3,910	4,503	5,068	5,007	5,654	5,625	6,341	7,112	7,947	8,852
GDP deflator	19.5	10.7	8.8	7.8	6.8	8.0	7.4	6.3	5.4	4.6
Consumer prices (end of period)	20.0	7.1	9.0	9.5	7.5	8.9	7.6	6.5	6.1	5.0
Consumer prices (annual average)	21.7	11.5	10.4	9.1	7.6	9.0	8.2	7.0	6.0	5.0
Investment and savings (percent of GDP)										
National savings	-2.3	2.3	4.4	1.9	4.8	4.7	5.2	5.5	5.8	6.3
Gross investment	10.8	13.5	13.4	11.3	12.9	12.3	13.1	13.3	13.5	13.9
Government	4.4	6.7	6.5	4.8	6.0	5.4	6.0	6.2	6.4	6.6
Private	6.4	6.8	6.8	6.5	7.0	6.9	7.1	7.1	7.2	7.2
Saving-investment balance	-13.0	-11.1	-8.9	-9.3	-8.1	-7.6	-7.9	-7.7	-7.7	-7.6
Central government (percent of GDP on a fiscal year basis)[1]										
Revenue	21.7	23.6	22.4	21.3	22.6	22.6	23.5	23.0	23.5	23.8
Tax and nontax revenue	18.0	20.1	19.5	19.8	19.5	20.2	20.0	20.2	20.5	21.0
Grants	3.7	3.5	2.8	1.5	3.1	2.3	3.5	2.8	2.9	2.9
Expenditure and net lending	28.5	28.7	29.7	29.2	26.0	26.5	26.3	26.2	26.5	26.8
Overall balance (excluding grants)	-10.5	-8.6	-10.1	-9.4	-6.5	-6.3	-6.2	-6.0	-5.9	-5.8
Overall balance (including grants)	-6.8	-5.1	-7.3	-7.9	-3.4	-3.9	-2.7	-3.2	-3.0	-2.9
Foreign financing	1.9	2.5	3.2	2.6	1.3	0.6	1.9	1.6	1.8	1.8
Total domestic financing	5.0	4.3	5.9	7.8	3.1	4.8	0.9	1.6	1.2	1.1
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Discrepancy	0.3	0.0	0.3	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Primary balance	-2.8	-0.6	-3.0	-4.3	0.1	0.0	1.1	0.4	0.4	0.4
Primary balance (excluding budget support and dedicated grants)	-4.3	-2.4	-4.0	-4.9	-2.2	-1.1	-1.0	-0.6	-0.6	-0.6
Money and credit (change in percent of broad money at the beginning of the period, unless otherwise indicated)										
Money and quasi money	15.2	19.7	12.6	11.9	11.6	12.3	12.7	12.1	11.9	11.5
Net foreign assets	2.1	11.1	-0.6	-11.5	4.7	7.4	10.4	12.2	12.6	13.5
Net domestic assets	13.1	8.5	13.2	23.5	6.8	4.9	2.3	0.0	-0.8	-2.0
Credit to the government	17.5	21.3	4.1	9.8	3.0	2.9	1.8	1.5	1.1	0.5
Credit to the private sector (percent change)	4.6	0.4	4.1	8.0	6.7	10.1	12.5	13.3	14.4	15.3
External sector (US$ millions, unless otherwise indicated)										
Exports (goods and services)	1,603	1,667	1,857	1,844	1,975	1,982	2,111	2,247	2,394	2,565
Imports (goods and services)	2,505	2,592	2,747	2,695	2,769	2,846	2,975	3,157	3,375	3,611
Gross official reserves	605	758	703	695	755	791	936	1,099	1,260	1,453
(months of imports)	2.8	3.4	3.0	2.9	3.1	3.2	3.6	3.9	4.2	4.5
(percent of reserve money)	183.2	198.9	175.2	164.5	178.3	178.2	198.8	218.9	233.5	251.3
Current account (percent of GDP)	-13.0	-11.1	-8.9	-9.3	-8.1	-7.6	-7.9	-7.7	-7.7	-7.6
Current account, excl. official transfers (percent of GDP)	-13.0	-11.4	-10.1	-9.3	-8.1	-8.7	-7.9	-7.7	-7.7	-7.6
Current account, excl. project related imports (percent of GDP)	-9.8	-7.8	-6.0	-7.1	-5.2	-4.8	-4.7	-4.4	-4.4	-4.2
Current account, excl. official transfers and project related imports (percent of GDP)	-9.7	-8.0	-7.2	-7.1	-5.2	-5.9	-4.7	-4.4	-4.4	-4.2
Real effective exchange rate (percent change)	-13.3	2.9	...	...	...	...	...	...	...	...
Overall balance (percent of GDP)	-2.0	2.1	-0.8	-1.0	0.5	1.1	1.7	2.1	2.3	2.4
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Terms of trade (percent change)	-0.1	-3.4	-5.9	-4.1	-1.1	-0.9	0.3	0.3	0.5	0.5
Debt stock and service (percent of GDP, unless otherwise indicated)										
External debt (public sector)	32.0	33.2	32.1	31.2	32.2	31.4	31.5	31.1	30.4	29.9
NPV of Public external debt (percent of exports)	76.3	82.7	74.2	75.7	72.2	74.3	74.1	73.0	71.5	70.0
Domestic public debt	23.5	24.5	22.2	26.1	22.2	24.8	23.8	22.8	21.6	19.9
Total public debt	55.6	57.7	54.3	57.3	54.4	56.1	55.4	54.0	52.0	49.8
External debt service (percent of exports)	12.8	4.3	7.5	7.2	5.4	4.5	4.6	5.0	5.4	5.1
External debt service (percent of revenue excl. grants)	20.2	6.0	10.4	9.5	7.8	6.1	6.3	6.8	7.2	6.7
91-day treasury bill rate (end of period)	24.0	14.7	...	...	...	...	...	...	...	...

Sources: Malawian authorities and IMF staff estimates and projections.

[1] The fiscal year starts in July and ends in June. The current fiscal year, 2018, runs from July 1, 2018 to June 30, 2019.

Table 2a. Malawi: Central Government Operations, 2016/17–22/23

(Billions of Kwacha)

	2016/17	2017/18			2018/19			2019/20		2020/21	2021/22	2022/23
		Approved Budget	Program	Est.	Approved Budget	Program	Proj.	Program	Proj.	Proj.		
Revenue	989	1,140	1,065	1,007	1,264	1,206	1,194	1,318	1,402	1,542	1,758	1,994
Tax and nontax revenue	841	993	931	937	1,067	1,039	1,070	1,158	1,194	1,355	1,541	1,755
Tax Revenue	750	901	839	830	940	940	956	1,048	1,076	1,222	1,391	1,588
Taxes on income and profits	383	477	422	419	477	477	481	531	541	615	700	799
Taxes on goods and services	308	362	354	353	402	401	407	447	458	520	592	676
Taxes on international trade	70	79	75	76	78	84	89	93	101	114	130	149
Other taxes	-11	-17	-13	-18	-17	-21	-21	-23	-24	-27	-31	-35
Nontax revenue	91	92	92	107	127	99	114	110	118	133	149	166
Grants	148	148	134	70	197	167	123	160	208	187	218	240
Budget support grants	12	56	0	0	60	60	0	0	60	0	0	0
Project grants	74	59	87	44	74	48	67	98	83	116	140	155
Dedicated grants	62	33	48	26	63	59	56	63	65	71	78	85
Expenditure and net lending	1,201	1,336	1,414	1,384	1,488	1,387	1,402	1,472	1,566	1,756	1,986	2,239
Current expenditure	924	979	1,093	1,152	1,132	1,075	1,125	1,124	1,215	1,357	1,517	1,683
Wages and salaries	265	310	315	316	394	375	390	418	439	494	553	617
Interest payments	185	177	190	190	183	185	208	165	228	243	261	277
Domestic	173	163	176	177	169	169	189	146	211	224	239	253
Foreign	12	14	14	14	14	16	19	18	17	20	22	25
Goods and services	251	291	289	327	336	298	306	300	305	354	411	466
Generic goods and services	96	128	130	130	130	130	120	141	145	163	183	204
Census	0	3	3	3	6	5	6	6	0	0	0	0
Road maintenance and storage levey expenses	26	18	20	28	32	22	22	25	24	27	30	33
Agricultural sector	4	5	7	7	7	6	7	8	9	11	13	14
Health sector	37	37	36	40	45	43	43	52	57	70	87	102
Education sector	24	25	25	25	28	29	29	35	39	49	60	70
National / local elections	1	11	10	30	51	34	51	4	2	2	3	0
Statutory expenditures	5	2	2	4	2	3	2	3	2	2	2	3
Maize purchases and winter cropping program	31	35	25	35	20	10	10	10	10	11	13	15
Rural electrification	20	12	18	22	15	15	15	16	16	18	21	23
Subsidies and other current transfers	160	196	237	242	215	214	217	237	239	262	287	317
Pension and gratuities	52	69	69	76	81	82	81	92	91	102	114	127
Transfers to road and revenue authorities	23	27	25	25	28	28	29	31	32	37	42	48
Transfers to public entities and households	56	68	110	106	66	71	66	80	76	85	95	107
Fertilizer and seed subsidy	29	33	33	35	41	33	41	34	40	38	35	36
Of which: seed subsidy	1	7	5	7	11	5	11	6	13	13	13	16
Arrears payments[1]	62	4	62	77	4	4	4	4	4	5	6	6
of which: Issuance of zero interest promissory notes for securiti	59	0	58	73	0	0	0	0	0	0	0	0
Development expenditure	274	353	317	227	349	308	270	345	343	392	467	554
Foreign financed	246	218	228	149	219	218	197	226	223	256	312	347
Domestically financed	28	135	89	78	130	90	73	119	120	136	155	207
Net lending	3.5	4	4	4	8	4	8	3	7	7	2	1
Overall balance (including grants)	-212	-196	-349	-376	-225	-181	-208	-153	-164	-214	-227	-244
Discrepancy	0	0	14	-19	0	0	0	0	0	0	0	0
Overall balance (incl. grants and discrepancy)	-212	-196	-335	-395	-225	-181	-208	-153	-164	-214	-227	-244
Overall balance[2]	-152	-196	-277	-323	-225	-181	-208	-153	-164	-214	-227	-244
Total financing (net)	212	196	335	395	225	181	208	154	165	214	227	244
Foreign financing (net)	104	167	155	122	41	71	32	114	112	107	135	151
Borrowing	128	196	183	150	82	107	79	155	154	157	192	215
Budget support loans	0	60	63	65	0	0	0	0	0	0	0	0
Project loans	106	125	100	82	79	107	79	127	140	140	172	192
Other external loans[3]	22	11	20	2	3	0	0	28	14	17	20	24
Amortization	-25	-29	-28	-27	-40	-36	-47	-41	-43	-50	-58	-64
Sale of non-financial assets (privatization proceeds)	11	0	0	0	0	0	0	0	0	0	0	0
Net issuance of promissory notes for securitizing domestic arrears	-15	0	-45	-25	0	-54	-78	0	0	0	0	0
Net domestic financing (NDF)	111	28	225	298	183	164	254	40	54	107	93	93
of which: RBM financing of central government	172		69	-43		0	0	0	0	0	0	0
Financing gap	0	0	0	0	0	0	0	0	-1	0	0	0
Memorandum items:												
Issuance of promissory notes for securitizing domestic arrears	59	0	58	73	0	0	0	0	0	0	0	0
Primary balance (including grants and discrepancy)	-27	-18	-145	-205	-42	4	0	11	65	29	34	33
Primary balance (excluding budget support and dedicated grants)	-101	-107	-193	-231	-164	-115	-56	-51	-61	-42	-44	-52
Adjusted primary balance (including grants and discrepancy)[4]			-163									
Domestic fiscal balance[5]	-111	-121	-252	-293	-195	-128	-127	-85	-142	-138	-131	-136
Maturing promissory notes for domestic arrears	74	0	103	98	0	54	78	0	0	0	0	0
NDF adjusted for payment of arrears	37	28	123	200	183	111	176	40	54	107	93	93
Nominal GDP (fiscal year)	4,183	4,735	4,764	4,735	5,292	5,339	5,292	5,953	5,956	6,697	7,497	8,365

Sources: Malawi Ministry of Finance and IMF staff projections.

[1] This includes promissory notes issued for the repayment of domestic arrears accumulated before FY2014/15.

[2] Excludes issuance of promissory notes for securitization of arrears.

[3] Other external loans include program loans other than budgetary support.

[4] Adjusted primary balance is calculated by subtracting shortfalls in budget support grants, dedicated grants, and budget support loans, as well as increase in debt service payments to WB and AfDB.

[5] Domestic fiscal balance is calculated by subtracting current and domestically-financed development expenditures from domestic revenues.

Table 2b. Malawi: Central Government Operations, 2016/17–22/23

(Percent of GDP)

	2016/17	2017/18			2018/19			2019/20		2020/21	2021/22	2022/23
		Approved Budget	Program	Est.	Approved Budget	Program	Proj.	Program	Proj.		Proj.	
Revenue	23.6	24.1	22.4	21.3	23.9	22.6	22.6	22.1	23.5	23.0	23.5	23.8
Tax and nontax revenue	20.1	21.0	19.5	19.8	20.2	19.5	20.2	19.5	20.0	20.2	20.5	21.0
Tax Revenue	17.9	19.0	17.6	17.5	17.8	17.6	18.1	17.6	18.1	18.2	18.6	19.0
Taxes on income and profits	9.2	10.1	8.9	8.9	9.0	8.9	9.1	8.9	9.1	9.2	9.3	9.6
Taxes on goods and services	7.4	7.6	7.4	7.4	7.6	7.5	7.7	7.5	7.7	7.8	7.9	8.1
Taxes on international trade	1.7	1.7	1.6	1.6	1.5	1.6	1.7	1.6	1.7	1.7	1.7	1.8
Other taxes	-0.3	-0.4	-0.3	-0.4	-0.3	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Nontax revenue[1]	2.2	1.9	1.9	2.3	2.4	1.8	2.2	1.8	2.0	2.0	2.0	2.0
Grants	3.5	3.1	2.8	1.5	3.7	3.1	2.3	2.7	3.5	2.8	2.9	2.9
Budget support grants	0.3	1.2	0.0	0.0	1.1	1.1	0.0	0.0	1.0	0.0	0.0	0.0
Project grants	1.8	1.3	1.8	0.9	1.4	0.9	1.3	1.6	1.4	1.7	1.9	1.9
Dedicated grants	1.5	0.7	1.0	0.5	1.2	1.1	1.1	1.1	1.1	1.1	1.0	1.0
Expenditure and net lending	28.7	28.2	29.7	29.2	28.1	26.0	26.5	24.7	26.3	26.2	26.5	26.8
Current expenditure	22.1	20.7	23.0	24.3	21.4	20.1	21.3	18.9	20.4	20.3	20.2	20.1
Wages and salaries	6.3	6.5	6.6	6.7	7.4	7.0	7.4	7.0	7.4	7.4	7.4	7.4
Interest payments	4.4	3.7	4.0	4.0	3.5	3.5	3.9	2.8	3.8	3.6	3.5	3.3
Domestic	4.1	3.5	3.7	3.7	3.2	3.2	3.6	2.5	3.5	3.3	3.2	3.0
Foreign	0.3	0.3	0.3	0.3	0.3	0.3	0.4	0.3	0.3	0.3	0.3	0.3
Goods and services	6.0	6.2	6.1	6.9	6.3	5.6	5.8	5.0	5.1	5.3	5.5	5.6
Generic goods and services	2.3	2.7	2.7	2.7	2.5	2.4	2.3	2.4	2.4	2.4	2.4	2.4
Road maintenance and storage levy expenses	0.6	0.4	0.4	0.6	0.6	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Agricultural sector	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2
Health sector	0.9	0.8	0.8	0.8	0.9	0.8	0.8	0.9	1.0	1.1	1.2	1.2
Education sector	0.6	0.5	0.5	0.5	0.5	0.5	0.6	0.6	0.7	0.7	0.8	0.8
National / local elections	0.0	0.2	0.2	0.6	1.0	0.6	1.0	0.1	0.0	0.0	0.0	0.0
Statutory expenditures	0.1	0.0	0.0	0.1	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0
National AIDS Commission	0.2	0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Maize purchases and winter cropping programs	0.7	0.7	0.5	0.7	0.4	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Rural electrification	0.5	0.3	0.4	0.5	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Subsidies and other current transfers	3.8	4.1	5.0	5.1	4.1	4.0	4.1	4.0	4.0	3.9	3.8	3.8
Pension and gratuities	1.2	1.4	1.4	1.6	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Transfers to road and revenue authorities	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.6	0.6
Transfers to public entities	1.3	1.4	2.3	2.2	1.2	1.3	1.2	1.3	1.3	1.3	1.3	1.3
Fertilizer and seed subsidy	0.7	0.7	0.7	0.7	0.8	0.6	0.8	0.6	0.7	0.6	0.5	0.4
Of which: seed subsidy	0.0	0.2	0.1	0.2	0.2	0.1	0.2	0.1	0.2	0.2	0.2	0.2
Arrears payments[1]	1.5	0.1	1.3	1.6	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
of which: Issuance of zero interest promissory notes for securitizing domestic ar	1.4	0.0	1.2	1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Development expenditure	6.5	7.5	6.6	4.8	6.6	5.8	5.1	5.8	5.8	5.8	6.2	6.6
Foreign financed	5.9	4.6	4.8	3.1	4.1	4.1	3.7	3.8	3.7	3.8	4.2	4.1
Domestically financed	0.7	2.8	1.9	1.7	2.5	1.7	1.4	2.0	2.0	2.0	2.1	2.5
Net lending	0.1	0.1	0.1	0.1	0.2	0.1	0.2	0.1	0.1	0.1	0.0	0.0
Overall balance (including grants)	-5.1	-4.1	-7.3	-7.9	-4.2	-3.4	-3.9	-2.6	-2.7	-3.2	-3.0	-2.9
Discrepancy	0.0	0.0	0.3	-0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (including grants and discrepancy)	-5.1	-4.1	-7.0	-8.4	-4.2	-3.4	-3.9	-2.6	-2.7	-3.2	-3.0	-2.9
Overall balance[2]	-3.6	-4.1	-5.8	-6.8	-4.2	-3.4	-3.9	-2.6	-2.7	-3.2	-3.0	-2.9
Total financing (net)	5.1	4.1	7.0	8.4	4.2	3.4	3.9	2.6	2.8	3.2	3.0	2.9
Foreign financing (net)	2.5	3.5	3.2	2.6	0.8	1.3	0.6	1.9	1.9	1.6	1.8	1.8
Borrowing	3.1	4.1	3.8	3.2	1.5	2.0	1.5	2.6	2.6	2.3	2.6	2.6
Budget support loans	0.0	1.3	1.3	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	2.5	2.6	2.1	1.7	1.5	2.0	1.5	2.1	2.4	2.1	2.3	2.3
Other external loans[3]	0.5	0.2	0.4	0.1	0.1	0.0	0.0	0.5	0.2	0.3	0.3	0.3
Amortization	-0.6	-0.6	-0.6	-0.6	-0.8	-0.7	-0.9	-0.7	-0.7	-0.8	-0.8	-0.8
Sale of non-financial assets (privatization proceeds)	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net issuance of promissory notes for securitizing domestic arrears	-0.4	0.0	-0.9	-0.5	0.0	-1.0	-1.5	0.0	0.0	0.0	0.0	0.0
Net domestic financing (NDF)	2.7	0.6	4.7	6.3	3.5	3.1	4.8	0.7	0.9	1.6	1.2	1.1
of which: RBM financing of central government	4.1		1.4	-1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:												
Primary balance (including grants and discrepancy)	-0.6	-0.4	-3.0	-4.3	-0.8	0.1	0.0	0.2	1.1	0.4	0.4	0.4
Primary balance (excluding budget support and dedicated grants)	-2.4	-2.3	-4.0	-4.9	-3.1	-2.2	-1.1	-0.9	-1.0	-0.6	-0.6	-0.6
Adjusted primary balance (including grants and discrepancy)[4]			-3.4									
Domestic fiscal balance[5]	-2.6	-2.6	-5.3	-6.2	-3.7	-2.4	-2.4	-1.4	-2.4	-2.1	-1.8	-1.6
Maturing promissory notes for domestic arrears	1.8	0.0	2.2	2.1	0.0	1.0	1.5	0.0	0.0	0.0	0.0	0.0
NDF adjusted for payment of arrears	0.9	0.6	2.6	4.2	3.5	2.1	3.3	0.7	0.9	1.6	1.2	1.1
Nominal GDP (fiscal year)	4,183	4,735	4,764	4,735	5,292	5,339	5,292	5,953	5,956	6,697	7,497	8,365

Sources: Malawi Ministry of Finance and IMF staff projections.

[1] This includes promissory notes issued for the repayment of domestic arrears accumulated before FY2014/15.

[2] Excludes issuance of promissory notes for securitization of arrears.

[3] Other external loans include program loans other than budgetary support.

[4] Adjusted primary balance is calculated by subtracting shortfalls in budget support grants, dedicated grants, and budget support loans.

[5] Domestic fiscal balance is calculated by subtracting current and domestically-financed development expenditures from domestic revenues.

Table 2c. Malawi: Central Government Quarterly Operations in FY 17/18 and FY 18/19

(Billions of Kwacha)

	2017/18					2018/19				
	Q1	Q2	Q3	Q4	Annual	Q1	Q2	Q3	Q4	Annual
	Act.	Act.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	248.8	234.1	255.5	268.8	1,007.3	298.5	298.5	298.5	298.5	1,193.8
Tax and nontax revenue	225.3	215.3	239.0	257.4	937.1	267.6	267.6	267.6	267.6	1,070.4
Tax revenue	206.4	194.1	207.6	221.7	829.8	239.0	239.0	239.0	239.0	956.1
Taxes on income and profits	102.5	91.9	110.3	114.5	419.2	120.3	120.3	120.3	120.3	481.0
Taxes on goods and services	88.6	88.7	83.4	91.9	352.6	101.7	101.7	101.7	101.7	406.9
Taxes on international trade	18.0	18.8	19.0	20.5	76.2	22.4	22.4	22.4	22.4	89.5
Other taxes	-2.7	-5.2	-5.2	-5.2	-18.3	-5.3	-5.3	-5.3	-5.3	-21.2
Nontax revenue	18.9	21.2	31.5	35.7	107.3	28.6	28.6	28.6	28.6	114.3
Grants	23.5	18.8	16.5	11.4	70.2	30.9	30.9	30.9	30.9	123.4
Budget support grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project grants	15.4	17.5	7.3	4.1	44.3	16.7	16.7	16.7	16.7	67.0
Dedicated grants	8.1	1.3	9.2	7.3	25.9	14.1	14.1	14.1	14.1	56.4
Expenditure and net lending	378.1	356.7	332.2	316.6	1,383.7	354.8	349.4	351.3	346.7	1,402.2
Current expenditure	311.4	296.9	280.6	263.4	1,152.3	285.4	280.0	281.9	277.4	1,124.6
Wages and salaries	76.1	79.4	81.5	79.2	316.2	97.5	97.5	97.5	97.5	390.0
Interest payments	44.5	39.2	57.4	49.2	190.3	52.9	49.9	54.6	51.1	208.4
Domestic	43.4	34.9	55.5	43.0	176.8	47.3	44.2	50.6	47.0	189.2
Foreign	1.1	4.3	1.9	6.2	13.5	5.6	5.7	4.0	4.0	19.3
Goods and services	110.3	85.8	66.2	64.3	326.7	79.9	77.4	74.7	73.7	305.6
Generic goods and services	44.6	38.0	27.8	19.4	129.7	32.6	30.1	28.8	28.8	120.3
Census	1.2	1.5	0.2	0.3	3.2	1.6	1.6	1.6	1.6	6.4
Road Maintenance	6.7	7.5	7.1	6.8	28.0	5.4	5.4	5.4	5.4	21.8
Agricultural sector	1.4	1.4	3.0	1.0	6.7	1.8	1.8	1.8	1.8	7.1
Health sector	9.3	13.2	7.9	9.2	39.6	10.8	10.8	10.8	10.8	43.4
Education sector	8.5	7.4	4.5	5.0	25.5	7.3	7.3	7.3	7.3	29.1
National / local elections	6.9	6.9	7.9	8.3	30.1	12.9	12.9	12.9	12.9	51.5
PFEM	0.2	0.4	0.1	0.0	0.7	0.0	0.0	0.0	0.0	0.0
Statutory expenditures	0.5	0.7	2.3	0.4	3.9	0.4	0.4	0.4	0.4	1.5
National AIDS Commission	1.2	0.4	0.4	0.4	2.3	0.0	0.0	0.0	0.0	0.0
Maize purchases and winter cropping program	19.8	4.9	0.0	10.0	34.7	3.5	3.5	2.0	1.0	10.0
Rural Electrification	10.0	3.6	5.1	3.5	22.3	3.7	3.7	3.7	3.7	14.6
Subsidies and other current transfers	58.8	77.4	64.9	41.2	242.4	54.1	54.1	54.1	54.1	216.6
Pension and gratuities	19.4	16.4	19.1	21.2	76.2	20.2	20.2	20.2	20.2	80.6
Transfers to road and revenue authorities	6.3	6.4	6.3	6.3	25.1	7.2	7.2	7.2	7.2	28.7
Transfers to public entities and households	32.5	45.5	14.3	13.6	105.9	16.5	16.5	16.5	16.5	66.0
Fertilizer and seed subsidy	0.7	9.2	25.3	0.0	35.2	10.3	10.3	10.3	10.3	41.3
Of which: seed subsidy	0.0	1.0	6.2	0.0	7.2	2.8	2.8	2.8	2.8	11.3
Arrears payments[1]	21.6	15.1	10.5	29.5	76.8	1.0	1.0	1.0	1.0	4.0
Of which, issuance of zero-coupon promissory notes	17.9	14.9	10.5	29.5	72.8	0.0	0.0	0.0	0.0	0.0
Development expenditure	64.5	59.8	49.8	53.2	227.3	67.4	67.4	67.4	67.4	269.5
Foreign financed	43.2	40.2	30.6	35.0	149.1	49.1	49.1	49.1	49.1	196.5
Domestically financed	21.3	19.5	19.2	18.3	78.2	18.3	18.3	18.3	18.3	73.0
Net lending	2.2	0.0	1.8	0.0	4.0	2.0	2.0	2.0	2.0	8.0
Overall balance (including grants)	-129.3	-122.5	-76.7	-47.8	-376.4	-56.3	-50.9	-52.8	-48.3	-208.3
Discrepancy	27.4	8.7	-33.0	-22.2	-19.1	0.0	0.0	0.0	0.0	0.0
Overall balance (including grants and discrepancy)	-101.9	-113.9	-109.7	-70.0	-395.5	-56.3	-50.9	-52.8	-48.3	-208.3
Overall balance[2]	**-84.0**	**-98.9**	**-99.2**	**-40.6**	**-322.7**	**-56.3**	**-50.9**	**-52.8**	**-48.3**	**-208.3**
Total financing (net)	101.9	113.9	109.7	70.0	395.5	56.3	50.9	52.8	48.3	208.3
Foreign financing (net)	78.5	12.1	16.3	15.3	122.3	6.2	6.0	10.1	9.9	32.2
Borrowing	81.1	21.4	19.6	27.5	149.7	19.7	19.7	19.7	19.7	78.8
Budget support loans	61.1	1.8	0.4	1.8	65.1	0.0	0.0	0.0	0.0	0.0
Project loans	20.0	18.4	18.0	25.8	82.1	19.7	19.7	19.7	19.7	78.8
Other external loans[3]	0.0	1.3	1.2	0.0	2.5	0.0	0.0	0.0	0.0	0.0
Amortization	-2.6	-9.3	-3.3	-12.2	-27.4	-13.5	-13.7	-9.6	-9.8	-46.6
Net Issuance of promissory notes for securitizing domestic arrears	-2.2	-4.5	-5.8	-12.7	-25.2	-22.7	-14.9	-10.5	-29.5	-77.6
Net domestic financing (NDF)	25.7	106.2	99.1	67.4	298.4	72.9	59.9	53.2	67.9	253.8
of which: RBM financing of central government	-15.1	84.6	0.0	0.0	69.5	0.0	0.0	0.0	0.0	0.0
Financing gap	27.4	8.7	-33.0	-22.2	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Primary balance (including grants and discrepancy)	-57.4	-74.7	-52.2	-20.9	-205.2	-3.5	-1.0	1.8	2.8	0.1
Primary balance (excluding issuance of promissory notes for arrears)	-39.5	-59.7	-41.8	8.6	-132.4	-3.5	-1.0	1.8	2.8	0.1
Domestic fiscal balance [4]	-107.4	-101.1	-60.8	-24.2	-293.5	-36.1	-30.6	-32.5	-28.0	-127.2
Maturing promissory notes for domestic arrears	20.2	19.4	16.2	42.2	98.0	22.7	14.9	10.5	29.5	77.6
NDF adjusted for payment of arrears	5.5	86.8	82.9	25.2	200.5	50.2	44.9	42.7	38.4	176.2
Nominal GDP					4,735					5,292

Sources: Malawi Ministry of Finance and IMF staff estimates.

[1] This includes promissory notes issued for the repayment of domestic arrears accumulated before FY2014/15.

[2] Excludes issuance of promissory notes for securitization of arrears.

[3] Other external loans include program loans other than budgetary support.

[4] Domestic fiscal balance is calculated by subtracting current and domestically-financed development expenditures from domestic revenues.

Table 3a. Malawi: Monetary Authorities' Balance Sheet, 2016–19

(Billions of Kwacha, unless otherwise indicated)

	2016	2017	2018				2019			
	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Dec.
	Act.	Est.	Est.		Proj.		Proj.			
Reserve money	241	279	255	301	295	317	300	336	330	356
Currency outside banks	146	165	147	207	...	...	...	...	...	...
Cash in vault	38	35	27	24	...	...	...	...	...	...
Commercial bank deposits with RBM	56	78	81	70	...	...	...	...	...	...
Net foreign assets (NFA)	225	319	248	315	266	237	247	270	284	319
Foreign assets	439	550	481	546	539	521	532	569	585	634
Foreign liabilities	-214	-231	-234	-231	-273	-284	-286	-299	-301	-315
Net domestic assets	16	-40	7	-15	29	80	53	67	46	37
Credit to government (net)	256	397	419	295	295	295	295	295	295	295
Credit to domestic banks	0	0	0	0	0	0	0	0	0	0
Other items (net)	-240	-437	-411	-309	-266	-215	-242	-228	-390	-258
Open market operations	-227	-401	-395	-283	...	...	...	...	...	...
Others	-12	-36	-16	-26	...	...	...	...	...	...
Memorandum items:										
Money multiplier	3.7	3.9	4.0	3.8	3.8	3.8	3.8	3.8	3.8	3.8
Annual growth of reserve money (percent)	16.8	15.9	18.7	14.2	15.6	13.5	17.6	11.8	12.1	12.3
91-day treasury bill rate	24.0	14.7	14.0	14.1	...	...	...	...	...	...
NFA of the central bank (US$ millions)	310	440	435	435	361	316	324	348	360	398
Foreign assets (US$ millions)	605	758	753	753	732	695	699	734	742	791
Foreign liabilities (US$ millions)	-295	-318	-318	-318	-371	-379	-375	-386	-381	-393

Sources: Reserve Bank of Malawi; and IMF staff projection

Table 3b. Malawi: Monetary Survey, 2016–19

(Billions of Kwacha, unless otherwise indicated)

	2016	2017	2018				2019			
	Dec.	Dec.	Mar.	Jun.	Sept.	Dec.	Mar.	June.	Sept.	Dec.
	Act.	Est.	Est.		Proj.		Proj.			
Money and quasi-money	897	1,074	1,021	1,142	1,119	1,202	1,138	1,276	1,254	1,350
Money	396	503	477	551	...	...	...	...	...	...
Quasi-money	501	572	544	591	...	...	...	...	...	...
Of which: foreign currency deposits	222	234	184	211	...	...	...	...	...	...
Net foreign assets (NFA)	356	455	344	408	359	332	344	368	384	421
Monetary authorities	225	319	248	315	266	237	247	270	284	319
Gross foreign assets	439	550	481	546	539	521	532	569	585	634
Foreign liabilities	-214	-231	-234	-231	-273	-284	-286	-299	-301	-315
Commercial banks (net)	131	137	96	92	94	95	97	98	100	102
Net domestic assets	541	618	676	734	759	870	794	908	869	929
Credit to government (net)	338	529	583	510	619	634	646	666	672	668
Credit to statutory bodies (net)	9	8	4	12	4	4	5	5	5	5
Credit to private sector	408	410	398	428	460	443	418	449	511	487
Other items (net)	-214	-328	-308	-216	-323	-211	-274	-212	-319	-231
Memorandum items:										
Velocity of money (annualized GDP divided by broad money)	4.4	4.2	4.5	4.1	4.4	4.2	4.1	4.4	4.2	4.2
Annual growth of broad money (percent)	15.2	19.7	17.0	14.6	13.2	11.9	11.4	11.8	12.1	12.3
Annual growth of credit to the private sector (percent)	4.6	0.4	0.4	2.1	11.7	8.0	5.0	4.9	11.2	10.1
NFA of the commercial banks (US$ millions)	181.0	188.2	132.9	127.1	127.1	127.1	127.1	127.1	127.1	127.1
Gross foreign assets (US$ millions)	204.2	261.2	163.8	187.2	187.2	187.2	187.2	187.2	187.2	187.2
Foreign liabilities (US$ millions)	-23.2	-73.0	-30.9	-60.2	-60.2	-60.2	-60.2	-60.2	-60.2	-60.2
Foreign currency deposits(US$ millions)	305.2	319.1	251.6	289.3	...	...	...	...	...	...
Nominal GDP (billions of Kwacha)	3,910	4,503	4,606	4,735	4,868	5,007	5,134	5,292	5,454	5,625

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

Table 4a. Malawi: Balance of Payments, 2016–23
(Millions of U.S. dollars, unless otherwise indicated)

	2016	2017	2018		2019		2020	2021	2022	2023
	Est.		Prog.	Proj.	Prog.	Proj.	Proj.			
Current account balance	-709.8	-686.7	-602.9	-637.0	-572.1	-553.3	-604.7	-627.3	-671.0	-708.9
Merchandise trade balance	-595.8	-650.0	-623.2	-590.9	-544.9	-605.3	-608.5	-637.3	-685.9	-730.1
Exports	1,480.3	1,542.0	1,714.9	1,701.9	1,805.8	1,813.8	1,927.3	2,052.7	2,188.6	2,345.4
Of which: Tobacco	578.5	583.9	634.3	586.3	664.5	621.3	655.3	691.1	728.9	772.7
Imports	-2,076.2	-2,192.0	-2,338.0	-2,292.8	-2,350.7	-2,419.1	-2,535.8	-2,690.1	-2,874.5	-3,075.5
Of which: Petroleum	-218.0	-306.7	-188.5	-446.5	-193.3	-477.9	-456.9	-473.7	-497.2	-527.7
Project related	-178.3	-207.1	-197.4	-152.8	-203.3	-201.6	-246.5	-266.7	-289.6	-313.6
Maize	-183.6		-75.0	0.0						
Services balance	-428.9	-410.3	-412.4	-408.0	-401.8	-410.7	-413.8	-441.0	-473.0	-507.3
Interest public sector	-14.7	-14.8	-19.1	-21.6	-20.2	-19.8	-20.9	-22.6	-24.3	-26.3
Other factor payments (net)	-108.1	-120.5	-126.8	-126.4	-132.5	-131.5	-138.1	-145.7	-154.5	-164.6
Nonfactor (net)	-306.1	-275.0	-266.6	-260.1	-249.1	-259.5	-254.9	-272.7	-294.2	-316.3
Receipts	122.5	125.3	142.4	142.0	168.8	167.7	184.1	194.2	205.9	219.2
Payments	-428.7	-400.4	-409.0	-402.1	-417.9	-427.2	-438.9	-466.9	-500.1	-535.6
Unrequited transfers (net)	314.9	373.7	432.7	362.0	374.6	462.7	417.7	451.0	487.9	528.5
Private (net)	315.7	358.4	354.5	362.8	375.5	388.1	418.5	451.9	488.8	529.4
Official (net)	-0.8	15.3	78.2	-0.8	-0.8	74.6	-0.9	-0.9	-0.9	-0.9
Receipts	0.0	16.1	79.1	0.0	0.0	75.5	0.0	0.0	0.0	0.0
Budget support	0.0	16.1	79.1	0.0	0.0	75.5	0.0	0.0	0.0	0.0
Payments	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.9	-0.9	-0.9	-0.9
Capital account balance	497.3	317.3	348.6	282.8	339.4	346.9	400.5	436.3	465.6	505.5
Project and dedicated grants	144.9	188.9	188.0	121.8	165.4	169.7	209.8	232.0	247.2	268.9
Off-budget project support[1]	352.4	128.4	160.7	161.0	174.0	177.2	190.7	204.3	218.3	236.6
Financial account balance	114.3	380.1	201.1	285.6	270.7	288.6	338.4	365.7	403.6	429.6
Medium- and long-term flows (net)	-6.5	207.5	52.5	43.9	107.4	98.8	132.9	137.8	155.5	169.2
Disbursements	130.1	239.9	142.5	117.9	174.7	149.6	188.6	200.1	222.4	240.5
Budget support and other program loans	0.0	86.1	0.0	3.0	0.0	0.0	0.0	0.0	0.0	0.0
Project support	109.8	129.7	115.8	113.3	147.4	140.5	169.4	178.4	198.3	213.6
Other medium-term loans	20.3	24.1	26.7	1.7	27.3	9.1	19.1	21.7	24.1	26.9
Amortization	-136.6	-32.5	-90.0	-74.0	-67.3	-50.9	-55.7	-62.3	-66.9	-71.3
SDR allocation	-3.1	5.3	0.0	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign direct investment and other inflows	170.0	131.5	146.1	134.6	160.7	153.3	177.0	197.8	216.3	231.5
Short-term capital	36.8	48.3	2.4	45.9	2.5	36.6	28.5	30.1	31.8	28.9
Commercial banks net foreign assets	-86.0	-7.2	0.0	61.1	0.0	0.0	0.0	0.0	0.0	0.0
Errors and omissions	-5.0	113.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-106.3	129.9	-53.2	-69.7	38.0	82.2	134.2	174.8	198.1	226.2
Financing	106.3	-129.9	53.2	69.7	-38.0	-82.2	-134.2	-174.8	-198.1	-226.2
Gross reserves (- increase)	65.3	-152.9	54.7	62.6	-52.1	-95.4	-145.1	-163.4	-160.3	-193.6
Liabilities	41.0	23.1	-1.5	7.1	14.1	13.2	10.9	-11.3	-37.8	-32.6
Of which: IMF (net)	51.6	4.8	2.4	2.6	14.6	14.7	12.0	-10.3	-36.8	-32.0
Purchases/drawings	76.4	26.6	31.6	31.5	31.7	31.4	31.5	15.8	0.0	0.0
Repurchases/repayments	24.8	21.8	29.3	29.0	17.1	16.7	19.5	26.2	36.8	32.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Gross official reserves	605.0	757.9	702.7	695.3	754.8	790.7	935.8	1,099.2	1,259.6	1,453.2
Months of imports[2]	2.8	3.4	3.0	2.9	3.1	3.2	3.6	3.9	4.2	4.5
Net international reserves	398.7	533.9	480.2	428.6	518.2	510.8	645.0	819.8	1,017.9	1,244.1
Current account balance (percent of GDP)										
Excluding official transfers	-13.0	-11.4	-10.1	-9.3	-8.1	-8.7	-7.9	-7.7	-7.7	-7.6
Excluding project related imports	-9.8	-7.8	-6.0	-7.1	-5.2	-4.8	-4.7	-4.4	-4.4	-4.2
Excluding official transfers and project related imports	-9.7	-8.0	-7.2	-7.1	-5.2	-5.9	-4.7	-4.4	-4.4	-4.2
Import price index (2005 = 100)	111.4	116.8	124.4	126.8	124.8	127.6	126.9	126.1	125.3	124.7
Import volume (percent change)	4.9	0.4	4.9	-5.4	0.2	4.9	5.4	6.7	7.6	7.5
REER (percent change)	-13.3	2.9	...	...	...	...	...	...	...	...
Terms of trade (percent change)	-0.1	-3.4	-5.9	-4.1	-1.1	-0.9	0.3	0.3	0.5	0.5
Nominal GDP (millions of U.S. dollars)	5,445	6,166	6,746	6,820	7,024	7,257	7,672	8,141	8,696	9,307

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

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

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

Table 4b. Malawi: Balance of Payments, 2016–23
(Percent of GDP)

	2016	2017	2018		2019		2020	2021	2022	2023
		Est.	Prog.	Proj.	Prog.	Proj.		Proj.		
Current account balance	-13.0	-11.1	-8.9	-9.3	-8.1	-7.6	-7.9	-7.7	-7.7	-7.6
Merchandise trade balance	-10.9	-10.5	-9.2	-8.7	-7.8	-8.3	-7.9	-7.8	-7.9	-7.8
Exports	27.2	25.0	25.4	25.0	25.7	25.0	25.1	25.2	25.2	25.2
Of which: Tobacco	10.6	9.5	9.4	8.6	9.5	8.6	8.5	8.5	8.4	8.3
Imports	-38.1	-35.6	-34.7	-33.6	-33.5	-33.3	-33.1	-33.0	-33.1	-33.0
Of which: Petroleum	-4.0	-5.0	-2.8	-6.5	-2.8	-6.6	-6.0	-5.8	-5.7	-5.7
Project related	-3.3	-3.4	-2.9	-2.2	-2.9	-2.8	-3.2	-3.3	-3.3	-3.4
Maize	-3.4		-1.1	0.0						
Services balance	-7.9	-6.7	-6.1	-6.0	-5.7	-5.7	-5.4	-5.4	-5.4	-5.5
Interest public sector	-0.3	-0.2	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Other factor payments (net)	-2.0	-2.0	-1.9	-1.9	-1.9	-1.8	-1.8	-1.8	-1.8	-1.8
Nonfactor (net)	-5.6	-4.5	-4.0	-3.8	-3.5	-3.6	-3.3	-3.3	-3.4	-3.4
Receipts	2.3	2.0	2.1	2.1	2.4	2.3	2.4	2.4	2.4	2.4
Payments	-7.9	-6.5	-6.1	-5.9	-5.9	-5.9	-5.7	-5.7	-5.8	-5.8
Unrequited transfers (net)	5.8	6.1	6.4	5.3	5.3	6.4	5.4	5.5	5.6	5.7
Private (net)	5.8	5.8	5.3	5.3	5.3	5.3	5.5	5.6	5.6	5.7
Official (net)	0.0	0.2	1.2	0.0	0.0	1.0	0.0	0.0	0.0	0.0
Receipts	0.0	0.3	1.2	0.0	0.0	1.0	0.0	0.0	0.0	0.0
Budget support	0.0	0.3	1.2	0.0	0.0	1.0	0.0	0.0	0.0	0.0
Payments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital account balance	9.1	5.1	5.2	4.1	4.8	4.8	5.2	5.4	5.4	5.4
Project and dedicated grants	2.7	3.1	2.8	1.8	2.4	2.3	2.7	2.8	2.8	2.9
Off-budget project support[1]	6.5	2.1	2.4	2.4	2.5	2.4	2.5	2.5	2.5	2.5
Financial account balance	2.1	6.2	3.0	4.2	3.9	4.0	4.4	4.5	4.6	4.6
Medium- and long-term flows (net)	-0.1	3.4	0.8	0.6	1.5	1.4	1.7	1.7	1.8	1.8
Disbursements	2.4	3.9	2.1	1.7	2.5	2.1	2.5	2.5	2.6	2.6
Budget support and other program loans	0.0	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project support	2.0	2.1	1.7	1.7	2.1	1.9	2.2	2.2	2.3	2.3
Other medium-term loans	0.4	0.4	0.4	0.0	0.4	0.1	0.2	0.3	0.3	0.3
Amortization	-2.5	-0.5	-1.3	-1.1	-1.0	-0.7	-0.7	-0.8	-0.8	-0.8
SDR allocation	-0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign direct investment and other inflows	3.1	2.1	2.2	2.0	2.3	2.1	2.3	2.4	2.5	2.5
Short-term capital	0.7	0.8	0.0	0.7	0.0	0.5	0.4	0.4	0.4	0.3
Commercial banks net foreign assets	-1.6	-0.1	0.0	0.9	0.0	0.0	0.0	0.0	0.0	0.0
Errors and omissions	-0.1	1.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-2.0	2.1	-0.8	-1.0	0.5	1.1	1.7	2.1	2.3	2.4
Financing	2.0	-2.1	0.8	1.0	-0.5	-1.1	-1.7	-2.1	-2.3	-2.4
Gross reserves (- increase)	1.2	-2.5	0.8	0.9	-0.7	-1.3	-1.9	-2.0	-1.8	-2.1
Liabilities	0.8	0.4	0.0	0.1	0.2	0.2	0.1	-0.1	-0.4	-0.4
Of which: IMF (net)	0.9	0.1	0.0	0.0	0.2	0.2	0.2	-0.1	-0.4	-0.3
Purchases/drawings	1.4	0.4	0.5	0.5	0.5	0.4	0.4	0.2	0.0	0.0
Repurchases/repayments	0.5	0.4	0.4	0.4	0.2	0.2	0.3	0.3	0.4	0.3
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Gross official reserves	11.1	12.3	10.4	10.2	10.7	10.9	12.2	13.5	14.5	15.6
Months of imports[2]	2.8	3.4	3.0	2.9	3.1	3.2	3.6	3.9	4.2	4.5
Current account balance (percent of GDP)										
Excluding official transfers	-13.0	-11.4	-10.1	-9.3	-8.1	-8.7	-7.9	-7.7	-7.7	-7.6
Excluding project related imports	-9.8	-7.8	-6.0	-7.1	-5.2	-4.8	-4.7	-4.4	-4.4	-4.2
Excluding official transfers and project related imports	-9.7	-8.0	-7.2	-7.1	-5.2	-5.9	-4.7	-4.4	-4.4	-4.2
Value of exports of GNFs (percent change)	-1.9	4.0	4.0	10.6	10.6	7.5	6.6	6.4	6.6	7.1
Value of imports of GNFs (percent change)	6.8	3.5	3.5	4.0	4.0	5.6	4.5	6.1	6.9	7.0

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

Table 5. Malawi: Selected Banking Soundness Indicators, 2012–18

Key ratios	Dec-12	Dec-13	Dec-14	Dec-15	Dec-16	Dec-17	Aug-18
Capital Adequacy							
1. Regulatory Tier 1 capital to risk weighted assets	16.4	16.2	13.5	12.4	13.8	15.3	15.8
2. Regulatory total capital to risk weighted assets	20.2	19.1	17.1	15.8	17.0	19.4	19.3
3. Total capital to total assets	14.3	15.4	17.6	17.1	16.7	15.9	16.8
Asset composition and quality							
1. Non-performing loans to gross loans and advances	9.4	15.4	14.9	10.6	17.0	15.7	9.3
2. Provisions to non-performing loans	26.8	29.1	31.8	25.7	25.5	34.5	50.8
3. Total loans and advances to total assets	50.8	40.5	40.3	40.0	34.8	28.1	32.3
4. Foreign currency loans to total loans and advances	7.9	13.5	19.1	28.6	21.8	27.9	25.4
Earnings and profitability							
1. Return on assets (ROA)	5.0	4.8	4.0	3.1	2.7	2.3	2.2
2. Return on equity (ROE)	36.9	37.5	26.8	19.2	18.4	15.7	16.2
3. Non-interest expenses to gross income	36.8	39.7	45.4	51.4	50.0	49.7	51.7
4. Interest margin to gross income	36.8	39.7	---	50.2	47.8	50.8	48
5. Non-Interest Income to Revenue	---	31.8	37.8	30.5	28.0	27.3	31.2
6. Net Interest Income to Assets	---	9.1	8.4	9.7	9.7	8.7	5.8
7. Personnel expenses to non-interest expenses	46.0	45.4	45.1	45.3	43.8	46.5	44.3
Liquidity							
1. Liquid assets to deposits and short-term liabilities	45.4	59.1	62.4	59.0	72.3	77.0	59.5
2. Total loans to total deposits	72.4	56.6	58.3	58.5	54.2	45.1	68.9
3. Liquid Assets to total assets	34.5	43.7	48.8	43.3	50.4	55.0	43.3
4. Foreign exchange liabilities to total liabilities	17.9	26.3	---	26.1	19.7	19.8	16.3

Source: Reserve Bank of Malawi.

Table 6. Malawi: External Financing Requirements and Sources, 2016–23
(Millions of USD)

	2016	2017	2018	2019	2020	2021	2022	2023
Total requirement	-780	-887	-648	-774	-805	-852	-897	-973
Current account, excluding official transfers	-709	-702	-636	-628	-604	-626	-670	-708
Debt amortization	-137	-32	-74	-51	-56	-62	-67	-71
Gross reserves accumulation (- increase)	65	-153	63	-95	-145	-163	-160	-194
Total sources	780	887	648	774	805	852	897	973
Expected disbursements (official)	627	573	400	571	588	636	687	745
Grants	496	333	282	422	400	435	465	505
Medium- and long-term loans	130	240	118	150	189	200	222	240
Private sector (net)	105	305	246	188	204	227	247	260
IMF (net)	52	5	3	15	12	-10	-37	-32
Drawings	76	27	32	31	32	16	0	0
Repayments	25	22	29	17	20	26	37	32
Financing gap	0	0	0	0	0	0	0	0
Gross official reserves	605	758	695	791	936	1099	1260	1453
Months of imports	2.8	3.4	2.9	3.2	3.6	3.9	4.2	4.5

Source: IMF staff estimates.

Table 7. Malawi: Schedule of Disbursements under ECF Arrangement, 2018–21

(Millions of SDR)

Amount	% of Quota[1]	Availability date	Conditions Necessary for Disbursement	Status
11.15	8.033	April 30, 2018	Executive Board Approval of Three Year ECF arrangement.	Disbursed
11.15	8.033	October 15, 2018	Observance of performance criteria for June 30, 2018, and completion of first review.	
11.15	8.033	April 15, 2019	Observance of performance criteria for December 31, 2018, and completion of second review.	
11.15	8.033	October 15, 2019	Observance of performance criteria for June 30, 2019, and completion of third review.	
11.15	8.033	April 15, 2020	Observance of performance criteria for December 31, 2019, and completion of fourth review.	
11.15	8.033	October 15, 2020	Observance of performance criteria for June 30, 2020, and completion of fifth review.	
11.175	8.051	April 15, 2021	Observance of performance criteria for December 31, 2020, and completion of the sixth review.	
78.075	**56.25**	**Total for the ECF**		
Memorandum item:				
Malawi's Quota (millions SDR)		138.80		

Source: IMF staff estimates.

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

Table 8. Malawi: Indicators of Capacity to Repay the Fund, 2018–31

	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Projected Payments based on Existing Drawings:														
(SDR millions)														
Principal[1]	11.43	11.89	13.80	18.44	25.81	22.37	20.88	18.28	11.55	4.18	1.12	0.00	0.00	0.00
Charges and interest	0.16	0.64	0.64	0.64	0.64	0.64	0.64	0.64	0.64	0.64	0.64	0.64	0.64	0.64
Projected Payments based on Prospective Drawings:														
(SDR millions)														
Principal	0.00	0.00	0.00	0.00	0.00	0.00	3.35	7.81	12.27	13.39	13.39	10.04	5.58	1.12
Charges and interest	0.00	0.00	0.01	0.00	0.00	0.00	0.01	0.00	0.00	0.00	0.01	0.00	0.00	0.00
Projected Payments based on Existing and Prospective Drawings:														
SDR millions	11.59	12.53	14.45	19.08	26.45	23.01	24.88	26.73	24.46	18.21	15.16	10.68	6.22	1.76
US$ Millions	16.62	18.02	20.80	27.46	38.07	34.34	37.13	39.90	36.51	27.18	22.63	15.94	9.28	2.63
Percent of exports of goods and services	0.90	0.91	0.99	1.22	1.59	1.34	1.35	1.35	1.15	0.80	0.62	0.41	0.22	0.06
Percent of debt service	12.44	20.36	21.38	24.46	29.47	26.25	26.34	26.75	23.96	17.66	14.15	10.03	5.81	1.65
Percent of quota	8.35	9.03	10.41	13.75	19.06	16.58	17.93	19.26	17.62	13.12	10.92	7.69	4.48	1.27
Percent of gross official reserves	2.39	2.28	2.22	2.50	3.02	2.36	2.33	2.28	1.91	1.30	0.98	0.62	0.33	0.08
Projected Level of Credit Outstanding based on Existing and Prospective Drawings:														
SDR millions	159.5	169.9	178.4	171.1	145.3	122.9	98.7	72.6	48.8	31.2	16.7	6.7	1.1	0.0
US$ Millions	229.0	244.5	256.7	246.3	209.1	176.8	142.0	104.5	70.2	44.9	24.1	9.6	1.6	0.0
Percent of exports of goods and services	12.4	12.3	12.2	11.0	8.7	6.9	5.2	3.5	2.2	1.3	0.7	0.2	0.0	0.0
Percent of debt service	171.4	276.1	263.9	219.4	161.9	135.2	100.7	70.1	46.1	29.2	15.1	6.1	1.0	0.0
Percent of quota	114.9	122.4	128.5	123.3	104.7	88.6	71.1	52.3	35.2	22.5	12.1	4.8	0.8	0.0
Percent of gross official reserves	32.9	30.9	27.4	22.4	16.6	12.2	8.9	6.0	3.7	2.1	1.0	0.4	0.1	0.0
Memorandum items:														
Exports of goods and services (millions of U.S. dollars)	1,844	1,982	2,111	2,247	2,394	2,565	2,748	2,948	3,162	3,388	3,630	3,873	4,144	4,435
Debt service (millions of U.S. dollars)	133.6	88.5	97.3	112.3	129.2	130.8	141.0	149.1	152.4	153.9	159.9	159.0	159.7	159.3
Quota (SDR millions)	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8	138.8
Gross official reserves (millions of U.S. dollars)	695	791	936	1,099	1,260	1,453	1,593	1,747	1,915	2,098	2,310	2,554	2,844	3,163
GDP (millions of U.S. dollars)	6,820	7,257	7,672	8,141	8,696	9,307	9,954	10,641	11,384	12,192	13,054	13,974	14,954	15,980

Source: IMF staff projections.

[1] Principal payment in 2018 includes the amount already paid as of September 30, 2018.

Table 9. Malawi: Projected External Borrowing
(January 1, 2018–December 31, 2018)

PPG external debt contracted or guaranteed[1]	Volume of new debt (US$ million)	PV of new debt (US$ million)
Sources of debt financing		
Consessional debt, of which [2]	**439**	**227**
Multilateral debt	439	227
Bilateral debt	0	0
Non-concessional debt, of which [2]	**0**	**0**
Semi-concessional[3]	0	0
Commercial terms[4]	0	0
Use of debt financing		
Infrastructure	439	227
Budget Finanicng	0	0
Memo Items		
Indicative projections		
Year 2	108	82-101
Year 3	161	61-74

Source: IMF staff projections.

[1] Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate.

[2] Debt with a grant element of at least 35 percent.

[3] Debt with a positive grant element below 35 percent.

[4] Debt without a positive grant element. For commercial debt, the present value would be defined as the nominal/face value.

Table 10. Malawi: Quantitative Targets, 2018–19[1]

	Target type [2]	2018							2019				
		End-Jun.				End-Sept	End-Dec.		End-Mar.		End-Jun.		End-Sept
		Prog.	Adj. Prog.	Est.	Status	IT[13]	Prog.[13]	Modified Prog.	IT[13]	Modified IT	IT[13]	Prog.	IT
I. Monetary targets (millions of kwacha)													
Reserve money (ceiling on stock) (upper bound)[3]	PC	303,482		300,792	Met	299,091	323,385	326,115	300,406	308,798	340,106	346,236	340,175
Reserve money (ceiling on stock)[3]		294,643				290,380	313,966	316,617	291,656	299,804	330,200	336,151	330,267
Reserve money (ceiling on stock) (lower bound)[3]		285,803				281,668	304,547	307,118	282,906	290,810	320,294	326,067	320,359
II. Fiscal targets (millions of kwacha)													
Primary balance (floor)[4,5,6]	PC	-144,929	-163,338	-205,170	Not Met	44,906	29,813	-4,456	16,219	-2,684	3,625	89	-1,236
RBM financing of central government (ceiling)[6,7]	PC	69		-43	Met	0	0	0	0	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0		1,000	Not met	0	0	0	0	0	0	0	0
Social spending (floor)[6,9]	IT	186,132		279,952	Met	87,972	175,944	182,207	263,917	273,310	351,889	364,413	103,104
III. External sector targets (US$ millions, unless otherwise indicated)													
Net international reserves of the RBM (floor)[4,5,8]	PC	434.1	408.7	527.7	Met	454.7	480.2	428.6	488.2	436.6	484.5	460.4	473.1
Accumulation of external payments arrears (ceiling)[6,10]	PC	0		0	Met	0	0	0	0	0	0	0	0
New non-concessional external debt contracted (ceiling)[6,10]	PC	0		127	Not Met[12]	0	0	0	0	0	0	0	0
Memorandum items:													
Net foreign assets of the RBM (US$ millions, end of period)[6]		339.8		434.5		360.4	385.9	316.0	393.9	324.0	390.2	347.8	360.4
Budget support (US$ millions)[6]		84.3		89.1		79.1	79.1	0.0	79.1	0.0	79.1	0.0	0.0
Budget support (millions of kwacha)[6]		62,633.8		65,088.4		60,000.0	60,000.0	0.0	60,000.0	0.0	60,000.0	0.0	0.0
Nominal external concessional borrowing (US$ millions)[6]		166		116		35	70	53	104	79	137	105	49
Debt service payments to the World Bank and AfDB (US$ millions)[6]		13.4		12.0		3.8	7.5	19.8	12.1	24.9	16.7	30.1	5.2
Debt service payments to the World Bank and AfDB (millions of kwacha)[6]		9,994		8,781		2,851	5,821	14,680	9,538	18,842	13,337	23,137	4,041
Joint Fund on Health receipts (millions of kwacha)[6]		6,569		0		2,288	4,577	4,577	6,865	6,865	9,153	9,153	1,831
Joint Fund on Education receipts (millions of kwacha)[6]		6,987		4,716		4,325	8,651	8,656	12,976	12,983	17,301	17,311	2,000
Program exchange rate (kwacha per US$)[11]		725		725		725	725	732	725	732	725	732	732

Source: IMF staff projections.

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

[2] "PC" means Performance Criterion and "IT" means Indicative Target. The PC test date for the 2nd Review will be end-December 2018. Test dates for future reviews will be end-June and end-December. End-September and end-March targets are ITs.

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

[4] Targets are subject to an adjustor for budget support and debt service payments, as specified in the TMU.

[5] Targets are subject to an adjustor for donor-funded social sector expenditures consistent with the TMU.

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

[7] Targets are subject to an adjuster equivalent to 10 percent of previous year's tax revenue, as specified in the TMU.

[8] Defined as stocks.

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

[10] Evaluated on a continuous basis.

[11] Starting from End-September 2019, the program exchange rate is changed to the level that reflects the actual (instead of indicative) exchange rate, consistent with the TMU.

[12] A nonresident bank purchased T-notes of MK92 billion in the domestic market, which constitutes contracting new non-concessional external debt according to the TMU. This is due to an oversight in the TMU which excluded T-bills but not T-notes from the items subject to the PC. The definition of the external debt PC in the TMU has been modified going forward to exclude both T-notes and T-bills from the PC on new non-concessional external debt.

[13] Target levels set in IMF Country Report No. 18/115.

Table 11a. Malawi: Structural Benchmarks (May–October 2018)

Structural benchmark	Target date	Macro Rationale	Status
Public financial management			
Submission of five reports by the MDAs[1] by mid-following month and publication on the MoF website. Maintain/strengthen sanctions on MDAs for misreporting/non-compliance.	Continuous (monthly from May 15, 2018)	Improve fiscal transparency; prevent accumulation of new domestic arrears; reduce vulnerabilities to corruption.	Not Met *Partially Implemented*
Set-up and maintain a transparent commitment control system for all MDAs, compile the consolidated commitments of the government centrally by the MOF by the end of the following month and place it on the Ministry of Finance website. Also classify the bills, which are overdue for more than 90 days. Apply sanctions to the controlling officers of the MDAs for incurring arrears without the approval of the Minister of Finance.	Continuous (monthly from May 31, 2018)	Better control on all government commitments and arrears, if any.	Not Met *Implemented with Delay*
Prepare quarterly consolidated financial statements (including all MDAs) with fully reconciled bank accounts and publish within six months after the end of each quarter in the first year and within 90 days after the end of each quarter in the second and third. The financial statements should be certified by the Auditor General.	Continuous (quarterly from March 31, 2019)	Improve fiscal transparency and integrity of the accounting system; routinize reconciliation of all bank accounts; strengthen cash planning; reduce vulnerabilities to corruption.	NA
Reconcile all bank accounts MG1 and seven operating accounts and ways and means transactions within 90 days after the end of each month signed by the Accountant General and Secretary to the Treasury. The reconciliation should clear all the backlog and have a track record of three consecutive months.	Continuous (monthly from July 29, 2018)	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.	Not Met *Partially Implemented*
Reconcile all debt data between the MOF and RBM.	Continuous (monthly from April 30, 2018)	Enhance debt management; improve transparency and monitoring of public debt.	Not Met *Implemented with Delay*
Prepare monthly cash forecasts (broken down by economic classification) of the next 12 months based on input from all MDAs.	End-June 2018	Strengthen cash management; timely implementation of the budget; reduce vulnerabilities to corruption.	Met
Adjust the bank reconciliation of FY2013-14 – 2014-15 based on the findings of forensic audit of MK236 billion and adjust the opening and closing balances of the bank reconciliation of FY2015-16.	End-June 2018	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.	Not Met
Financial sector			
Develop a monetary policy communication strategy.	End-June 2018	Prepare for the eventual implementation of inflation targeting.	Met
Submit to Parliament amendments to the *RBM Act,* which are in line with the recommendations of the IMF Safeguards Monitoring Report, dated 6 June 2016.	End-October 2018	Preserve financial and debt sustainaiblity.	Not Met *Subsequently Modified to Prior Action*

Sources: IMF staff and Malawian authorities.
[1] Ministry, department, and agency.

Table 11b. Malawi: Structural Benchmarks (November–December 2018)

Structural benchmark	Target date	Macro Rationale
Public financial management		
Submission to the MoF of five reports by the MDAs[1] by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted and published 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance.	Continuous (monthly from May 15, 2018)	Improve fiscal transparency; prevent accumulation of new domestic arrears; reduce vulnerabilities to corruption.
Maintain a transparent commitment control system for all MDAs; MoF to centrally compile consolidated commitments of the government by end of the following month and place it on the MoF website. Classify bills overdue for more than 90 days by age. ST to apply sanctions to the controlling officers of the MDAs for incurring arrears without the approval of the Minister of Finance.	Continuous (monthly from May 31, 2018)	Better control on all government commitments and arrears, if any.
Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within six months after the end of each quarter in the first year and within 90 days after the end of each quarter in following years. The financial reports should be certified by the Auditor General.	Continuous (quarterly from March 31, 2019)	Improve fiscal transparency and integrity of the accounting system; routinize reconciliation of all bank accounts; strengthen cash planning; reduce vulnerabilities to corruption.
Reconcile all bank accounts MG1 and six operating accounts (except salary accounts until September 2019) and ways and means transactions within 90 days after the end of each month signed by the Accountant General and Secretary to the Treasury. The reconciliation should clear all the backlog and have a track record of three consecutive months.	Continuous (monthly from July 29, 2018)	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.
Reconcile all debt data between the MOF and RBM.	Continuous (monthly from April 30, 2018)	Enhance debt management; improve transparency and monitoring of public debt.
CMU undertakes variance analysis on forecasting errors every three months, reports a summary of minutes of the meeting, and takes actions to improve MDA submissions.	End-December 2018	Strengthen cash and debt management; timely implementation of the budget; reduce vulnerabilities to corruption.
Finalize and issue the draft regulations, policies and guidelines covering issues of ownership, payment of dividend and surplus, and preparation of PMPBs.	End-December 2018	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.

Sources: IMF staff and Malawian authorities.

[1] Ministry, department, and agency.

Table 11c. Malawi: Structural Benchmarks (2019)

Structural benchmark	Target date	Macro Rationale
Public financial management		
Pilot ex-post reviews/performance audits of some major capital projects in collaboration with the NAO.	End-June 2019	Improve efficiency of public investment.
Submit to Parliament a report on the pilot audit of the main public corporations in collaboration with the NAO.	End-June 2019	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Move from monthly to quarterly budget release (set in a conservative manner), and allow MDAs to commit, through IFMIS, up to the released budget.	End-June 2019	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; and achieve comprehensive coverage in IFMIS.
Bring all TSA sub-accounts into IFMIS including projects, receipts and payments.	End-June 2019	Enhance cash management; achieve comprehensive coverage in IFMIS; and strengthen controls on bank reconciliation and reporting; reduce vulnerabilities to corruption.
Use IFMIS to record commitments or all types of expenditure (based on purchase orders or contracts) prior to the submission of new contracts to the ST for vetting (includes linking HRMS and IFMIS) and all domestic debt commitments, expenditures, and payments in real time. Disclose on the MoF website information on (i) accumulated commitments against the budget allocation and (ii) outstanding bills classified by age, on a monthly basis, 30 days after the reference period.	End-August 2019	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption.
Audit of the Public-Sector Investment Program (PSIP) database, including the efficiency and timeliness of its processes, and its coverage.	End-December 2019	Improve efficiency of public investment.
Streamline activities of DAD to ensure its front office operations include more active engagement in domestic debt management policies and operations in collaboration with the RBM.	End-December 2019	Enhance debt management; improve transparency and monitoring of public debt.
Submit to Parliament and publish on the MoFEPD website a consolidated annual report on SOEs (including case studies for ESCOM, ADMARC, and Blantyre Water Board).	End-February 2020	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Financial sector		
Develop a strategy to pace the unwinding of RBM holdings of government securities that minimizes adverse effects on public debt management and monetary policy implementation.	End-September 2019	Improve debt management and governance.
Develop a roadmap for increasing access to finance.	End-December 2019	Increase financial sector intermediation.

Sources: IMF staff and Malawian authorities.

Table 12. Malawi: Prior Actions

Measures	Macro Rationale
Submission to the MoF of the three remaining reports for April-September 2018 (from the continuous SB) by the MDAs[1] and publish on the MoF website.	Improve fiscal transparency.
Remobilize the IFMIS steering committee by holding a meeting.	Improve fiscal transparency.
Publication of the RBM's communication strategy.	Enhance RBM credibility and prepare for the eventual implementation of inflation targeting.
Submit to Parliament amendments to the RBM Act, which are in line with the recommendations of the IMF Safeguards Monitoring Report, dated 6 June 2016.	Preserve financial and debt sustainaiblity.

Sources: IMF staff and Malawian authorities.
[1] Ministry, department, and agency.

Annex I. Risk Assessment Matrix

Source of Risk	Relative Likelihood in next 1–3 years[1]	Impact if Realized	Policy advice[2]
Global Risks			
Tight global financial conditions.	**High**	**Medium** Increased financial volatility makes foreign investors more risk averse, reduces financial flows, raises debt service costs and refinancing risks, contributes to currency depreciation, elevates inflationary pressures and undermines growth prospects.	Keep fiscal discipline and make monetary policy consistent with growth and inflation objectives, maintain adequate foreign reserves, and smooth short-term exchange rate volatility.
Weakening demand in key partner economies.	**Medium**	**Medium** Weak external demand dampens exports and donor financing, depressing real GDP growth.	Adopt policies to increase fiscal space to respond to contingences, tighten monetary policy and increase exchange rate flexibility to absorb shocks, strengthen FX reserve buffer to facilitate adjustment, and continue efforts to diversify the export base.
Energy prices volatility.	**Medium**	**Medium** Energy price fluctuations and higher fuel demand and import prices can add to balance of payments pressures and increased domestic production costs.	Tighten monetary policy, increase exchange rate flexibility, strong FX reserve buffer, use the automatic fuel price adjustment mechanism and adjust electricity prices to smooth price movement, ensure adequate energy supplies and contain additional fiscal cost/ contingent liabilities.
Regional and Domestic Risks			
Expansionary fiscal policies.	**High**	**High** Domestic borrowing for unduly high fiscal deficits leads to inflationary pressures, crowding out the private sector; there is a risk of reemergence of payment arrears.	Pursue restrictive fiscal policies, adopt corrective measures to limit spending, exert effective commitment control systems, increase revenue mobilization, and improve debt management.
Delayed PFM reforms and lacking expenditure control.	**High**	**High** Uneven progress of PFM reform and deficient expenditure control undermine confidence in budgetary processes and efforts to effectively and transparently manage expenditure.	Accelerate implementation of PFM reform programs, strengthen corruption control, and communicate regularly and transparently.
Excessive external borrowing.	**Medium**	**High** Implementing an over-ambitious capital investment program, especially, if financed with non-concessional external loans, debilitates the precarious medium to long-term debt sustainability position.	Elaborate a prudent and well appraised public investment program, secure concessional financing, and assess the impact of borrowing on debt sustainability.

Deficient conduct of monetary policy.	**Medium**	**High** Conflicting signals on policy intentions confuse market participants' confidence.	Improve the communication of monetary policy and adopt a clear and effective monetary operational framework.
Deteriorating financial stability.	**Medium**	**Medium** Increasing non-performing loans and deteriorating financial positions threaten financial sector stability.	Strengthen banking supervision and inspection to contain emerging risks by developing early warning systems and countervailing measures, eliminate domestic arrears accumulation.
Spending pressures ahead of elections.	**High**	**High** Weak policy discipline and reform efforts could lead to macro-economic policy slippages.	Maintain strong political commitment to program implementation and strengthen vigilance and control in expenditure monitoring.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline scenario path, which is most likely to materialize in the view of IMF staff. The Relative Likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline scenario.

[2] The policy response suggested by Fund staff assumes all other circumstances remain unchanged.
For a combination of shocks, policy responses would need to be modified to avoid conflicts.

Annex II. Joint Bank-Fund Debt Sustainability Analysis[1]

Malawi Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	*Moderate*
Overall risk of debt distress	*High*
Granularity in the risk rating	*Some space to absorb shocks*
Application of judgment	Yes: Vulnerabilities from high public domestic debt

Malawi's external debt is assessed to be at a moderate risk of debt distress, but with some space to absorb shocks. While the mechanical results of the model point to low risk—with all four external debt burden indicators below the thresholds determined by Malawi's debt carrying capacity[2]—judgement was applied given vulnerabilities from high domestic debt.

Malawi is assessed to be at high overall risk of debt distress. This mainly reflects increasing amounts of domestic debt at high interest rates during recent years. The present value of total public debt is projected to decline throughout the program period but would breach the benchmark through 2025.

The projected borrowing path and debt policies remain broadly unchanged since the last DSA. Fiscal discipline should be strengthened to avoid accumulation of domestic debt at high interest rates. Close attention will be needed to the financing terms of any proposed infrastructure investments given limited headroom for further borrowing. To enhance resilience to shocks, efforts should be stepped up to further diversify the economy, particularly exports, broaden the revenue base, and strengthen public financial management.

[1] The Debt Sustainability Analysis has been prepared jointly by IMF and International Development Association (IDA) staff using the debt sustainability framework for low-income countries approved by the Boards of both institutions.

[2] Malawi's debt carrying capacity is classified as "weak" according to the composite indicator score determined by the World Bank's Country Policy and Institutional Assessment (CPIA) Index and other key fundamentals including real GDP growth, import coverage of reserves, remittances as percent of GDP, and growth rate of the world economy. The relevant thresholds for external debt under this category are: 30 percent for PV of debt-to-GDP ratio, 140 percent for PV of debt-to-exports ratio, 10 percent for debt service-to-exports ratio, and 14 percent for debt service-to-revenue ratio. The benchmark on total public debt (sum of public and publicly guaranteed external debt and public domestic debt) is 35 percent for PV of total debt-to-GDP ratio.

Public Debt Coverage

1. Public debt used for the DSA is public and publicly guaranteed (PPG) external and public domestic debt, covering debt contracted and guaranteed by the central government and the Reserve Bank of Malawi (RBM). Due to data limitations, it does not include debt held by state and local governments, other elements in the general government (such as the social security fund and extra budgetary funds), or non-guaranteed state-owned enterprise (SOE) debt. However, the authorities are committed to strengthening the oversight and monitoring of SOEs, including conducting pilot audits of the largest SOEs, publishing consolidated annual reports on SOEs, and developing a prototype SOE database over the next few years (staff report Table 11, ¶20). These steps will help gradually broaden the public debt coverage. For the current DSA, the stress tests, described below, include an adjustment to reflect the portions of the public sector not captured in the reported debt data (Text Table 1).

Text Table 1. External and Public DSAs: Coverage of Public Debt and Design of Contingent Liabilities (Tailored) Stress Tests

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

	The country's coverage of public debt	The central government, central bank, government-guaranteed debt		
		Default	Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0 percent of GDP	2.0	Limited debt coverage.
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	2.0	
4	PPP	35 percent of PPP stock	0.0	
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	5.0	
	Total (2+3+4+5) (in percent of GDP)		9.0	

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

Background on Debt

2. Malawi's public and publicly guaranteed (PPG) external debt stood at about US$2.04 billion (33.2 percent of GDP) in 2017, up from $1.72 billion in 2016 (32 percent of GDP). The increase in PPG external debt during 2017 mainly reflects $382 million of new disbursements (with $353 million from multilaterals and $29 million from bilateral creditors) and principal payment of about US$150 million, as well as $20 million in guarantees to SOEs.

3. Public external debt is held mainly by multilateral creditors (78 percent of total, Text Table 2). The main provider is the International Development Association (IDA) followed by the African Development Fund (ADF) and the IMF. China and India are the main bilateral

creditors.[3] Public external debt at end-2017 was concessional with an average grant element above 35 percent.

4. New concessional external loans signed this year ($439 million, all from multilateral creditors) are financing priority infrastructure projects. They cover water and sanitation, irrigation, agricultural commercialization, financial advancement for rural markets, and digitalization.

Text Table 2. Composition of Public and Publicly Guaranteed Medium- and Long-Term External Debt
(Million U.S. dollars)

	2015		2016		2017	
	Actual	Share	Actual	Share	Actual	Share
Multilateral	1,172	73	1,293	75	1,584	78
IMF	163	10	206	12	224	11
IDA	590	37	642	37	860	42
ADF	229	14	248	14	290	14
IFAD	72	4	73	4	77	4
Other multilateral	119	7	124	7	133	6
Bilateral	440	27	426	25	437	21
China	243	15	227	13	236	12
India	152	9	147	9	142	7
Others	45	3	52	3	58	3
Commercial	0.4	0	0	0	0	0
Guarantees to SOEs	n.a.		n.a.		20	1
Total	1,612	100	1,719	100	2,041	100

Sources: Malawian authorities and IMF staff calculations.

5. Public domestic debt is held by the RBM, commercial banks, and the non-bank financial sector. As noted in the previous DSA, the recent spike in public domestic debt reflects a progressive shift of debt from external to domestic borrowing during recent years (Text Table 3, Text Figure 1). In the first eight months of the year, the RBM reduced its holdings of the central government debt by MK 71 billion (a decline of about 13 percent from the end-2017 level). Nevertheless, the RBM remains the largest creditor of domestic debt, holding over a third of public domestic debt. Mirroring the reduction in the RBM holdings of central government debt is the rapid increase by government debt holdings of commercial banks, pension funds, and insurance companies.

[3] Data on private external debt remains unavailable, but the amounts are not believed to be large.

6. Public domestic debt, 24.5 percent of GDP at end-2017, is expected to rise to 26.1 percent in 2018—3.9 percentage points higher than envisaged in the previous DSA. The primary deficit in FY 2017/18 was 4.3 percent compared to the previously programmed level of 3.4 percent (net of a shortfall in grants). This was mainly due to unexpected maize purchases (to ensure food security in some parts of the country), higher arrears payments (based on court rulings), and increased spending to hold elections. Consequently, net domestic financing, and in turn, the domestic debt level has risen. The current DSA incorporates guarantees to SOEs of MK 17 billion (0.4 percent of GDP).

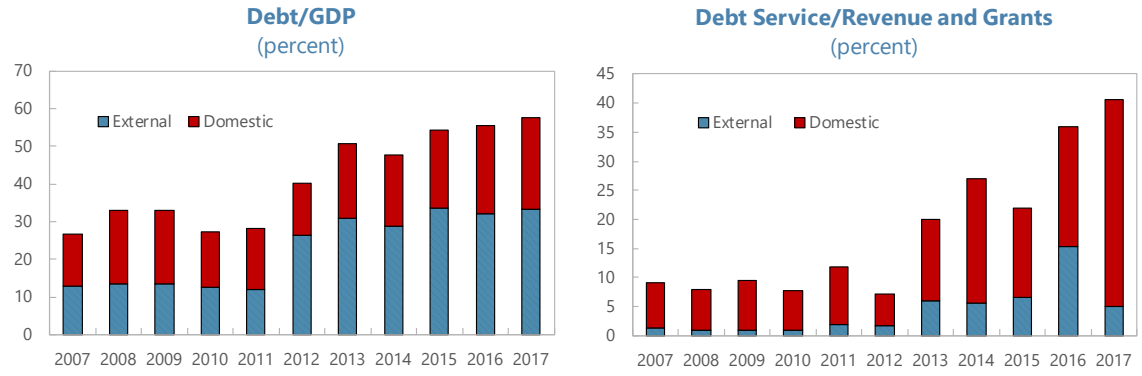
7. As of August 2018, nonresidents hold about MK 117 billion treasury bills and notes denominated in kwacha (10 percent of total or about 2 percent of GDP). Due to difficulties in monitoring such debt, the current DSA uses a currency-based definition for domestic/external debt, classifying the kwacha-denominated debt owed to nonresidents as domestic. There is no material difference between the two criteria. The terms of these treasury bills/notes held by nonresidents and residents are the same.

Text Table 3. Composition of Gross Domestic Debt
(Percent of GDP)

	2012	2013	2014	2015	2016	2017
Treasury bills at cost value	9.0	9.1	6.9	6.2	5.8	5.6
Treasury notes	2.7	1.8	5.4	9.6	13.0	15.2
Local registered stocks (LRS)	0.20	0.07	0.04	0.00	0.02	0.02
Ways and means advances from RBM	1.7	5.2	3.0	0.9	0.9	1.0
Promissory notes	0.1	3.6	3.7	4.2	3.8	2.3
Commercial bank advances	0.100	0.007	0.005	0.019	0.004	0.004
Gurantees to SOEs	n.a.	n.a.	n.a.	n.a.	n.a.	0.378
Total	**13.8**	**19.8**	**19.0**	**21.0**	**23.5**	**24.5**

Sources: Malawian authorities; IMF staff estimates.

Text Figure 1. Public and Publicly Guaranteed Debt



Sources: Malawian authorities and IMF calculations.

Background on Macro Forecasts

8. The medium- and long-term macroeconomic framework underlying this DSA is consistent with the scenario presented in the Staff Report for the First Review of the ECF (Text Table 4 and Box 1). To compensate for expenditure overruns in FY 2017/18 and rein in the debt buildup, the current DSA assumes a cumulative additional tightening of the primary balance by about 2 percent of GDP over FY 2018/19–19/20, relative to the previously programmed path. The improvement is achieved mainly through higher tax revenues (e.g., improved revenue collection, impact of expeditiously implemented tax policies, collection of arrears) and nontax revenues (e.g., higher dividends supported by revised dividend policies and increased tariffs charged by some SOEs) as well as lower goods and services spending, subsidies, and domestic development. Efforts to enhance SOE oversight and monitoring will also help generate SOEs' revenue generation capacity, ensure more efficient spending and public service delivery, and reduce potential transfers and eliminate bailouts.

Text Table 4. Macroeconomic Forecast and Assumptions
(Previous and Current DSAs)

	Real GDP growth (percent)		Primary deficit (percent of GDP)		Change in public debt (percent of GDP)		Current account (percent of GDP)		FDI (percent of GDP)	
Year	Previous	Current	Previous	Current	Previous	Current	Previous	Current	Previous	Current
2015	2.9	2.9	2.7	2.7	6.2	6.7	-9.4	-8.9	1.8	1.8
2016	2.3	2.3	2.4	2.4	0.0	1.1	-13.6	-13.0	3.1	3.1
2017	4.0	4.0	3.2	3.6	0.7	2.1	-10.0	-11.1	2.0	2.1
2018	3.5	3.2	-0.4	0.3	3.6	-0.3	-8.9	-9.3	2.2	2.0
2019	4.5	4.0	0.9	-1.0	-0.3	-1.2	-8.1	-7.6	2.3	2.1
2020	5.0	5.0	-0.3	-0.2	-2.1	-0.8	-7.9	-7.9	2.4	2.3
2021	5.5	5.5	-0.1	-0.3	-2.4	-1.4	-7.7	-7.7	2.5	2.4
2022	6.0	6.0	-0.3	-0.4	-2.5	-2.0	-7.7	-7.7	2.5	2.5
2023	6.5	6.5	-0.3	-0.6	-2.7	-2.2	-7.6	-7.6	2.5	2.5
Avg 2024-38	6.5	6.5	0.7	0.4	-1.2	-1.3	-6.4	-6.5	2.5	3.1

Sources: Malawian authorities and IMF staff calculations and projections.

Box 1. Baseline Macroeconomic Assumptions

Real GDP growth is projected to moderate to 3.2 percent this year, rebound to 4 percent next year, and gradually stabilize at 6.5 percent over the long term, about 1.5 percentage points higher than the average during 2008-17. These growth prospects are predicated on recent land reforms that will facilitate the use of irrigation infrastructure as well as further significant improvements in irrigation infrastructure and cropping techniques (including diversification away from maize production), enhanced electricity generation, better road and telecommunications networks, and greater access to finance for the private sector. It is also assumed that the quality and capacity of the government's public investment and debt management steadily improves, beginning with the reforms under the current ECF.

Inflation is projected to rise to 9.5 percent by end-2018 (reflecting the impact of higher maize and energy prices) before resuming a gradual disinflation path to reach 5 percent by 2023. Tight fiscal and monetary policies are expected to continue anchoring inflation expectations.

The exchange rate is projected to remain constant in real effective terms.

Private sector credit growth is expected to remain subdued (at 8 percent) this year due to weak credit demand before strengthening to 10 percent next year and averaging about 14 percent during 2020–2023 in line with stronger real growth.

The tax revenue to GDP ratio is anticipated to edge up by 0.4 percentage points during FY 2017/18–2018/19 and gradually rise in the medium to long term, assuming the implementation of a mix of tax policy measures (streamlining various tax incentives, expanding the VAT base and improving SME taxation) and tax administration measures (rollout of the Integrated Tax Administration System and improving tax compliance).

External debt will be mainly contracted with multilateral creditors on concessional terms. For FY 2019/20, the framework assumes about $80 million budget support grants from the World Bank, while the previous DSA incorporated it in FY 2018/19.

New disbursements on external loans. The disbursements for FY 2017/18 fell short of the originally programmed amount by about 0.4 percentage points of GDP, due to lower implementation. Project capital spending covered by external loans is projected to reach 3.7 percent of GDP in FY 2018/19 and FY 2019/20 and rise slightly in subsequent fiscal years.

The current account deficit is projected to shrink gradually, reflecting large and persistent import needs. The projections remain broadly unchanged from the last DSA.

Gross official reserves (at $733 million as of end-September) are expected to moderate to about $700 million this year, covering 2.9 months of next year's imports, mainly due to a sharp worsening in terms of trade which limited the improvement in the current account balance and a shortfall of project loans and grants. Over the medium term, reserves are projected to gradually rise, covering 4.5 months of imports by 2023.

Net domestic financing. It is assumed that the government's net domestic financing moderates to 4.7 percent in FY 2018/19, following a spike to 6.3 percent in FY 2017/18. Beyond FY 2018/19, net domestic financing is expected to be contained within 2 percent of GDP.

9. In Malawi, one of the most important source of financing the current account deficit has been capital account flows, consisting of project grants, dedicated grants, and off-budget support, which totaled around 6 percent of GDP over the past 5 years. These flows are expected to average at 5-6 percent of GDP over the medium term. This, combined with price and exchange rate factors, led to large negative residuals going forward (Table 1).

10. Over the longer term, external financing in the form of project support loans is expected to gradually moderate while foreign direct investment will play an increasingly important role. The grant element of project loans will remain relatively high over the forecast period, with no access to market financing. In line with a strengthening of Malawi's external position and ability to service external debt, project and dedicated grants are expected to decline to less than one percent over the long term, with no resumption of budget support operations assumed beyond the World Bank disbursement in FY 2019/20.

11. The realism tools suggest that the baseline macroeconomic assumptions are reasonable (Figure 4).

- *The total fiscal adjustments* (reduction in primary deficit) are projected at 4 percent of GDP between 2017 and 2020. It lies in the lower half of the top quartile based on the historical distribution of fiscal adjustment among low-income countries. Continued donor support would help stabilize the economy and boost private sector confidence, and reforms under the ECF would support an improved business environment and attract more FDI. Moreover, reforms to tax policy and administration would increase transparency of business processes, reduce corruption, strengthen compliance, and raise tax revenue. Higher tax revenue will in turn better support much needed high-quality spending on social sector, help achieving SDGs.

- *The projected growth path* lies above what is implied by assuming only a fiscal impact from the last observed growth rate (which is 4 percent in 2017) with a fiscal multiplier of 0.4 (a standard multiplier in low-income countries). However, the baseline medium-term growth forecasts build in significant improvements in the drivers of growth, which will help lift growth potential to a level significantly higher than its historical average. These improvements include more robust agricultural production (owing to infrastructure and cropping improvements), enhanced electricity generation, better transportation networks, improved access to finance, and timely implementation of structural reforms that lower the cost of doing business, improve policies and governance, and reduce vulnerabilities to corruption, boosting private sector involvement and donor confidence. However, risks are tilted to the downside. External risks include adverse weather, infestations, worsened terms of trade, while internal risks encompass intensified governance challenge and weaker-than-expected reform implementation.

- *Public and private investment rates* are expected to remain broadly unchanged starting in 2019. For this year, the shortfall of project grants and loans led to a drop in foreign financed development spending, weighing on public investment. The projected 5-year average *contribution of government capital to real GDP growth* is also expected to remain unchanged from last DSA.

Country Classification and Determination of Scenario Stress Tests

12. Malawi's debt carrying capacity is classified as remaining weak. Unlike in the previous DSA, the current classification of the debt carrying capacity is guided by the composite indicator (CI) score. The CI, in turn, is determined by the World Bank's CPIA and other variables from the macroeconomic framework, such as real GDP growth, import coverage of reserves, remittances as percent of GDP, and growth of the world economy. Malawi's CI is 2.65, just below the threshold value of 2.69, which puts it in the "weak" category. The four external debt burden thresholds and the total public debt benchmark are determined by this classification of the debt carrying capacity (Text Table 5).

13. There are two tailored stress tests:

- One tailored stress test combines contingent liabilities of a one-time debt shock (equivalent to 9 percent of GDP) in 2019, to capture the potential impact of limited public debt coverage (2 percent of GDP, instead of the default level of zero) and contingent liabilities from SOEs (equal to the default level of 2 percent of GDP—the medium SOE external liability identified by a Fund staff survey in 2016) and the need for bank recapitalization (equal to the default level of 5 percent of GDP—the average cost to the government of a financial crisis in a low-income country since 1980). Malawi's experience in recent years, such as the recapitalization of the RBM due to exchange rate devaluation and the Agricultural Development and Marketing Corporation (ADMARC) bailout, has illustrated that the materialization of contingent liabilities can contribute to an unexpected increase in the debt-to-GDP ratio.

- The second tailored stress test is a natural disaster induced one-off shock (of 10 percent of GDP) to external PPG debt-to-GDP ratio in 2019. While Malawi is not on the list of Fund's natural disaster-prone countries,[4] judgment was applied as the country is historically vulnerable to weather-related shocks— Malawi recently suffered from two consecutive weather shocks over two years (floods followed by a drought)—which resulted in a sharp increase in food insecurity, triggering a humanitarian crisis.

[4] This list is based on the IMF Policy Paper "Small states' resilience to natural disaster and climate change—role for the IMF" (December 2016).

Text Table 5. Composite Indicator and Threshold Tables

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

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

New framework				
	Cut-off values			
Weak	CI ≤	2.69		
Medium	2.69	< CI ≤		3.05
Strong	CI >	3.05		

External DSA

14. Under the baseline scenario, all debt burden indicators remain below their indicative thresholds. The PPG external debt is projected to peak at 34.8 percent of GDP in 2020, with a PV of debt-to-GDP ratio of 20.4 percent. The PV of PPG external debt is expected to decline gradually to around 15 percent over the long term. The debt service-to-exports ratio is expected to average around 5 percent in the next six years and gradually decline to about 4 percent over the longer term.

15. Under the historical scenario, the external debt is projected to increase and breach the threshold of the PV of debt-to-GDP ratio over the long term. This scenario envisages real GDP growth, the primary balance-to-GDP ratio, the GDP deflator, the non-interest current account, and net FDI flows permanently remain at their historical levels. For instance, the current account deficit is to remain elevated (10 percent of GDP) and FDI subdued (1.5 percent of GDP). However, as noted in the previous DSA, the likelihood is low for Malawi to repeat its history by running high and protracted current account deficits in the medium to long term. FDI inflows are expected to pick up steadily as macroeconomic stability is entrenched, and the business environment improves.

16. Under the standard and tailored stress test scenarios, all debt burden indicators remain below their indicative thresholds. A one-time nominal exchange rate deprecation of 30 percent in 2019 constitutes the most extreme shock for the PV of debt-to GDP ratio and debt service-to-revenue ratio increasing the PV of debt to 25.5 percent of GDP in the same year. On the other hand, an export shock (nominal export growth set to its historical average minus one

standard deviation) in 2019 and 2020, equivalent to a decline of 4 percent each year, is the most extreme shock for PV debt and debt service to exports ratio (Figure 1, Table 1, and Table 3).

Overall Risk of Public Debt Distress

17. Total public debt is projected to edge down to 57.3 percent this year, from 57.7 percent in 2017. Despite a 2-percentage-point decline of PPG external debt, public domestic debt is expected to peak at 26.1 percent this year (up from 24.5 percent in 2017), before gradually declining to just below 20 percent by 2023, supported by continuous improvements in primary balances (Figure 3). As the RBM has stopped financing the central government deficit (RBM financing is limited to liquidity management), all net domestic financing will be met by commercial banks and non-banks, with the expected average nominal interest rates on domestic debt gradually moderating from around 18 percent now to below 15 percent through medium term. Guided by a multi-year strategy, the RBM will gradually unwind its significant holdings of government securities to be absorbed by private sector investors as the domestic debt market continues to develop.

18. Under the baseline, the PV of the total debt-to-GDP ratio is projected to remain continuously above the benchmark throughout 2025. This path is broadly unchanged from that envisaged in the last DSA—where the PV of total debt was expected to decline below 35 percent of GDP by 2023. This reflects stronger medium-term fiscal consolidation broadly offsetting the debt impact of the fiscal overrun in FY 2017/18 and a slightly higher contribution from the average real interest rate—assuming the increase in FY 2017/18 deficits could further dent confidence and raise interest rates as well as a shift towards longer-term maturities of debt.

19. Under all the standard and tailored stress test scenarios, the PV of the total debt-to-GDP ratio remains above the benchmark through 2023, sometimes even well above it. The natural disaster shock constitutes the most extreme shock which elevates the PV of the total debt-to-GDP ratio to 55 percent and above 35 percent even in 2028. The natural disaster shock is also the most extreme shock for the debt service-to-revenue ratio and is expected to add to the debt service burden by nearly 25 percent of revenue in the peak year of 2021 (Figure 2, Table 2, and Table 4).

Risk Rating and Vulnerabilities

20. Malawi is assessed to have a moderate risk of external debt distress with some space to absorb shocks, but a high overall risk of debt distress due to high public domestic debt (Figure 5). On external debt, the mechanical results of the model point to low risk, with all four external debt burden indicators below the thresholds determined by its debt carrying capacity. However, judgment was applied given elevated vulnerabilities from high public domestic debt. The main risks to the ratings assessment arise from limited data coverage, macroeconomic uncertainty (especially from weather shocks), weaker-than-expected policy implementation, and tighter global financial conditions and weak global economy which could depress export growth.

21. Absorption of the shocks that Malawi faces while maintaining macroeconomic stability and debt sustainability will require careful macroeconomic management and difficult policy choices.

- *Increasing fiscal restraint and budget credibility*. Malawi should increase fiscal restraint and budget credibility to contain fiscal deficits and reduce domestic borrowing at high interest rates. Moreover, strengthening expenditure prioritization in line with development priorities will be key to achieving higher, more diversified, and resilient growth.

- *Prudent project selection*. Given limited headroom for further borrowing, close attention and prudence should be applied to project identification and the financing terms of any proposed infrastructure investments. The government should focus on projects with high returns that are closely aligned to development priorities and rely on concessional loans that contain borrowing costs. Reining in domestic borrowing, which currently occurs at high interest rates, would also serve this purpose and avoid crowding out of private sector credit expansion.

- *Broadening revenue base and strengthening public financial management*. Given Malawi's high aid dependency, risks of negative financing shocks in the form of delayed donor support, or lower-than-expected revenue collection remain. Such an environment requires further efforts to maximize the impact of finite domestic resources, including broadening the tax base (e.g., currently under 50 percent of the TINS issues are active tax payers) and strengthening public procurement and public financial management.

- *Reducing the sovereign-bank nexus*. There is a significant nexus between sovereign debt and the banking system since the RBM and commercial banks have been the main sources of domestic financing for the central government. Such large exposure of bank balance sheets to the sovereign risks a negative feedback loop if fiscal challenges emerge or liquidity conditions tighten.

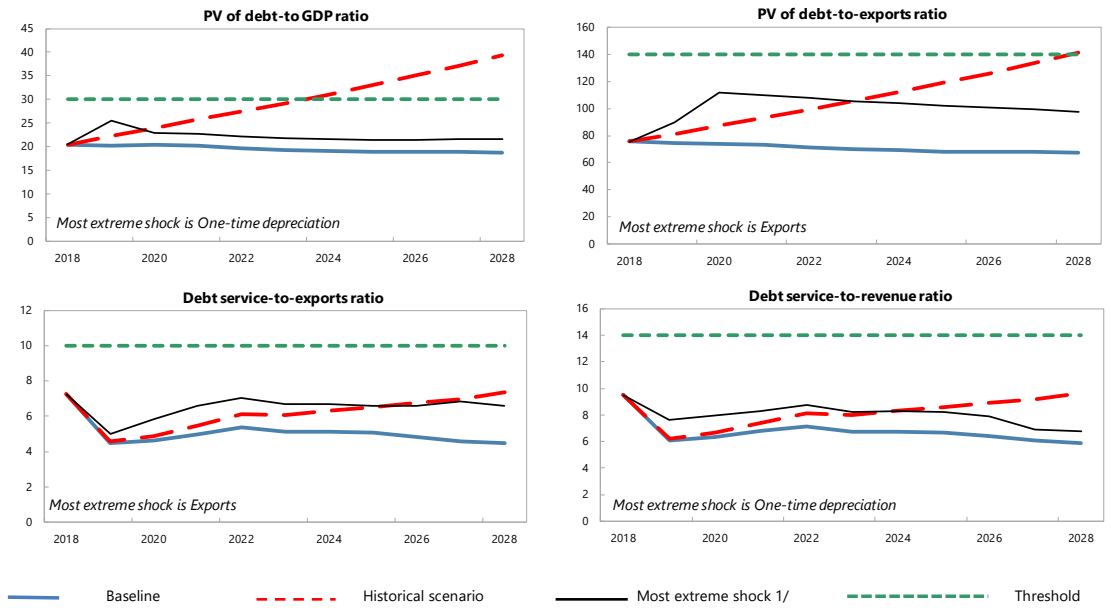
- *Closely monitoring contingent liabilities*. Contingent liabilities have in general been one of the largest sources of fiscal risk. Malawi's experience in recent years, such as recapitalization of the RBM due to exchange rate devaluation and the ADMARC bailout, has illustrated that the materialization of contingent liabilities can contribute to unexpected increases in the debt-to-GDP ratio, crowding out private credit and jeopardizing debt sustainability. Efforts should be stepped up to estimate, disclose, manage, and contain contingent liabilities, especially those in the financial sector and state-owned enterprises.

Authorities' Views

22. The authorities agreed with the DSA assessment of the risk of external debt distress remaining "moderate" and the overall risk of debt distress as high. They acknowledged the significant vulnerabilities from growing public domestic debt. Therefore, while the country has a

strong need for critical infrastructure projects, the authorities are committed to ensuring that financing of the projects preserves debt sustainability.

Figure 1. Malawi: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2018–2028



Customization of Default Settings	Size	Interactions
Tailored Tests		
Combined CLs	Yes	
Natural Disasters	No	No
Commodity Prices 2/	n.a.	n.a.
Market Financing	n.a.	n.a.

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

Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.1%	1.1%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	33	33
Avg. grace period	6	6

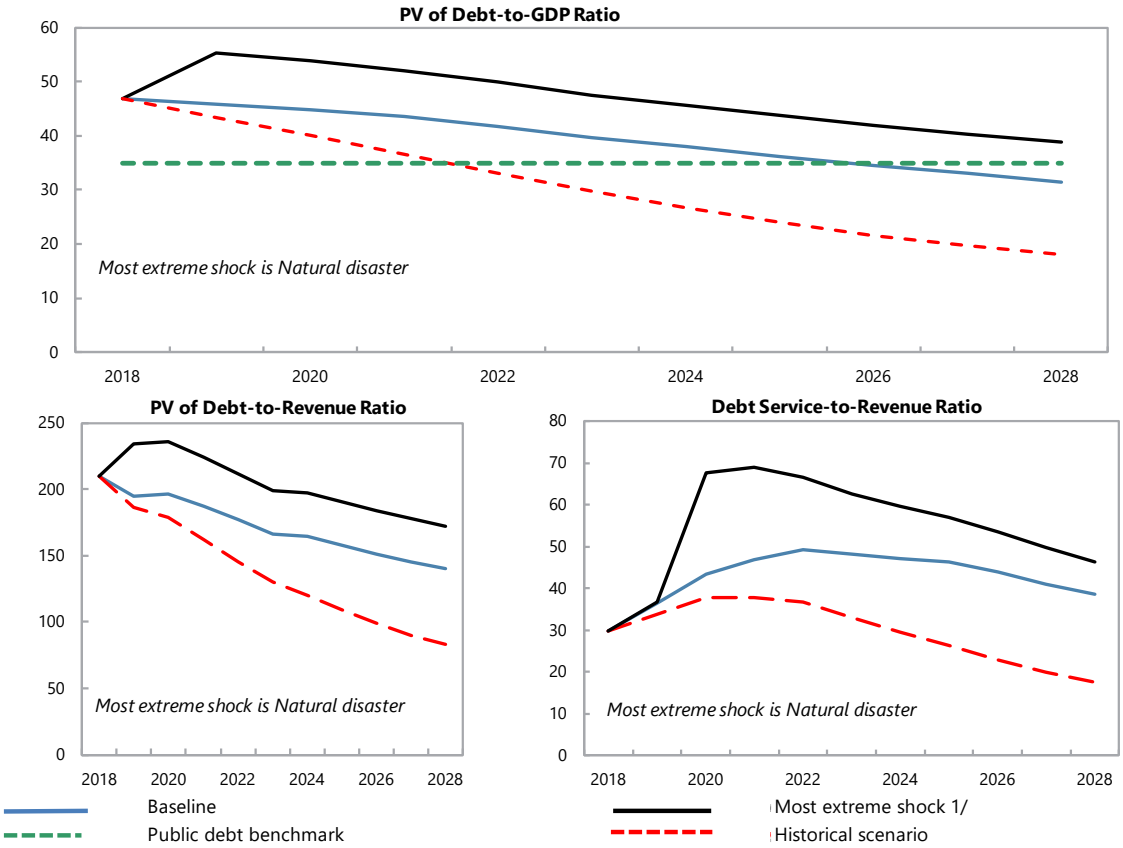
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2028. Stress tests with one-off breaches are also presented (if any), while these one-off breaches are deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF research department.

Figure 2. Malawi: Indicators of Public Debt Under Alternative Scenarios, 2018–2028



Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	29%	29%
Domestic medium and long-term	21%	21%
Domestic short-term	50%	50%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.1%	1.1%
Avg. maturity (incl. grace period)	33	33
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	7.4%	7.4%
Avg. maturity (incl. grace period)	2	2
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	5%	5.0%

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

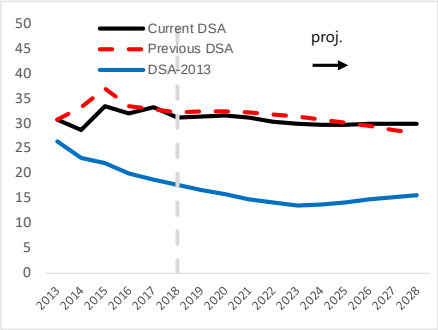
Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2028. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

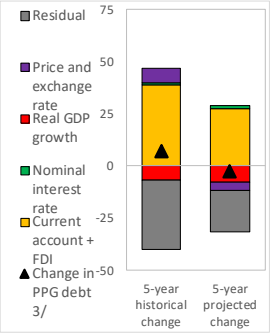
Figure 3. Malawi: Divers of Debt Dynamics—Baseline Scenario

External debt

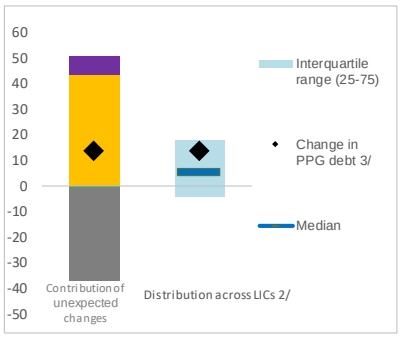
Gross Nominal PPG External Debt
(in percent of GDP; DSA vintages)



Debt-creating flows
(percent of GDP)

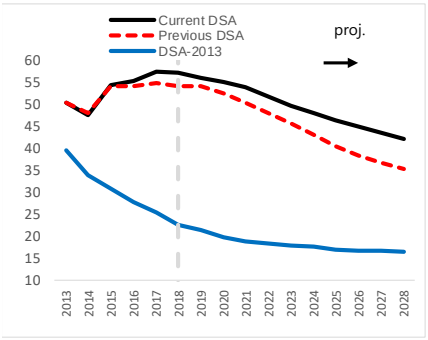


Unexpected Changes in Debt 1/
(past 5 years, percent of GDP)

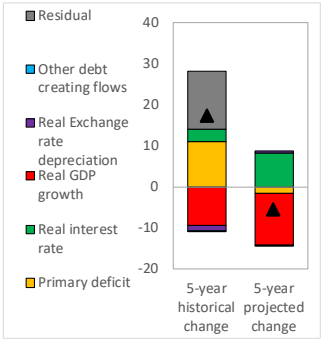


Public debt

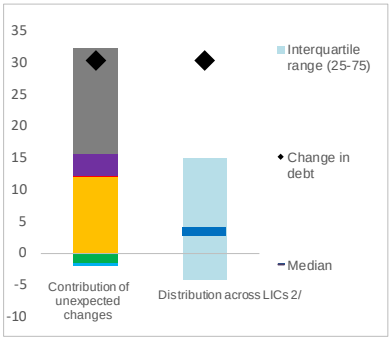
Gross Nominal Public Debt
(in percent of GDP; DSA vintages)



Debt-creating flows
(percent of GDP)



Unexpected Changes in Debt 1/
(past 5 years, percent of GDP)



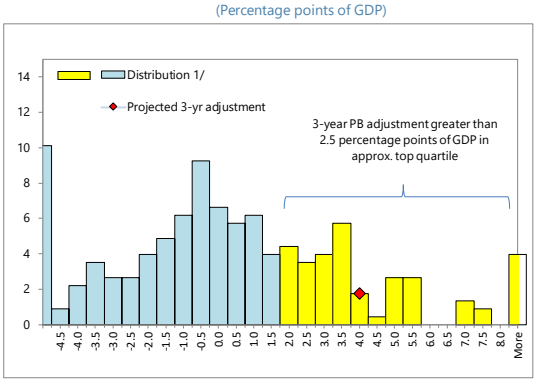
1/ Difference between anticipated and actual contributions on debt ratios.

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

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

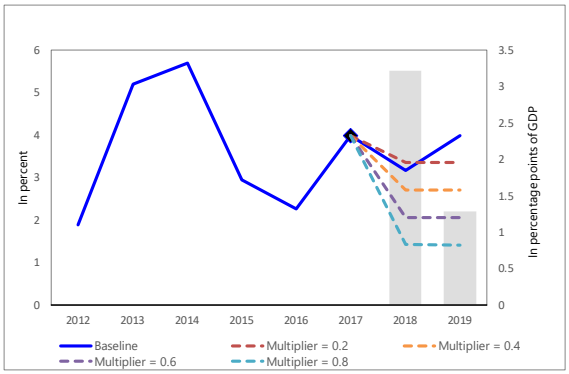
Figure 4. Malawi: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



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

Fiscal Adjustment and Possible Growth Paths 1/



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

Public and Private Investment Rates
(% of GDP)

Contribution to Real GDP growth
(percent, 5-year average)

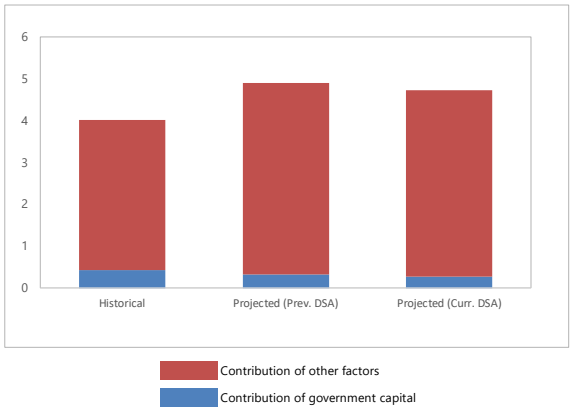


Figure 5. Malawi: Qualification of the Moderate Category, 2018-2028[1/]

Sources: Country authorities; and staff estimates and projections.

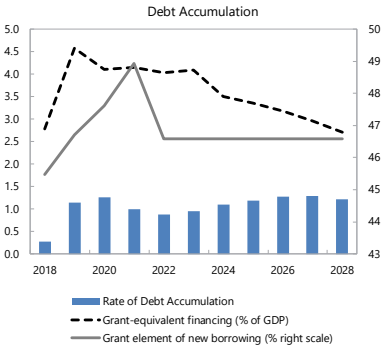
1/ For the PV debt/GDP and PV debt/exports thresholds, x is 20 percent and y is 40 percent. For debt service/Exports and debt service/revenue thresholds, x is 12 percent and y is 35 percent.

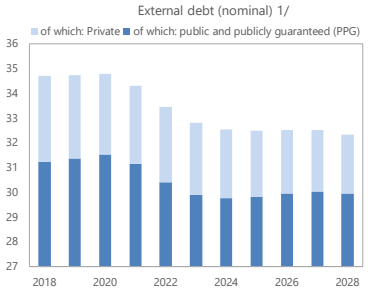
Table 1. Malawi: External Debt Sustainability Framework, Baseline Scenario, 2015–2038

(in percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028	2038	Historical	Projections
External debt (nominal) 1/	**36.9**	**36.2**	**36.9**	**34.7**	**34.7**	**34.8**	**34.3**	**33.4**	**32.8**	**32.3**	**26.7**	**27.1**	**33.4**
of which: public and publicly guaranteed (PPG)	**33.5**	**32.0**	**33.2**	**31.2**	**31.4**	**31.5**	**31.1**	**30.4**	**29.9**	**29.9**	**25.1**	**23.6**	**30.5**
Change in external debt	4.6	-0.7	0.8	-2.2	0.0	0.1	-0.5	-0.9	-0.6	-0.2	-1.0		
Identified net debt-creating flows	**5.4**	**16.4**	**4.8**	**6.3**	**4.2**	**3.9**	**3.5**	**3.3**	**3.1**	**2.3**	**-0.3**	**7.8**	**3.5**
Non-interest current account deficit	**8.6**	**12.7**	**10.8**	**8.9**	**7.3**	**7.6**	**7.4**	**7.4**	**7.3**	**6.9**	**4.7**	**9.9**	**7.5**
Deficit in balance of goods and services	11.1	16.6	15.0	12.5	11.9	11.3	11.2	11.3	11.2	11.0	9.1	**13.9**	**11.4**
Exports	25.5	29.4	27.0	27.0	27.3	27.5	27.6	27.5	27.6	27.8	27.3		
Imports	36.6	46.0	42.0	39.5	39.2	38.8	38.8	38.8	38.8	38.8	36.4		
Net current transfers (negative = inflow)	-4.9	-5.8	-6.1	-5.3	-6.4	-5.4	-5.5	-5.6	-5.7	-5.9	-6.0	**-5.7**	**-5.7**
of which: official	-0.4	0.0	-0.2	0.0	-1.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other current account flows (negative = net inflow)	2.4	1.9	1.9	1.7	1.8	1.8	1.8	1.8	1.8	1.7	1.5	**1.7**	**1.8**
Net FDI (negative = inflow)	**-1.8**	**-3.1**	**-2.1**	**-2.0**	**-2.1**	**-2.3**	**-2.4**	**-2.5**	**-2.5**	**-2.9**	**-3.6**	**-1.9**	**-2.5**
Endogenous debt dynamics 2/	**-1.5**	**6.8**	**-3.9**	**-0.6**	**-1.0**	**-1.4**	**-1.5**	**-1.6**	**-1.7**	**-1.7**	**-1.4**		
Contribution from nominal interest rate	0.3	0.3	0.3	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.3		
Contribution from real GDP growth	-0.9	-1.0	-1.3	-1.1	-1.3	-1.6	-1.8	-1.9	-2.0	-2.0	-1.7		
Contribution from price and exchange rate changes	-0.9	7.5	-2.9	...	...	...	...	...	...	...	...		
Residual 3/	**-0.8**	**-17.1**	**-4.0**	**-8.5**	**-4.2**	**-3.9**	**-3.9**	**-4.2**	**-3.7**	**-2.5**	**-0.8**	**-5.8**	**-3.9**
of which: exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	**...**	**...**	**22.4**	**20.5**	**20.3**	**20.4**	**20.2**	**19.7**	**19.3**	**18.7**	**16.0**		
PV of PPG external debt-to-exports ratio	**...**	**...**	**82.7**	**75.7**	**74.3**	**74.1**	**73.0**	**71.5**	**70.0**	**67.4**	**58.8**		
PPG debt service-to-exports ratio	**7.2**	**12.8**	**4.3**	**7.2**	**4.5**	**4.6**	**5.0**	**5.4**	**5.1**	**4.5**	**3.8**		
PPG debt service-to-revenue ratio	**10.0**	**20.2**	**6.0**	**9.5**	**6.1**	**6.3**	**6.8**	**7.2**	**6.7**	**5.9**	**4.8**		
Gross external financing need (Billion of U.S. dollars)	0.6	0.7	0.6	0.6	0.5	0.5	0.5	0.6	0.6	0.7	0.6		
Key macroeconomic assumptions													
Real GDP growth (in percent)	2.9	2.3	4.0	3.2	4.0	5.0	5.5	6.0	6.5	6.5	6.5	**5.0**	**5.7**
GDP deflator in US dollar terms (change in percent)	2.7	-16.8	8.9	7.2	2.3	0.7	0.6	0.8	0.5	0.5	1.1	**-0.6**	**1.3**
Effective interest rate (percent) 4/	0.9	0.7	0.9	1.3	0.9	0.9	0.9	0.9	0.9	1.0	1.1	**0.7**	**1.0**
Growth of exports of G&S (US dollar terms, in percent)	-7.2	-1.9	4.0	10.6	7.5	6.6	6.4	6.6	7.1	7.1	7.2	**6.9**	**7.3**
Growth of imports of G&S (US dollar terms, in percent)	-2.4	6.8	3.5	4.0	5.6	4.5	6.1	6.9	7.0	6.4	6.6	**6.7**	**6.3**
Grant element of new public sector borrowing (in percent)	...	...	...	45.5	46.7	47.6	48.9	46.6	46.6	46.6	46.6	**...**	**46.8**
Government revenues (excluding grants, in percent of GDP)	18.5	18.6	19.7	20.6	20.1	20.1	20.4	20.7	20.9	21.1	21.3	**17.9**	**20.7**
Aid flows (in Billion of US dollars) 5/	0.4	0.3	0.4	0.2	0.4	0.4	0.4	0.4	0.4	0.5	0.4		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	2.8	4.6	4.1	4.1	4.0	4.1	2.7	1.2	**...**	**3.6**
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	70.0	77.5	73.2	75.4	74.7	74.8	64.4	58.4	**...**	**70.7**
Nominal GDP (Billion of US dollars)	6.4	5.4	6.2	6.8	7.3	7.7	8.1	8.7	9.3	13.1	26.3		
Nominal dollar GDP growth	5.7	-14.9	13.2	10.6	6.4	5.7	6.1	6.8	7.0	7.1	7.7	**4.5**	**7.1**
Memorandum items:													
PV of external debt 7/	...	...	26.1	23.9	23.7	23.7	23.3	22.7	22.2	21.1	17.6		
In percent of exports	...	...	96.5	88.5	86.6	85.9	84.5	82.5	80.6	75.9	64.5		
Total external debt service-to-exports ratio	7.2	12.8	5.9	8.7	5.8	5.8	6.2	6.5	6.1	5.2	4.1		
PV of PPG external debt (in Billion of US dollars)			1.4	1.4	1.5	1.6	1.6	1.7	1.8	2.4	4.2		
(PVt-PVt-1)/GDPt-1 (in percent)				0.3	1.1	1.3	1.0	0.9	1.0	1.2	0.7		
Non-interest current account deficit that stabilizes debt ratio	4.1	13.5	10.1	11.1	7.3	7.5	7.9	8.3	8.0	7.0	5.7		

Definition of external/domestic debt	Currency-based
Is there a material difference between the two criteria?	No





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
4/ Current-year interest payments divided by previous period debt stock.
5/ Defined as grants, concessional loans, and debt relief.
6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).
7/ Assumes that PV of private sector debt is equivalent to its face value.
8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

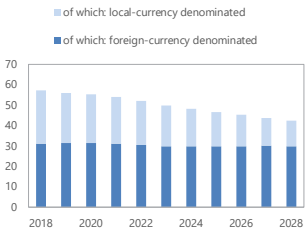
Table 2. Malawi: Public Sector Debt Sustainability Framework, Baseline Scenario, 2015–2038

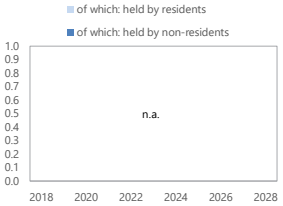
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028	2038	Historical	Projections
Public sector debt 1/	**54.4**	**55.6**	**57.7**	**57.3**	**56.1**	**55.4**	**54.0**	**52.0**	**49.8**	**42.4**	**30.0**	**42.8**	**50.1**
of which: external debt	**33.5**	**32.0**	**33.2**	**31.2**	**31.4**	**31.5**	**31.1**	**30.4**	**29.9**	**29.9**	**25.1**	**23.6**	**30.5**
Change in public sector debt	6.7	1.1	2.1	-0.3	-1.2	-0.8	-1.4	-2.0	-2.2	-1.4	-1.1		
Identified debt-creating flows	**6.1**	**-0.8**	**0.4**	**-0.4**	**-1.4**	**-1.0**	**-1.3**	**-1.5**	**-1.9**	**-1.2**	**-1.1**	**0.4**	**-1.2**
Primary deficit	**2.7**	**2.4**	**3.6**	**0.3**	**-1.0**	**-0.2**	**-0.3**	**-0.4**	**-0.6**	**0.4**	**0.5**	**1.5**	**-0.1**
Revenue and grants	21.7	21.3	23.0	22.4	23.5	22.8	23.2	23.6	23.8	22.5	21.7	**23.3**	**23.0**
of which: grants	3.2	2.7	3.3	1.8	3.4	2.7	2.9	2.8	2.9	1.4	0.5		
Primary (noninterest) expenditure	24.4	23.7	26.5	22.7	22.6	22.6	22.9	23.1	23.2	22.9	22.3	**24.8**	**23.0**
Automatic debt dynamics	**3.4**	**-2.9**	**-3.2**	**-0.7**	**-0.5**	**-0.7**	**-0.9**	**-1.1**	**-1.3**	**-1.6**	**-1.6**		
Contribution from interest rate/growth differential	-1.6	-0.6	-0.8	0.2	-0.9	-1.1	-1.2	-1.3	-1.7	-2.0	-1.9		
of which: contribution from average real interest rate	-0.2	0.6	1.4	2.0	1.3	1.6	1.7	1.7	1.5	0.7	0.0		
of which: contribution from real GDP growth	-1.4	-1.2	-2.1	-1.8	-2.2	-2.7	-2.9	-3.1	-3.2	-2.7	-1.9		
Contribution from real exchange rate depreciation	5.0	-2.3	-2.4	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	**0.0**	**-0.3**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Privatization receipts (negative)	0.0	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	**0.6**	**1.9**	**1.7**	**-0.9**	**0.6**	**0.5**	**0.2**	**-0.2**	**0.1**	**0.2**	**0.2**	**2.7**	**0.1**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	**...**	**...**	**46.9**	**47.0**	**45.7**	**44.9**	**43.5**	**41.7**	**39.6**	**31.5**	**21.2**		
PV of public debt-to-revenue and grants ratio	**...**	**...**	**204.0**	**209.7**	**194.4**	**196.5**	**187.4**	**176.9**	**166.1**	**140.0**	**97.3**		
Debt service-to-revenue and grants ratio 3/	**22.0**	**36.0**	**40.6**	**29.7**	**36.3**	**43.4**	**46.9**	**49.2**	**48.1**	**38.5**	**19.1**		
Gross financing need 4/	4.4	5.7	12.9	7.0	7.6	9.7	10.5	11.1	10.8	9.0	4.7		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	2.9	2.3	4.0	3.2	4.0	5.0	5.5	6.0	6.5	6.5	6.5	**5.0**	**5.7**
Average nominal interest rate on external debt (in percent)	1.2	1.1	1.1	1.5	1.0	1.0	1.0	1.0	1.1	1.1	1.2	**1.0**	**1.1**
Average real interest rate on domestic debt (in percent)	-1.4	3.3	6.8	9.4	6.8	8.3	8.9	9.4	8.7	7.0	5.2	**2.0**	**7.9**
Real exchange rate depreciation (in percent, + indicates depreciation)	17.9	-7.1	-7.8	...	...	...	...	...	...	...	...	**5.2**	**...**
Inflation rate (GDP deflator, in percent)	20.9	19.5	10.7	7.8	8.0	7.4	6.3	5.4	4.6	4.6	5.2	**16.3**	**5.6**
Growth of real primary spending (deflated by GDP deflator, in percent)	15.8	-0.7	16.4	-11.6	3.3	5.2	6.7	7.3	6.9	5.6	6.6	**5.2**	**4.4**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-4.0	1.3	1.5	0.7	0.2	0.5	1.0	1.5	1.6	1.8	1.6	**-0.4**	**1.3**
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

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

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

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

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

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

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

Table 3. Malawi: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2018–2028

	Projections 1/										
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
PV of debt-to GDP ratio											
Baseline	20.5	20.3	20.4	20.2	19.7	19.3	19.1	18.9	18.9	18.8	18.7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	20.5	22.2	24.0	25.7	27.4	29.1	**31.0**	**32.9**	**35.0**	**37.1**	**39.3**
B. Bound Tests											
B1. Real GDP growth	20.5	21.0	21.9	21.6	21.1	20.7	20.4	20.3	20.2	20.2	20.1
B2. Primary balance	20.5	21.0	21.9	22.2	22.2	22.1	22.1	22.1	22.1	22.0	21.9
B3. Exports	20.5	22.0	25.2	24.9	24.3	23.8	23.4	23.2	23.0	22.6	22.2
B4. Other flows 3/	20.5	22.1	23.5	23.2	22.7	22.2	21.9	21.7	21.5	21.2	20.9
B5. One-time 30 percent nominal depreciation	20.5	25.5	23.0	22.8	22.2	21.8	21.6	21.5	21.5	21.6	21.6
B6. Combination of B1-B5	20.5	23.4	24.1	23.8	23.2	22.8	22.5	22.3	22.1	21.9	21.6
C. Tailored Tests											
C1. Combined contingent liabilities	20.5	21.7	22.5	22.8	22.8	22.6	22.6	22.6	22.6	22.6	22.5
C2. Natural disaster	20.5	22.2	23.1	23.6	23.7	23.7	23.8	23.9	24.1	24.2	24.2
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	75.7	74.3	74.1	73.0	71.5	70.0	69.1	68.4	68.0	67.8	67.4
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	75.7	81.3	87.3	93.3	99.4	105.7	112.2	118.9	126.0	133.5	**141.2**
B. Bound Tests											
B1. Real GDP growth	75.7	74.3	74.1	73.0	71.5	70.0	69.1	68.4	68.0	67.8	67.4
B2. Primary balance	75.7	76.7	79.7	80.6	80.7	80.2	80.0	79.7	79.5	79.3	78.7
B3. Exports	75.7	89.6	111.9	110.1	107.8	105.4	103.7	102.3	101.1	99.5	97.8
B4. Other flows 3/	75.7	80.8	85.5	84.1	82.4	80.6	79.3	78.3	77.4	76.5	75.3
B5. One-time 30 percent nominal depreciation	75.7	74.3	66.4	65.5	64.2	62.9	62.2	61.7	61.5	61.8	61.8
B6. Combination of B1-B5	75.7	86.8	82.2	90.0	88.1	86.2	84.9	83.9	82.9	82.1	81.1
C. Tailored Tests											
C1. Combined contingent liabilities	75.7	79.4	81.7	82.7	82.7	82.2	81.9	81.6	81.4	81.4	80.9
C2. Natural disaster	75.7	82.7	85.6	87.2	87.7	87.6	87.8	88.0	88.3	88.7	88.6
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	7.2	4.5	4.6	5.0	5.4	5.1	5.1	5.1	4.9	4.6	4.5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	7.2	4.6	4.9	5.5	6.1	6.1	6.3	6.5	6.8	7.0	7.3
B. Bound Tests											
B1. Real GDP growth	7.2	4.5	4.6	5.0	5.4	5.1	5.1	5.1	4.9	4.6	4.5
B2. Primary balance	7.2	4.5	4.7	5.1	5.5	5.3	5.3	5.3	5.1	5.0	5.0
B3. Exports	7.2	5.0	5.9	6.6	7.1	6.7	6.7	6.6	6.6	6.8	6.6
B4. Other flows 3/	7.2	4.5	4.7	5.2	5.6	5.3	5.3	5.2	5.3	5.2	5.1
B5. One-time 30 percent nominal depreciation	7.2	4.5	4.6	4.9	5.3	5.0	5.0	5.0	4.7	4.2	4.1
B6. Combination of B1-B5	7.2	4.7	5.3	5.7	6.2	5.8	5.8	5.8	5.9	5.6	5.5
C. Tailored Tests											
C1. Combined contingent liabilities	7.2	4.5	4.7	5.1	5.6	5.3	5.3	5.3	5.1	4.8	4.7
C2. Natural disaster	7.2	4.6	4.9	5.3	5.8	5.5	5.6	5.5	5.3	5.1	4.9
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	9.5	6.1	6.3	6.8	7.2	6.7	6.8	6.7	6.4	6.1	5.9
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	9.5	6.2	6.7	7.4	8.1	8.0	8.4	8.6	8.9	9.2	9.7
B. Bound Tests											
B1. Real GDP growth	9.5	6.3	6.8	7.3	7.7	7.2	7.2	7.2	6.9	6.5	6.3
B2. Primary balance	9.5	6.1	6.4	6.9	7.4	6.9	7.0	6.9	6.8	6.6	6.6
B3. Exports	9.5	6.1	6.6	7.3	7.7	7.2	7.2	7.1	7.1	7.4	7.1
B4. Other flows 3/	9.5	6.1	6.5	7.1	7.4	7.0	7.0	6.9	7.0	6.9	6.7
B5. One-time 30 percent nominal depreciation	9.5	7.6	7.9	8.3	8.8	8.2	8.3	8.2	7.9	6.9	6.8
B6. Combination of B1-B5	9.5	6.3	6.9	7.4	7.8	7.3	7.4	7.3	7.5	7.1	6.9
C. Tailored Tests											
C1. Combined contingent liabilities	9.5	6.1	6.4	7.0	7.4	7.0	7.0	7.0	6.7	6.4	6.2
C2. Natural disaster	9.5	6.1	6.5	7.0	7.4	7.0	7.1	7.1	6.8	6.4	6.3
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	14	14	14	14	14	14	14	14	14	14	14

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

Table 4. Malawi: Sensitivity Analysis for Key Indicators of Public Debt, 2018–2028

	Projections 1/										
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
PV of Debt-to-GDP Ratio											
Baseline	**47.0**	**45.7**	**44.9**	**43.5**	**41.7**	**39.6**	**37.9**	**36.1**	34.5	33.0	31.5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	**47**	**43**	**40**	**37**	33	30	27	24	22	20	18
B. Bound Tests											
B1. Real GDP growth	**47**	**48**	**50**	**49**	**49**	**47**	**46**	**45**	**44**	**43**	**43**
B2. Primary balance	**47**	**49**	**51**	**49**	**47**	**45**	**43**	**41**	**39**	**37**	**35**
B3. Exports	**47**	**47**	**49**	**48**	**46**	**44**	**42**	**40**	**38**	**36**	35
B4. Other flows 3/	**47**	**48**	**48**	**47**	**45**	**43**	**41**	**39**	**37**	**35**	34
B5. One-time 30 percent nominal depreciation	**47**	**48**	**45**	**43**	**40**	**37**	34	32	29	27	25
B6. Combination of B1-B5	**47**	**48**	**46**	**44**	**42**	**39**	**37**	35	34	32	31
C. Tailored Tests											
C1. Combined contingent liabilities	**47**	**53**	**52**	**50**	**48**	**45**	**43**	**41**	**39**	**38**	**36**
C2. Natural disaster	**47**	**55**	**54**	**52**	**50**	**48**	**46**	**44**	**42**	**40**	**39**
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
PV of Debt-to-Revenue Ratio											
Baseline	209.7	194.4	196.5	187.4	176.9	166.1	164.2	157.6	151.5	145.7	140.0
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	210	186	179	162	145	130	120	109	99	90	83
B. Bound Tests											
B1. Real GDP growth	210	203	216	211	204	196	199	196	193	191	188
B2. Primary balance	210	210	225	213	200	187	185	177	170	164	157
B3. Exports	210	201	216	206	195	184	182	175	168	161	154
B4. Other flows 3/	210	202	211	201	190	179	177	170	163	156	150
B5. One-time 30 percent nominal depreciation	210	205	199	187	172	157	150	139	129	119	110
B6. Combination of B1-B5	210	204	204	190	177	164	160	152	148	143	138
C. Tailored Tests											
C1. Combined contingent liabilities	210	227	228	216	203	190	187	180	173	166	160
C2. Natural disaster	210	234	236	224	211	199	197	190	184	178	172
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Debt Service-to-Revenue Ratio											
Baseline	29.7	36.3	43.4	46.9	49.2	48.1	47.1	46.2	43.8	41.1	38.5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2018-2028 2/	30	34	38	38	37	33	30	26	23	20	18
B. Bound Tests											
B1. Real GDP growth	30	37	48	54	59	60	61	61	60	58	56
B2. Primary balance	30	36	53	64	63	58	56	53	49	46	43
B3. Exports	30	36	44	47	50	48	47	46	44	42	40
B4. Other flows 3/	30	36	44	47	49	48	47	46	44	42	39
B5. One-time 30 percent nominal depreciation	30	35	42	43	47	46	45	44	42	39	36
B6. Combination of B1-B5	30	35	43	52	53	50	47	46	44	43	41
C. Tailored Tests											
C1. Combined contingent liabilities	30	36	64	65	63	59	56	53	49	46	42
C2. Natural disaster	30	37	68	69	66	62	60	57	53	50	46
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

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

Appendix I. Letter of Intent

October 30, 2018

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

Dear Madame Lagarde:

1. We have made solid progress toward our program objectives under the IMF's Extended Credit Facility (ECF), notwithstanding continued challenges from climate shocks, power shortages, and election-driven spending pressures.

2. Most continuous and end-June 2018 quantitative performance criteria (QPC) were met, with two of the QPCs significantly overperforming. The QPC on the primary fiscal balance target (adjusted for deviations in budget support, dedicated grants, and debt service payments relative to program request) was missed due to unexpected maize purchases, court-ruled arrears payments, and increases in spending to hold elections. Strong remedial actions are being taken, including adopting a tighter than originally agreed fiscal stance in FY 2018/19. We have also identified non-priority spending items that can be cut to partially offset any future shortfalls in grants. We are coordinating with donors to improve the accuracy of our information on donor flows. The QPC on non-concessional external debt was missed due to an oversight in the Technical Memorandum of Understanding, which has been amended going forward.[1] We continue to implement measures to strengthen our debt management.

3. Some structural benchmarks (SBs) were met on time. Most of the remaining SBs were delayed due to unexpected capacity constraints and will be completed by end-October. The appointment of an IMF resident PFM advisor, after a four-month gap (June-October), is very

[1] A nonresident bank purchased Treasury Notes of MK 92 billion in the domestic market, which constitutes contracting of new non-concessional external debt according to the Technical Memorandum of Understanding (TMU). This is due to an oversight in the TMU which excluded Treasury Bills but not Treasury Notes from the items subject to the QPC. The definition of the external debt QPC in the TMU has been modified going forward to exclude both Treasury Notes and Treasury Bills from the QPC on new non-concessional external debt.

welcome and will support us in meeting future SBs. The indicative target (IT) on social spending was met but the IT on no new domestic arrears was missed by MK 1 billion.

4. We are actively entrenching macroeconomic stability and enhancing more inclusive and resilient growth, in line with the Malawi Growth and Development Strategy (MGDS) III and the policies agreed in our macroeconomic program supported by the ECF. Despite growing inflationary pressures, we have contained inflation to single digits. Economic growth is expected to accelerate from just above 3 percent in 2018 to around 4 percent in 2019 and to 6-7 percent over the medium term.

5. We are committed to maintaining debt sustainability while pursuing our ambitious infrastructure development plans. We will continue to ensure that new loans are concessional and accompanied by solid feasibility studies from an independent third party. In the event of an exceptional case, non-concessional borrowing could be considered in the context of later reviews based on its extraordinary merits (e.g., growth-criticality), along with early consultation with the IMF and the World Bank.

6. The attached Memorandum of Economic and Financial Policies (MEFP) describes the progress made in recent months toward the objectives laid out in our ECF-supported economic program. It also updates the previous MEFP and highlights the policy steps to be taken in the months ahead. Program implementation will be monitored through quantitative performance criteria, structural benchmarks and indicative targets as described in the Technical Memorandum of Understanding (TMU), Attachment II.

7. Based on the strength of the policies outlined in this letter and the MEFP and considering our performance under the program including through prior actions, we request (i) waivers of non-observance for the QPC on the primary fiscal balance and the continuous QPC on new non-concessional external debt; (ii) modification of the end-December 2018 PCs on reserve money, net international reserves of the RBM, and the primary fiscal balance; and (iii) the completion of the first review under the ECF.

8. We are confident that the policies contained in the attached MEFP are adequate to achieve the objectives of our program, but we will take any further measures that may be needed to attain these objectives. The Government of Malawi will consult with the Fund staff on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP, in accordance with Fund policies on such consultations. Malawi will provide the Fund staff with any information that may be necessary for monitoring the implementation of the measures to achieve program objectives.

9. The Government of Malawi authorizes the IMF to make this letter and the attached MEFP and TMU, as well as the related Staff Report available to the public, including through the IMF internet website.

Yours sincerely,

/s/

Mr. Goodall E. Gondwe
Minister of Finance, Economic Planning and Development

/s/

Dr. Dalitso Kabambe
Governor of the Reserve Bank of Malawi

Attachments:

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

Attachment—I. Memorandum of Economic and Financial Policies

October 30, 2018

RECENT ECONOMIC DEVELOPMENTS

1. **Malawi's economic growth has moderated while inflationary pressures have risen.**

- The economy is expected to grow at 3.2 percent this year, down from 4 percent last year. The slowdown reflects uneven rainfall and insect infestations weighing on agricultural production, except the tobacco harvest which has been strong. The deployment of diesel generators partly improved electricity generation capacity but supply shortages continue to challenge manufacturing and wholesale and retail trade. Continued macroeconomic stability is supporting confidence.

- While remaining in single digits, inflation rose from 7.1 percent at end-2017 to an anticipated 9.5 percent for end-2018. Upward pressures this year stem from higher maize prices and increases in fuel prices (15 percent in July/October) and electricity tariffs (45 percent in February/July/October).

2. **Fiscal policy faced challenges during FY 2017/18.**

- When the ECF arrangement was approved, the overall deficit combined with arrears payments was expected to exceed the original budget by 3.2 percent of GDP. This was due to underperformance of tax revenues (reflecting weaker than expected economic activity) and higher-than-budgeted spending from the unexpected bailout of ADMARC's maize purchase loan (1 percent of GDP), higher-than-expected domestic interest rates pushing up the interest bill, and arrears payments. These spending overruns were only partly offset by reduced domestically-financed development spending while a substantial shortfall in grants was offset by reduced foreign-financed capital spending.

- On the above basis, we set a primary deficit target of 3 percent of GDP under the ECF arrangement. By end-June 2018, the primary deficit target (a performance criterion under the ECF arrangement) was missed by 0.9 percent of GDP (adjusted for shortfalls in grants). This was due to larger-than-expected maize purchases—to ensure food security after poor maize harvests in some parts of the country—increases in election-related spending, and arrears payments. In accordance with the performance criteria under the ECF arrangement, we did not incur any external payment arrears. The performance criteria on the contracting of new non-concessional external debt was considered met but technically missed due to an oversight in the Technical Memorandum of Understanding (TMU).

- The domestically-financed portion of the fiscal deficit was financed by banks and non-banks and there was no net financing by the Reserve Bank of Malawi (RBM). Instead, the RBM's holdings of government securities was reduced by MK 43 billion during FY 2017/18—far exceeding the

performance criterion under the ECF arrangement that set a ceiling of MK 69 billion on RBM financing of the government.

3. **Outstanding arrears dating back to FY 2012/13 were mostly paid in FY 2017/18 largely through the issuance of zero interest promissory notes (1.5 percent of GDP).** Some of the past arrears are still being disputed in court cases. As of end-June 2018, MK 8 billion of court-ruled arrears, interest, and legal fees still need to be settled. About MK 1.1 billion (0.02 percent of GDP) of new arrears were accrued in FY 2017/18—which are in various stages of settlement. We intend to settle all certified arrears (including those resulting from court cases) expeditiously and apply sanctions to controlling officers who incurred arrears without the approval of the Minister of Finance. We will also mandate MDAs and sub-vented organizations that accrued fresh arrears to resolve them without resorting to the Treasury.

4. **We have maintained a tight monetary policy stance since mid-2016.** The policy rate has been kept at 16 percent after a 600 basis point reduction in 2017 in response to a trend decline in nonfood inflation. The interbank rate is now closely aligned with the policy rate and remains well within the rate corridor that was introduced in early 2016. On average, reserve money growth has slowed since end-2017 and its end-June 2018 stock was within the upper bound set under the ECF arrangement (a performance criterion).

5. **The Kwacha has been stable against the US dollar since December 2016**. This reflects the success of our monetary policy, overall favorable balance of payment developments, and gradually improving confidence in the economy. The real effective exchange rate appreciated 1.3 percent during the first seven months of 2018 relative to the same period in 2017. Net international reserves significantly overperformed its end-June target (a performance criterion under the ECF arrangement) by $119 million.

6. **Banking system resilience has improved.** On aggregate, the banking system has been well capitalized and profitable. Non-performing loans (NPLs) declined from 15.7 percent at end-2017 to 9.5 percent in August 2018 mainly due to write offs and loan recovery. Over the same period, provisions almost doubled with the adoption of IFRS9 requirements. The situations of two banks that were at the borderline of the minimum core capital requirement in December 2017 have improved significantly through capital injection, asset recovery, and write-offs. Nevertheless, the RBM's June 2018 stress test showed that several individual banks are vulnerable to credit, liquidity, and interest rate shocks.

ECONOMIC OUTLOOK AND POLICIES

A. Economic Outlook

7. **Economic growth is expected to rebound to 4.0 percent in 2019 and rise towards 6.5 percent over the medium term.** In the near term, economic activity will be driven by increased electricity generation and growing infrastructure investment. Over the medium term, crop diversification (e.g., cassava and sweet potatoes), improved irrigation, enhanced electricity generation, better road and telecommunication networks, increased donor assistance, and greater access to finance should support growth. Combined with on-going stabilization, reform programs (including those to improve competitiveness) and increased investment will solidify confidence, spur economic diversification, and support higher and more sustained inclusive growth and employment—including capitalizing on our young and dynamic population. Inflation is expected to remain at around 9 percent in 2019 with continued upward pressures from food prices and electricity tariff increases. Over the medium term it is expected to converge to our objective of 5 percent in line with strong fiscal and monetary policy implementation and declines in food and international fuel prices.

8. **Short-term risks are tilted to the downside.** Malawi's agriculture-driven economy is vulnerable to weather and pest shocks. Food security should be preserved by the already accumulated substantial food reserves and we are closely monitoring the situation. Spending pressures remain a risk in the run-up to the 2019 elections and slow reform implementation could further postpone donor support. Fluctuations in foreign exchange revenues, including volatile tobacco exports and short-term capital flows could also induce stress on the exchange rate. A slower than expected disinflation process could raise interest rates, increasing the government's interest bill and hampering access to finance. On the upside, better than expected harvests and higher than expected commodity prices could boost medium-term growth.

B. Monetary and Financial Sector Policies

9. **Monetary policy will continue focusing on entrenching disinflation**. It will aim to maintain the inflation rate in single digits while keeping real interest rates significantly positive. We will continue to exercise caution in our policy rate decisions in order to firmly anchor inflation expectations. Should inflationary pressures gain momentum, monetary policy will be further tightened (with the exception of liquidity provision to banks facing liquidity challenges). We will keep interbank rates within the corridor and concentrate on a few tenors in our repo operations.

10. **We will complete the transition to an interest rate-based operational framework and aim to adopt inflation targeting over the medium-term**. To this end, we will continue to improve primary and secondary market operations to further strengthen monetary policy transmission. Building on the IMF's Technical Assistance, by end-June 2018, we already developed a monetary policy communication strategy (a structural benchmark under the ECF arrangement) aimed at improving communication with all stakeholders and the public to enhance policy credibility. We plan to publish this strategy by end-October 2018. Supported by greater fiscal discipline, our policy framework and execution will be sufficient to anchor inflation expectations. We will continue to expand capacity in developing high frequency data, liquidity forecasting, and the forecasting and policy analysis system (FPAS) modeling.

11. **We will take significant steps to bolster the RBM's independence and effectiveness.**

- We will continue to gradually reduce the RBM's holdings of government securities. In recent years, the RBM's financing of government debt raised its holding of government securities to around 40 percent of its assets. A broadly equivalent amount of open market operations (OMOs) was used to mop up the excess structural liquidity. We will develop a multi-year strategy by September 2019 to gradually unwind most of these securities, taking into account the impact on the yield curve and on market appetite for primary issuance by the government. As part of this strategy, we will (i) reduce the RBM's existing OMO liabilities (to the extent it sells or stops rolling over government securities from its portfolio); and (ii) reach agreement between the government and the RBM on a switching operation that converts some of the existing RBM portfolio of government securities from long-term notes into maturities that would facilitate their use in OMOs (either by outright sale or in repo transactions). To ensure an orderly process, we will align the timing of this switching to OMO needs and the government will refinance these securities in the market on maturity (instead of asking the RBM to rollover its holdings or placing new securities with the RBM). Once the strategy has been developed, we will clearly communicate it to the public in order to smooth market reactions.

- We are repealing and replacing the RBM Act with a new RBM Act 2018 to enhance the mandate of the RBM— including its's autonomy and eliminating avenues for monetization of deficits (except for cash flow management). The amended Act, which is in line with the IMF Safeguards Assessment recommendations, will be submitted to Parliament by mid-November 2018. Revisions to the PFM Act will be aligned with the amended RBM Act and aim to strengthen the PFM regulatory framework.

12. **Financial sector stability will continue to be safeguarded**.

- By March-2019, all banks are expected to comply with IFRS9 standards, which went into effect in January 2018. The directive related to IFRS9 (Financial Services and Financial Asset Classification Directive) was gazetted in April 2018. We will ensure that most banks increase provisioning and

reduce their NPLs towards 5 percent by end-2018. To reduce the time required to recover collateral associated with NPLs, we will keep encouraging banks to improve analysis of collateral quality, including through continued enhancement the collateral registry.

- To improve banking system efficiency, we have taken measures to reduce the banking system's overhead costs (e.g., credit referencing system and the national ID registry). Going forward, as T-bill rates decline, banks that have been relying on government securities for their profit margins will need to modify their business models and reduce interest rate spreads. To address loan concentration risks, we will continue close monitoring, surveillance of large borrowers, and enforcement of the single borrower exposure limit. Regulations aimed at enhancing the consolidated and Domestic Systemically Important Banks supervision will take effect as of end-March 2019.

- Given rising bank lending in foreign currency, we will remain vigilant and ensure that all banks meet the net open position requirement and that lending in foreign currency is made particularly to clients with sources of foreign currency earnings. To this end, in April 2018, we issued the Financial Services (Foreign Currency Lending Ratio) Directive that limits foreign currency lending to borrowers engaged in foreign currency generating activities and up to 90 percent of a bank's foreign currency deposit balance.

13. **New initiatives are gradually being implemented.** Regulations related to the revised AML/CFT framework that was enacted in 2017, are being developed and we plan to gazette them by December 2018. We will formulate a roadmap for increasing access to finance (especially for small and medium size enterprises (SMEs)) by December 2019 and are already engaging the financial sector to improve their credit provision to SMEs. We will focus on developing skills in the banking sector and increasing financial literacy amongst the population. We will further improve financial infrastructure, including facilitating mobile banking infrastructure and increasing non-bank financial intermediation. Finally, we will increase protection of creditors' and borrowers' rights by improving contract enforcement.

14. **We will keep strengthening the regulatory framework of the financial system**. To this end, we will re-submit to Parliament, before end-June 2019, amendments to the Banking Act of 2010 and Financial Services Act of 2010 for eventual enactment. These amendments, which were informed by IMF technical assistance recommendations, will align the legal framework for bank resolution closer to best practices and provide more options for dealing with problem banks. They were submitted to Parliament in March 2015 but sent back to the Minister of Justice for clarification of a few sections. In an effort to operationalize the Payment Systems Act, which was passed by Parliament in June 2016, the RBM issued the Interoperability of Retail Payment Systems Directive in September2017, which supports interconnectivity between all retail payment solutions. In July 2018, the RBM also issued the Financial Services (Consolidated Supervision for Banks) Directive, four

Directives to Consolidate Financial Supervision (Licensing, Corporate Governance Requirements, Capital Adequacy and Credit Risk Management), and the Financial Services (Governance Requirements for Banks and Bank Holding Companies) Directive. The RBM is also preparing E-money Regulations, and the directive on mandatory use of point of sale (POS) devices by qualifying merchants.

15. **We are fully committed to the floating exchange rate regime.** We see this as a fundamental precondition for the success of our economic policies as it cushions shocks and supports economic diversification. We intend to develop a well-sequenced action plan to support greater exchange rate flexibility. It would deepen the interbank FX market and moderate the RBM's role to dampening excess volatility and accumulating reserves when needed. As part of the action plan, the RBM will identify and communicate to the public the objectives and modalities of FX intervention; frequently and regularly publish prices and volumes of interbank transactions; and conduct prudent risk management and oversight. We will also consider a more transparent auction-based system of FX intervention.

C. Fiscal Policy

16. **Our fiscal policy stance will support disinflation and help maintain debt sustainability**. To this end, we will contain spending within available resources, avoid accumulation of domestic and external arrears, and avoid non-concessional external borrowing. Continued implementation of prudent fiscal policies in the near- and medium-terms is necessary to keep the public debt-to-GDP ratio on a downward trajectory and prevent the private sector from being crowded out and productive government expenditure from being replaced by debt servicing costs.

17. **The approved FY 2018/19 budget foresees a relatively high primary deficit (0.8 percent of GDP) but we will aim to restore the budget balance**. Compared to FY 2017/18, we have increased wages (by an 18 percent weighted average) and hired more teachers and medical staff (to be funded by higher tax and non-tax revenues), we will target a primary fiscal balance of 0.1 percent of GDP. The significant tightening relative to FY 2017/18 includes corrections for last year's spending overruns and measures to help cope with this year's expected shortfall in budget support. Important measures we will adopt to achieve this target include:

- Expeditiously implement and enforce tax measures announced in the 2018/19 budget, including new transfer-pricing rules, debt-to-equity ratio, VAT withholding and VAT reverse charge mechanism on imported services.

- Enhance tax administration efforts based on more efficient use of risk analysis and progress in cleansing the tax registry.
- Increase user fees and charges to adjust for inflation and progress toward marginal cost pricing and improve their enforcement.
- Revise dividend policies to ensure profits and surpluses realized by SOEs are duly remitted to the government.
- Reinforce collection of tax arrears (e.g., use of distraint actions), including those owed by parastatals. All remaining tax refund arrears will be cleared. We will also ensure Malawi Revenue Authority (MRA) has sufficient resources (at least 3 percent of gross tax collections) to pay tax refunds on time.
- Reduce generic goods and services spending in non-priority areas (e.g., limiting internal travel, purchase of motor vehicle, and office supplies). Meanwhile, non-essential recurrent expenditures will be strictly limited.
- Reducing transfers to public entities by improving their revenue generating capacity. Reforms in state owned enterprises (SOEs, see below) will also reduce the likelihood of bailout requests.
- Reducing the maize procurement budget (assuming no extraordinary needs during FY 2018/19) while sustaining reforms to FISP.
- Social spending will be safeguarded, and if possible, increased as its quality improves.
- Domestically financed capital spending will be carefully aligned with implementation capacity and there will be an increased focus on enhancing spending efficiency.

18. **We plan to step up measures to enhance the oversight of SOEs.** Weak oversight and financial reporting makes it difficult to adequately monitor and manage risks to the budget and public debt from the SOEs. In this regard, we intend to finalize and issue regulations, policies, and guidelines by December 2018 that cover issues of ownership, payment of dividend and surplus, and preparation of the performance management plans and budgets (PMPBs). The mandate of the Public Finance Management Systems (PFMS) will be revised in line with revisions to the PFM Act. We will conduct pilot audits of the largest SOEs in collaboration with National Audit Office (NAO) and submit these reports to Parliament by June 2019. By February 2020, we plan to submit to Parliament and publish on the MoF website a consolidated annual report on SOEs, including risk analysis case studies on ESCOM, ADMARC, and the Blantyre Water Board that are in line with the recommendations of the IMF's recent technical assistance in this area. We will also develop a prototype SOE database by March 2019.

19. **As part of our efforts to raise spending efficiency, we aim to enhance our public investment management.** We will prioritize (with rankings) all public investment projects based on rigorous cost-benefit analysis, absorptive capacity, growth, poverty reduction, and debt sustainability considerations. We will conduct pilot ex-post reviews/performance audits of some major capital projects in collaboration with the NAO (end-June 2019). We will also increase the usefulness of the Public-Sector Investment Program (PSIP) database as a platform for the oversight and monitoring of investment projects, beginning with an audit of the PSIP database's coverage and the efficiency and timeliness of its processes by December 2019.

20. **Over the near- and medium-terms, we are committed to implementing broad-based tax reforms to foster a simple, efficient, transparent, and fair tax system.**

- To strengthen tax administration, we will (i) continue to advance a risk-based approach to tax compliance through increased data analysis; (ii) enhance the tax registry, improve the registration system, and enlarge the tax base (under 50 percent of the TINS issues are active taxpayers); (iii) place stiff penalties on malpractice of the use of EFDs and other instances of non-compliance, including due to abuse of transfer-pricing regulations; (iv) target to improve on-time filing and payment compliance across all tax types to at least 50 percent; and (v) adopt an integrated tax administration system (ITAS) by December 2019 which will also improve transparency of business processes and reduce corruption. Some key milestones in the rollout of ITAS include (i) cleansing data for the tax registry by September 2019; (ii) migrating data for all active taxpayers by December 2019; and (iii) begin piloting test ITAS in the LTO and two other tax offices by September 2019.

- In tax policy, we will continue to streamline tax incentives, review the industrial rebate scheme, discontinue discretionary granting of tax holidays, expand the VAT base by removing unnecessary exemptions, improve SME taxation, assess the implications of the PAYE allowance increase, and review taxation of small taxpayers. We will also undertake a comprehensive review of our tax system with a view to mobilize more domestic revenue and increase efficiency.

- We are also committed to working with donors to improve the accuracy of information on donor flows, especially the disbursements. This will be done through enhanced use of the aid management platform and joint portfolio reviews.

21. **Our near- and medium-term budgeting plans include enhancing the composition and quality of government spending, while containing fiscal slippages.** Unbudgeted expenditures (e.g., in goods and services) and non-essential recruitment will be avoided while wage increases will be limited to the inflation rate and FISP reforms will continue. Any shortfalls in grants will be partly compensated by cutting non-priority spending (contingency items in the budget include limiting external travel and deferral of non-priority maintenance and investment projects, altogether about

0.2 percent of GDP). The composition of public investment will continue focusing on pro-growth and poverty reducing expenditures. With high development needs and limited fiscal space, raising efficiency of spending in priority areas such as social spending will be at the core of our medium-term budgeting plan. To do so, we shall put into place measures to enhance the allocational mix of health and education budgets, improve fiscal transparency and accountability at national and sub-national level, strengthen program-based budgeting, and engender efficiency in frontline service delivery.

22. **We will also develop a plan to address the challenges involved in the current decentralization process.** This will include addressing issues of capacity and controls at the local level and eventually adopting a legal framework for budget systems and fiscal policy coordination.

D. Public Financial Management Reform

23. **We continue to make strides in public financial management reforms**. We have routinized monthly bank reconciliation (a structural benchmark under the ECF arrangement), except for salary accounts which will be incorporated by December 2018 for FY 2016/17, by June 2019 for FY 2017/18, and by September 2019 for FY 2018/19 when we will also become current for FY 2019/20. We will continue to maintain fully reconciled domestic debt data within and across each of the responsible units in the RBM and MoF (a structural benchmark under the ECF arrangement). To improve control and accountability, we have routinized monthly submission by MDAs of fiscal reports on the monthly funding release for two out of five reports (a structural benchmark under the ECF arrangement) and publication of the report summaries on the MoF website. The remaining three will be completed by end-October 2018. We will continue to strengthen the quality control of these reports (including strengthening sanctions on controlling officers in MDAs for misreporting or non-compliance). Given its strategic importance in expenditure control and arrear prevention, we will set-up an online commitment control system. Having adopted a commitment template that unifies data coverage and definition (at the MDA level), we have begun publishing consolidated monthly statements of the government's commitments on the MoF website including information on overdue (for more than 90 days) payments (a structural benchmark under the ECF arrangement). More systematic commitment control will enable timely detection of arrears and sanctioning of controlling officers who incurred them without approval of the Minister of Finance. We also plan to complete adjustment of the bank reconciliation of FY 2013/14-14/15 based on the findings of the forensic audit and adjust the opening and closing balances of the bank reconciliation of FY 2015/16. This will be completed once the criminal investigation based on the findings of the forensic audit are complete, which will enable wider dissemination of the audit report.

24. **Building on recent advances, we plan to further improve our financial reporting**. We intend to produce quarterly certified consolidated financial reports within six months after the end of the quarter with fully reconciled items. In the same vein, we will keep producing and publishing on the MoF website monthly budget execution reports by vote and economic classification. Once all commitments are included in IFMIS, these will be based on actual expenditure and not funding. With these, we are confident that the first quarter 2018/19 financial reports will be submitted to the Auditor General by end-March 2019 with fully reconciled bank accounts. Timely reporting will mean that Parliament will discuss reports that are not only reliable but also relevant. In addition, we aim to complete the rollout of the electronic fund transfer (EFT) by June 2019, including to the entire salary account (not just the net salary payment). This, combined with the Treasury Management System (TMS) module in IFMIS will permit automatic daily bank reconciliation.

25. **Clearance of the backlog in bank reconciliation will provide a good basis for implementing a new IFMIS.** Drawing on the IMF's technical assistance and the World Bank's advice, we will put in place a realistic and comprehensive implementation strategy (e.g., a phased approach in IFMIS implementation, a master plan, and a vendor implementation plan), a transparent governance framework (e.g., remobilizing the IFMIS Steering Committee by end-October), credible quality assurance, and a robust strategy to assure readiness (e.g., network/data center and business process re-engineering). Recognizing that implementing a new IFMIS will take time, we will continue allocating resources towards maintenance of the current IFMIS and expand its applications to include all TSA sub-accounts (including projects, receipts, and debt servicing payment) by June 2019 and expenditure commitments (including linking HRMIS and IFMIS) and debt transactions by August 2019. Once this expansion of IFMIS coverage is complete, we intend to publish commitments against budget allocation as well as outstanding bills by August 2019. We will also shift from monthly to quarterly budget release and allow MDAs to commit to the released budget through IFMIS beginning July 2019.

26. **Operations of the Cash Management Committee have been strengthened.** This was done by establishing a fully functional Cash Management Unit under the Secretary to the Treasury. In June, the unit prepared a cash forecast of the next twelve months (for FY 2018/19) and we plan to make this a monthly practice. From December 2018, the unit will prepare a variance analysis on forecasting errors every three months, report a summary of the meeting minutes, and take actions to improve MDA submissions. We will also introduce a Treasury Single Account (TSA) by June 2019 and bring most bank accounts into IFMIS by June 2019. We have consolidated banks accounts and aim to rationalize all remaining commercial bank accounts under the TSA by June 2019.

27. **We are developing a medium-term strategy that aims at solidifying the present gains**. We will embark on building human capacity through training to ensure that the reforms being implemented are sustained. A review of the PFM Act, currently underway, aims to ensure that laws and regulations are brought in line with the reforms that are taking place and emphasize a performance-based rewards and sanctions regime. Strengthening of oversight institutions such as the National Audit Office, Central Internal Audit Unit and the Public Accounts Committee will continue under the medium-term strategy that is being developed. We will also strengthen medium-term performance and efficiency of our budget by better linking MDA strategic planning and budgeting, improving the credibility of the Medium-Term Expenditure Framework, and strengthening the framework for engaging key stakeholders. Building on the enactment of a new Procurement Act, which closes various loopholes under the old act, we intend to improve our procurement framework continuously, to enhance transparency, control, and accountability. We will start by publishing all procurement information on the Public Procurement and Dispose of Assets Authority website. We will also use the performance contract with controlling officers to hold them accountable for adhering to relevant rules and procedures and strengthen procurement audits. Over time, we will consider gradually moving to an e-procurement system—as a part of the overall IFMIS implementation strategy.

E. Structural Reforms

28. **The Malawi Growth and Development Strategy (MGDS III) envisages a significant improvement of Malawi's business climate**. The objective of building productivity and competitiveness will require unlocking private sector potential. To this end, we will continue to improve the business environment, including by easing procedures to start a business and deal with construction permits, strengthening contract enforcement, and enhancing insolvency processes.

29. **We will also implement deep reforms in agricultural regulations and market intervention systems, agricultural subsidies, and land management systems:**

- ***ADMARC:*** A comprehensive strategic review of ADMARC (Agricultural Development and Marketing Corporation) has been completed and the report will soon be finalized. Based on this review's findings, we will implement a reform program to better balance maize price stabilization against fiscal sustainability and improve transparency and efficiency in this area.

- ***Control of trade:*** The Control of Goods Act has been amended to conform to international trade best practices and efforts are underway to finalize subsidiary legislation which will adequately define the public interest grounds needed to determine the thresholds for intervention. New bans or review of existing bans will be reviewed in consultation with stakeholders.

- ***FISP:*** We will continue FISP reform, focusing on containing its budget impact, an increased role for the private sector, better governance, and better beneficiary targeting.
- ***Land reform:*** We will continue implementing new land codes based on the lessons learned from our pilot programs.

F. Debt Management

30. **Malawi is classified as being at moderate risk of external debt distress and at high overall risk of debt distress due to high domestic debt**. We will limit our unified external borrowing to high priority projects which are in line with the MGDS III and maximize the grant element of external borrowing to ensure that total debt (and guarantees) contracted is consistent with debt sustainability. While MGDS III lays out ambitious goals for critical infrastructure projects, we are committed to ensuring that their financing preserves debt sustainability.

31. **We plan to strengthen debt management and monitoring**. We have developed a comprehensive medium-term debt strategy and will keep updating it. The Debt Management Committee is operational and will assess both domestic and external borrowings. The committee will ascertain loan concessionality and ensure debt sustainability taking into consideration the entire borrowing plan and the medium-term debt strategy. Borrowing in the FY 2018/19 budget will be consistent with our objectives of social development and poverty reduction and debt sustainability. We will ensure that new loans are, in principle, concessional and accompanied by solid feasibility studies from an independent third party. In the event of an exceptional case, non-concessional borrowing could be considered in the context of later reviews based on its extraordinary merits (e.g., growth-criticality) along with early consultation with the IMF and the World Bank. We will further improve our debt monitoring by allocating sufficient resources and increase training.

32. **We will take steps to improve coordination of debt and liquidity management as well as deepen the domestic debt market.** By December 2019, the activities of the MoF's Debt and Aid Management Division will be streamlined by establishing a specialized unit to undertake front office roles on domestic debt management and operations in collaboration with the RBM. Better cash flow forecasts (as outlined above) will improve debt and liquidity management coordination. We plan to gradually lengthen the maturity of government securities and develop a government securities benchmark issuance policy that will concentrate the amounts of benchmark tenors in maturity buckets of 3, 5, 7, and 10-years to develop the government securities yield curve. We will continue to develop the T-Bill yield curve by issuing 91, 182, and 364-day maturities in auctions. We plan to publish the indicative amounts in an issuance calendar that will be confirmed closer to auctions through announcements, and we will adhere to these announced auction schedules.

G. Fuel Pricing and Import Regime

33. **We will continue to improve our fuel security situation.** We have three fuel storage depots (capable of holding about 25 percent of annual consumption) and guidelines for their operation which clarifies the framework for collaboration between the storage operator and fuel importers or distributors. The framework has been running well with fuel importers who are in the process of integrating the facilities as a part of their logistics chain. It will enable the augmented storage cost to be fully passed on to the pump price. Since 2013, our fuel import regime had been based on private sector imports with cost recovery guaranteed by the automatic fuel pricing mechanism. Fuel imports were done jointly by a traditional private sector consortium (PIL) and NOCMA, based on their 2013 MOU, which expired in June 2018. Two new pieces of legislation have been promulgated to develop the wholesale and retail markets.

34. **The fuel import regime will remain unchanged for the rest of the 2018/19 fiscal year.** However, we will continue to evaluate the balance of security and efficiency under the current regime as more experience is gained. In particular, we are committed to ensuring a level-playing field for all market participants, while also putting in place a safeguard against, potentially disastrous, supply disruption. Given the importance of safeguarding governance risks in the sector, any further change in the fuel import regime or operation of the facility will be done in a transparent manner, with full private sector participation. We will produce, publish, and discuss with all stakeholders a fully-costed and well-thought out proposal for any change prior to implementation.

35. **We remain committed to retaining and implementing the fuel price automatic adjustment mechanism.** This mechanism has enabled full cost recovery by fuel importers while precluding government subsidy. The rule is that over ±5 percent change in formula-based underlying price triggers a price adjustment; and all other price changes are absorbed by the Price Stabilization Fund (PSF). Recently, to avoid sudden or large pump price increases, discretion has been applied and the PSF has been used to subsidize fuel distributors in place of the automatic price adjustment mechanism. This led to a pause in the adjustment of prices at the pump since October 2016. However, recent increases in imported oil prices led the Malawi Energy Regulatory Authority (MERA) to approve significant increases in petroleum and diesel prices in 2018. This will help narrow the gap between the landed cost and pump price of fuel and protect the PSF. Going forward, we intend to exercise strict restraints on the use of discretion over the ±5 percent price adjustment rule with a view to protect the PSF and avoid a backloaded, lumpy price adjustment. To increase transparency and accountability, we will consider disclosing more information on the use of the PSF (e.g., its financial statement).

H. Gender Equity

36. **We take note of the importance of addressing gender inequality in achieving inclusive growth**. Gender disparities hinder economic growth by impeding full realization of Malawi's human resource potential and aggravate economic exclusion, making it harder for woman to escape from poverty. Policy interventions will continue to focus on adolescent girls given the high potential impact of breaking the cycle of deprivation at an early stage of life.

- ***Ending child marriages:*** Last year's constitutional amendment to raise the minimum age for marriage from 15 to 18 was a critical first step. In addition, we plan to develop a comprehensive national program of action which will entail multifaceted strategic interventions—from social protection, to law enforcement, to health (particularly sexual and reproductive health), child protection, and public education.
- ***Keeping girls in school:*** We will continue to facilitate larger and more effective investment on classrooms, teachers, and education materials. We will also broaden our demand side interventions (e.g., more social assistance and targeted subsidy programs; which would be gender-sensitive).
- ***Assets and credit.*** Given the significance of a matrilineal system of land inheritence in Malawi, we are commited to the formalization of customary land rights that are key to women's access to finance. Policy interventions for access to finance, including gender neutral ones, will further help level the playing field.
- ***Labor market policies.*** We will consider non-gender-neutral policy options (e.g., childcare support) to help increase women's labor market participation.

PRIOR ACTIONS AND STRUCTURAL PROGRAM FOR 2018

37. **The macroeconomic policies supported by the ECF will be complemented by a strong structural program, which will make the transmission of economic policy more efficient.** The Prior Actions (Table 2) signal our commitment to a strong reform agenda, while the Structural Benchmarks for 2018-19 (Tables 3a and 3b) seek to reform key sectors of the economy.

Prior Actions

To be completed before program request goes to IMF Executive Board

- Submission to the MoF of the three remaining reports for April-September 2018 (from the continuous SB) by the MDAs and their publication on the MoF website.

- Remobilize the IFMIS steering committee by holding a meeting.
- Publication of the RBM's communication strategy.
- Submit to Parliament amendments to the *RBM Act*, which are in line with the recommendations of the IMF Safeguards Monitoring Report, dated 6 June 2016.

Structural Benchmarks and Program for 2018

Fiscal sector

- Submission of five reports by the MDAs by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted and published 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance (continuous).
- Maintain a transparent commitment control system for all MDAs; MoF to centrally compile consolidated commitments of the government by end of the following month and place it on the MoF website. Classify bills overdue for more than 90 days by age. ST to apply sanctions to the controlling officers of the MDAs for incurring arrears without the approval of the Minister of Finance (continuous).
- Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within six months after the end of each quarter in the first year and within 90 days after the end of each quarter in the second and third. The financial reports should be certified by the Auditor General (continuous).
- Reconcile all bank accounts MG1 and six operating accounts (except salary accounts until September 2019) and ways and means transactions within 90 days after the end of each month signed by the Accountant General and Secretary to the Treasury. The reconciliation should clear all the backlog and have a track record of three consecutive months (continuous).
- Reconcile all debt data between the MOF and RBM (continuous).
- CMU undertakes variance analysis on forecasting errors every three months, reports a summary of minutes of the meeting, and takes actions to improve MDA submissions (end-December 2018).
- Finalize and issue the draft regulations, policies and guidelines covering issues of ownership, payment of dividend and surplus, and preparation of PMPBs (end-December 2018).

Structural Benchmarks and Program for 2019-20

Fiscal sector

- Same continuous structural benchmarks as for 2018.
- Pilot ex-post reviews/performance audits of some major capital projects in collaboration with the NAO (end-June 2019).
- Submit to Parliament a report on the pilot audit of the main public corporations in collaboration with the NAO (end-June 2019).
- Move from monthly to quarterly budget release (set in a conservative manner), and allow MDAs to commit, through IFMIS, up to the released budget (end-June 2019).
- Bring all TSA sub-accounts into IFMIS including projects, receipts and payments (end-June 2019).
- Use IFMIS to record commitments or all types of expenditure (based on purchase orders or contracts) prior to the submission of new contracts to the ST for vetting (includes linking HRMS and IFMIS) and all domestic debt commitments, expenditures, and payments in real time. Disclose on the MoF website information on (i) accumulated commitments against the budget allocation and (ii) outstanding bills classified by age, on a monthly basis, 30 days after the reference period (end-August 2019).
- Audit of the Public-Sector Investment Program (PSIP) database, including the efficiency and timeliness of its processes, and its coverage (end-December 2019).
- Streamline activities of DAD to ensure its front office operations include more active engagement in domestic debt management policies and operations in collaboration with the RBM (end-December 2019).
- Submit to Parliament and publish on the MoFEPD website a consolidated annual report on SOEs (including case studies for ESCOM, ADMARC, and Blantyre Water Board, end-February 2020).

Financial sector

- Develop a strategy to pace the unwinding of RBM holdings of government securities that minimizes adverse effects on public debt management and monetary policy implementation (end-September 2019).
- Develop a roadmap for increasing access to finance (end-December 2019).

PROGRAM MONITORING

38. **The program will be monitored on a semi-annual basis, through quantitative targets (Table 1) and structural benchmarks (Tables 2, 3a, and 3b).** Quantitative targets for end-December 2018 and end-June 2019 are performance criteria while those for end-September 2018, end-March 2019, and end-September 2019 are indicative targets. The second and third reviews under the program will be completed on or after April 15, 2019 and October 15, 2019, respectively.

Table 1. Quantitative Targets, 2018-19[1]

	Target type [2]	2018							2019				
		End-Jun.				End-Sept	End-Dec.		End-Mar.		End-Jun.		End-Sept
								Modified		Modified			
		Prog.	Adj. Prog.	Est.	Status	IT[13]	Prog.[13]	Prog.	IT[13]	IT	IT[13]	Prog.	IT
I. Monetary targets (millions of kwacha)													
Reserve money (ceiling on stock) (upper bound)[3]	PC	303,482		300,792	Met	299,091	323,385	326,115	300,406	308,798	340,106	346,236	340,175
Reserve money (ceiling on stock)[3]		294,643				290,380	313,966	316,617	291,656	299,804	330,200	336,151	330,267
Reserve money (ceiling on stock) (lower bound)[3]		285,803				281,668	304,547	307,118	282,906	290,810	320,294	326,067	320,359
II. Fiscal targets (millions of kwacha)													
Primary balance (floor)[4,5,6]	PC	-144,929	-163,338	-205,170	Not Met	44,906	29,813	-4,456	16,219	-2,684	3,625	89	-1,236
RBM financing of central government (ceiling)[6,7]	PC	69		-43	Met	0	0	0	0	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0		1,000	Not met	0	0	0	0	0	0	0	0
Social spending (floor)[6,9]	IT	186,132		279,952	Met	87,972	175,944	182,207	263,917	273,310	351,889	364,413	103,104
III. External sector targets (US$ millions, unless otherwise indicated)													
Net international reserves of the RBM (floor)[4,5,8]	PC	434.1	408.7	527.7	Met	454.7	480.2	428.6	488.2	436.6	484.5	460.4	473.1
Accumulation of external payments arrears (ceiling)[6,10]	PC	0		0	Met	0	0	0	0	0	0	0	0
New non-concessional external debt contracted (ceiling)[6,10]	PC	0		127	Not Met[12]	0	0	0	0	0	0	0	0
Memorandum items:													
Net foreign assets of the RBM (US$ millions, end of period)[6]		339.8		434.5		360.4	385.9	316.0	393.9	324.0	390.2	347.8	360.4
Budget support (US$ millions)[6]		84.3		89.1		79.1	79.1	0.0	79.1	0.0	79.1	0.0	0.0
Budget support (millions of kwacha)[6]		62,633.8		65,088.4		60,000.0	60,000.0	0.0	60,000.0	0.0	60,000.0	0.0	0.0
Nominal external concessional borrowing (US$ millions)[6]		166		116		35	70	53	104	79	137	105	49
Debt service payments to the World Bank and AfDB (US$ millions)[6]		13.4		12.0		3.8	7.5	19.8	12.1	24.9	16.7	30.1	5.2
Debt service payments to the World Bank and AfDB (millions of kwacha)[6]		9,994		8,781		2,851	5,821	14,680	9,538	18,842	13,337	23,137	4,041
Joint Fund on Health receipts (millions of kwacha)[6]		6,569		0		2,288	4,577	4,577	6,865	6,865	9,153	9,153	1,831
Joint Fund on Education receipts (millions of kwacha)[6]		6,987		4,716		4,325	8,651	8,656	12,976	12,983	17,301	17,311	2,000
Program exchange rate (kwacha per US$)[11]		725		725		725	725	732	725	732	725	732	732

Source: IMF staff projections.

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

[2] "PC" means Performance Criterion and "IT" means Indicative Target. The PC test date for the 2nd Review will be end-December 2018. Test dates for future reviews will be end-June and end-December. End-September and end-March targets are ITs.

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

[4] Targets are subject to an adjustor for budget support and debt service payments, as specified in the TMU.

[5] Targets are subject to an adjustor for donor-funded social sector expenditures consistent with the TMU.

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

[7] Targets are subject to an adjuster equivalent to 10 percent of previous year's tax revenue, as specified in the TMU.

[8] Defined as stocks.

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

[10] Evaluated on a continuous basis.

[11] Starting from End-September 2019, the program exchange rate is changed to the level that reflects the actual (instead of indicative) exchange rate, consistent with the TMU.

[12] A nonresident bank purchased T-notes of MK92 billion in the domestic market, which constitutes contracting new non-concessional external debt according to the TMU. This is due to an oversight in the TMU which excluded T-bills but not T-notes from the items subject to the PC. The definition of the external debt PC in the TMU has been modified going forward to exclude both T-notes and T-bills from the PC on new non-concessional external debt.

[13] Target levels set in IMF Country Report No. 18/115.

Table 2. Prior Actions

Measures	Macro Rationale
Submission to the MoF of the three remaining reports for April-September 2018 (from the continuous SB) by the MDAs[1] and publish on the MoF website.	Improve fiscal transparency.
Remobilize the IFMIS steering committee by holding a meeting.	Improve fiscal transparency.
Publication of the RBM's communication strategy.	Enhance RBM credibility and prepare for the eventual implementation of inflation targeting.
Submit to Parliament amendments to the RBM Act, which are in line with the recommendations of the IMF Safeguards Monitoring Report, dated 6 June 2016.	Preserve financial and debt sustainaiblity.

Sources: IMF staff and Malawian authorities.
[1] Ministry, department, and agency.

Table 3a. Structural Benchmarks 2018

Structural benchmark	Target date	Macro Rationale
Public financial management		
Submission to the MoF of five reports by the MDAs[1] by mid-following month and publication of the summary on the MoF website (except for the reconciliation report which will be submitted and published 6 weeks after the end of the month). Maintain/strengthen sanctions on MDAs for misreporting/non-compliance.	Continuous (monthly from May 15, 2018)	Improve fiscal transparency; prevent accumulation of new domestic arrears; reduce vulnerabilities to corruption.
Maintain a transparent commitment control system for all MDAs; MoF to centrally compile consolidated commitments of the government by end of the following month and place it on the MoF website. Classify bills overdue for more than 90 days by age. ST to apply sanctions to the controlling officers of the MDAs for incurring arrears without the approval of the Minister of Finance.	Continuous (monthly from May 31, 2018)	Better control on all government commitments and arrears, if any.
Prepare quarterly consolidated financial reports (including all MDAs) with fully reconciled bank accounts and publish within six months after the end of each quarter in the first year and within 90 days after the end of each quarter in following years. The financial reports should be certified by the Auditor General.	Continuous (quarterly from March 31, 2019)	Improve fiscal transparency and integrity of the accounting system; routinize reconciliation of all bank accounts; strengthen cash planning; reduce vulnerabilities to corruption.
Reconcile all bank accounts MG1 and six operating accounts (except salary accounts until September 2019) and ways and means transactions within 90 days after the end of each month signed by the Accountant General and Secretary to the Treasury. The reconciliation should clear all the backlog and have a track record of three consecutive months.	Continuous (monthly from July 29, 2018)	Routinize reconciliation of all bank accounts; strengthen cash planning; improve the integrity of the accounting system; reduce vulnerabilities to corruption.
Reconcile all debt data between the MOF and RBM.	Continuous (monthly from April 30, 2018)	Enhance debt management; improve transparency and monitoring of public debt.
CMU undertakes variance analysis on forecasting errors every three months, reports a summary of minutes of the meeting, and takes actions to improve MDA submissions.	End-December 2018	Strengthen cash and debt management; timely implementation of the budget; reduce vulnerabilities to corruption.
Finalize and issue the draft regulations, policies and guidelines covering issues of ownership, payment of dividend and surplus, and preparation of PMPBs.	End-December 2018	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.

Sources: IMF staff and Malawian authorities.

[1] Ministry, department, and agency.

Table 3b. Structural Benchmarks 2019

Structural benchmark	Target date	Macro Rationale
Public financial management		
Pilot ex-post reviews/performance audits of some major capital projects in collaboration with the NAO.	End-June 2019	Improve efficiency of public investment.
Submit to Parliament a report on the pilot audit of the main public corporations in collaboration with the NAO.	End-June 2019	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Move from monthly to quarterly budget release (set in a conservative manner), and allow MDAs to commit, through IFMIS, up to the released budget.	End-June 2019	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; and achieve comprehensive coverage in IFMIS.
Bring all TSA sub-accounts into IFMIS including projects, receipts and payments.	End-June 2019	Enhance cash management; achieve comprehensive coverage in IFMIS; and strengthen controls on bank reconciliation and reporting; reduce vulnerabilities to corruption.
Use IFMIS to record commitments or all types of expenditure (based on purchase orders or contracts) prior to the submission of new contracts to the ST for vetting (includes linking HRMS and IFMIS) and all domestic debt commitments, expenditures, and payments in real time. Disclose on the MoF website information on (i) accumulated commitments against the budget allocation and (ii) outstanding bills classified by age, on a monthly basis, 30 days after the reference period.	End-August 2019	Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption.
Audit of the Public-Sector Investment Program (PSIP) database, including the efficiency and timeliness of its processes, and its coverage.	End-December 2019	Improve efficiency of public investment.
Streamline activities of DAD to ensure its front office operations include more active engagement in domestic debt management policies and operations in collaboration with the RBM.	End-December 2019	Enhance debt management; improve transparency and monitoring of public debt.
Submit to Parliament and publish on the MoFEPD website a consolidated annual report on SOEs (including case studies for ESCOM, ADMARC, and Blantyre Water Board).	End-February 2020	Mitigate fiscal risks asscociated with SOEs; enhance transparency in financial performance and market operations.
Financial sector		
Develop a strategy to pace the unwinding of RBM holdings of government securities that minimizes adverse effects on public debt management and monetary policy implementation.	End-September 2019	Improve debt management and governance.
Develop a roadmap for increasing access to finance.	End-December 2019	Increase financial sector intermediation.

Sources: IMF staff and Malawian authorities.

Attachment—II. Technical Memorandum of Understanding

October 30, 2018

INTRODUCTION

1. **This memorandum defines the quantitative performance criteria, benchmarks, and indicative targets for the program, as described in the Memorandum of Economic and Financial Policies (MEFP) for the period November 21, 2018-April 30, 2021** supported by the Extended Credit Facility (ECF) arrangement, and sets out the data reporting requirements.

2. **Coverage:** The central government includes ministries, departments, and agencies, and all other units of government that exercise authority over the entire economic territory. However, in contrast to the System of National Accounts 1993 (SNA 1993) and Government Finance Statistics Manual 2001 (GFSM 2001) standards, nonprofit institutions that are controlled and financed by the central government are excluded for purposes of this memorandum. The accounts of the monetary authorities include those of the Reserve Bank of Malawi (RBM). Monetary aggregates under the program are based on the nine-bank monetary survey.

QUANTITATIVE PERFORMANCE CRITERIA AND INDICATIVE TARGETS

3. Quantitative performance criteria are established for December 31, 2018 and June 30, 2019 with respect to:

- Reserve money (ceiling);
- Net official international reserves (NIR) of the RBM (floor);
- Primary balance of the central government including grants, cash basis (floor);
- RBM financing of the central government (ceiling);
- Accumulation of external payments arrears(ceiling);
- New non-concessional external debt (ceiling).

4. Indicative targets for March 31, 2019 and September 30, 2019 with respect to the above variables, and for these dates as well as December 31, 2018 and June 30, 2019 with respect to:

- New domestic arrears (ceiling);

- Social spending (floor).

I. Targets for Monetary Aggregates

- Ceiling on the Stock of Reserve Money

5. **A ceiling applies to the upper bound of a reserve money band (set +/-3 percent) around a central reserve money target.**

6. **Definition.** Reserve money is defined as the sum of currency issued by the RBM, including the vault cash of commercial banks, and balances of commercial bank accounts with the RBM. It includes required reserves held for kwacha deposits, other domestic currency liabilities, and other demand and time deposits held with the RBM.

7. **Reporting requirement**. Data on reserve money will be transmitted on a weekly basis. This transmission will include weekly balance sheet of the RBM which will show all items listed above in the definitions of reserve money.

J. Targets for Fiscal Sector

- **Floor on Primary Balance**

8. **A floor applies to the cumulative flow of primary fiscal balance since the beginning of the fiscal year.**

9. **Definition of the primary balance**. The program primary fiscal balance is measured from the financing side as the sum of net financial transactions of the central government – comprising the sum of net domestic borrowing, net foreign borrowing – less domestic and external interest payments.

10. **Definition of net domestic borrowing of the central government:** net domestic borrowing is computed as the sum of (1) net borrowing from the RBM (including, but not limited to, ways and means advances, loans, holdings of local registered stocks, promissory notes, and all government securities minus deposits); (2) net borrowing from commercial banks (including, but not limited to, advances, loans, holdings of local registered stocks, promissory notes, and all government securities minus deposits); (3) net borrowing from nonbanks (including, but not limited to, holdings of local registered stocks and all government securities); and (4) holdings of promissory notes. All government securities and locally registered stocks are valued at cost rather than face value. Transfers from extra-budgetary funds will not be considered revenues for this performance criterion.

They will be treated the same as borrowing from the private sector (as their accounts are outside the definition of government) and therefore as domestic borrowing. Asset sales or privatization revenues will be accounted for under financing as a separate category, separate from domestic or foreign financing in calculating net domestic borrowing.

11. **Definition of net foreign borrowing of the central government**: net foreign borrowing is defined as the sum of project and budget support loans by official creditors (both multi- and bilateral creditors) and commercial external borrowing, minus amortization due. Dedicated grants can finance current spending and be reclassified as project grants if used as foreign financed capital spending.

12. **Definition of budget support:** Budget support includes all grants and foreign financing not directly linked to additional budgetary expenditure. Excluded from this definition is external project financing to fund particular activities, such as financial support from the IMF, and donor inflows (in kwacha) from the U.S. dollar-denominated donor pool accounts for the Joint Funds on health, education, and agricultural, held in the Malawi banking system.

13. **Adjustors:**

- Adjustor on primary balance – budget support: The floor of primary balance will be adjusted upward by the full amount by which cumulative kwacha receipts from budget support exceed the program baseline. In the event of a budget support shortfall, the floor on primary balance will be adjusted downward by the amount subject to the limitation outlined in paragraph 13. Budget support is measured as the cumulative flow from the beginning of the fiscal year. It is recorded in the original currency of disbursement and then converted into kwacha using the program exchange rate listed in Table 1.

- Adjustor on primary balance – donor accounts for the social sector (including agriculture, the national aids commission (NAC), and Joint Funds on health and education): The floor on primary balance will be adjusted upward by the full amount in kwacha by which the donor inflows from the U.S. dollar-denominated donor accounts for social sector (as defined above in this bullet) are higher than in the program baseline. In the event of a shortfall, the floor on primary balance will be adjusted downward by the amount subject to the limitation outlined in paragraph 13. Donor inflows are measured from the beginning of the fiscal year. They are recorded in the original currency of disbursement and then converted into kwacha using the program exchange rate listed in Table 1.

- Adjustor clause on primary balance – debt service payments (defined as payments including both interest and principal): The floor on primary balance will be adjusted upward by the full cumulative amount by which debt service payments to the World Bank (WB) and the African Development Bank (AfDB) fall short of the program baseline. If the debt service payments are

higher than the program baseline, the floor on primary balance will be adjusted downward by the amount subject to the limitation outlined in paragraph 13. The cumulative amount will be measured from the beginning of the fiscal year. The debt service payments are recorded in the original currency of payments and converted into kwacha at the program exchange rate listed in Table 1.

14. **The total downward adjustment to primary balance** from a shortfall, relative to the program assumptions, of (i) budget support, (ii) donor inflows to the donor accounts for the social sector, and (iii) an excess of debt service payments to the WB and the AfDB, will be capped at US$65 million.

- **Ceiling on RBM Financing of the Central Government**

15. **Definition of RBM financing of the central government**. RBM financing of the central government is defined as net borrowing from the RBM by the central government (including ways and means advances, loans, holdings of local registered stocks, promissory notes, and all government securities minus deposits).

16. **Adjustors:**

- For cash management purposes, the ceiling on RBM financing of the central government for September 2018, December 2018, and March 2019 is subject to an upward adjustment of up to 10 percent of the previous financial year's domestic revenue (excluding grants).

17. **Reporting requirement**. Data on the RBM financing of the central government will be transmitted to the IMF on a monthly basis within 4 weeks from the end of the month.

- Ceiling on New Domestic Arrears

18. **Definition of domestic arrears:** Domestic arrears are overdue payment obligations of the central government other than external payment arrears, including on wages and salaries, pensions, transfers, domestic interest, goods and services, obligations arising from court cases, legally established compensation claims, principal payments on domestic loans, and tax refunds. Payments on wages and salaries, pensions, transfers, court-established obligations, and compensations are in arrears when they remain unpaid for more than 30 days beyond their due date. Domestic interest payments are in arrears when the payment is not made on the due date. Payments for goods and services are deemed to be in arrears if they have not been made within 90 days of the due date, or – if a grace period has been agreed – within the contractually agreed grace period. Tax refunds are in arrears if not paid within the time limit as set forth in respective tax laws.

- Floor on Social Spending

19. **Definition of social spending**. Using functional classification of expenditure, social spending is computed as the sum of central government spending on health, education, and government social protection (comprising the government expenditures by the ministries of health, education, and gender, children, disability and social welfare; and NAC, FISP, and maize). In order to maintain Malawi's commitment and progress toward poverty reduction, the social spending allocations in the government budget will not be adjusted downward to meet fiscal targets of the program.

20. **Donor pool-funded expenditures in support social spending**: In support of the health and education sectors, some donors pool resources (the donor pool) in Joint Funds, which are being managed by a fiscal agent. These funds are released outside normal government procedures (i.e., recurrent budget or development Part I budget) to the relevant sector.

21. **Reporting requirement**. Social spending and financial flows into and out of Joint Funds will be reported on a monthly basis from the beginning of the fiscal year.

K. Targets for External Sector

- **Floor on Net International Reserves of the RBM**

22. **Definition of net international reserves (NIR) of the RBM:** The NIR of the RBM is defined as gross reserves minus IMF and other short-term liabilities. The values of all foreign assets and liabilities will be converted into U.S. dollars at each test date using the program cross exchange rates listed in Table 1.

23. **Definition of gross reserve assets of the RBM.** Gross reserve assets are defined by the International Reserves and Foreign Currency Liquidity Guidelines for a Data Template as external assets immediately available and controlled by RBM "for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency's exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing)." (BPM6, paragraph 6.64).

24. **Gross reserve assets include the following**: (i) monetary gold holdings of the RBM; (ii) holdings of SDRs; (iii) the reserve position in the IMF; (iv) foreign convertible currency holdings; (v) foreign currency denominated deposits held in foreign central banks, the Bank for International Settlements, and other banks; (vi) loans to foreign banks redeemable upon demand; (vii) foreign securities; and (viii) other unpledged convertible liquid claims on nonresidents. It excludes the

following: (i) any foreign currency claims on residents; (ii) capital subscriptions in international institutions; (iii) foreign assets in nonconvertible currencies; (iv) transfers of foreign currency claims to RBM by other institutional units in Malawi just prior to reporting dates with accompanying reversals of such transfers soon after those dates; (v) assets obtained through currency swaps of less than three months duration; (vi) gross reserves that are in any way encumbered or pledged, including, but not limited to: (a) assets blocked when used as collateral for third party loans and third-party payments, or pledged to investors as a condition for investing in domestic securities; (b) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and (c) foreign reserves blocked for letters of credit.

Table 1. Cross rates for Nominal Exchange Rate and Gold Price for the 2018-21 ECF Arrangement

	31-Dec-2017
Gold bullion LBM [1] US$/troy ounce	1,257.13
SDR to US$ exchange rate	0.707
Euro to US$ exchange rate	0.845
Yuan to US$ exchange rate	6.594
Yen to US$ exchange rate	112.950
Sterling UK to US$ exchange rate	0.746
Australian $ to US$ exchange rate	1.308
Canadian $ to US$ exchange rate	1.278
Swiss Franc to US$ exchange rate	0.987
Malawian Kwacha to US$ exchange rate	732.03

Source: IMF (International Financial Statistics) and Reserve Bank of Malawi.

[1] LBM connotes London Bullion Market.

25. **Gross reserve liabilities of the RBM** are defined as the sum of the following: (i) outstanding medium and short-term liabilities of the RBM to the IMF; (ii) all short-term foreign currency liabilities of the RBM to nonresidents with an original maturity of up to, and including, one year; and (iii) all foreign currency denominated liabilities to residents (including, for instance, foreign currency denominated deposits of domestic banks and other residents with the RBM). SDR allocations are excluded from gross reserve liabilities of the RBM.

26. **Adjustors Applied to NIR Program Floor:**

- Adjustment clause on NIR – budget support: The program floor on NIR will be adjusted upward by the full amount by which the U.S. dollar-denominated inflows from the budget support exceed the program baseline. In the event of a shortfall in budget support inflows, the

downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 27. The budget support is measured as the cumulative flow from the beginning of the fiscal year. They will be recorded in the original currency of disbursement and then converted to U.S. dollars using the above defined program cross exchange rates.

- Adjustment clause on NIR – donor accounts for the social sector (including health and education Joint funds, and the NAC). The floor on the NIR of the RBM will be adjusted upward by the full amount by which the donor inflows from the U.S. dollar-denominated donor accounts for Joint funds and NAC held in the RBM are higher than the program baseline. In the event of a shortfall, the downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 27. These donor inflows are measured as the cumulative receipts by the budget from the beginning of the fiscal year. They will be recorded in the original currency of disbursement and then converted to U.S. dollars using the above defined program cross exchange rates.

- Adjustment clause on NIR – debt service payments (defined as payments including both interest and principal): The floor on NIR of the RBM will be adjusted upward by the full cumulative amount by which debt service payments to the WB and the AfDB fall short of the program baseline. In the event of any excess of debt service payments to the WB and the AfDB, the downward adjustment of the NIR floor will be subject to the limitation outlined in paragraph 27. Debt-service payments will be measured as the cumulative payments from the beginning of the fiscal year. They will be recorded in the original currency of payments and then converted to U.S. dollars using the above defined program cross exchange rates. This downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 27.

27. **The total downward adjustment to the NIR floor** from the combined impact of a (i) a shortfall of budget support relative to the program projections; (ii) a shortfall of inflows to the donor accounts for the social sector relative to the program projections; and (iii) any excess of debt service payments to the WB and the AfDB relative to the program projections, will be subject to a cumulative limit of US$65 million.

28. **Reporting requirement**. Data on foreign assets and foreign liabilities of the RBM will be transmitted on a monthly basis, including sub-components and a breakdown of assets that are pledged or encumbered. This transmission will include daily and weekly data on RBM's foreign exchange liabilities to commercial banks (including required reserves with the RBM) and the exchange rate used for their conversion into kwacha will be shown separately.

- Net Foreign Assets of the RBM

29. **Definition of Net Foreign Assets (NFA) of the RBM**: The NFA of the RBM are defined as its gross foreign assets (GFA) minus its gross foreign liabilities. Gross foreign liabilities are equal to

gross reserve liabilities as defined in paragraph 24, plus any other foreign liabilities not listed in that paragraph.

30. **Gross foreign assets (GFA) of the RBM are defined** as gross reserves assets as defined in paragraph 23, plus (i) any foreign currency claims on residents; (ii) capital subscriptions in international institutions; (iii) foreign assets in nonconvertible currencies; (iv) transfers of foreign currency claims to RBM by other institutional units in Malawi just prior to reporting dates with accompanying reversals of such transfers soon after those dates; (v) assets obtained through currency swaps of less than three months duration; (vi) gross reserves that are in any way encumbered or pledged, including, but not limited to: (a) assets blocked when used as collateral for third party loans and third-party payments, or pledged to investors as a condition for investing in domestic securities; (b) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and(c) foreign reserves blocked for letters of credit.

- Ceiling on Accumulation of External Payment Arrears

31. **Definition of external payment arrears**: External payment arrears consist of debt service obligations (principal and interest) of the central government or the RBM to nonresidents that have not been paid at the time they are due, as specified in contractual agreements, except on external debt subject to rescheduling or restructuring. This performance criterion will be monitored on a continuous basis.

- Ceiling on New Non-Concessional External Debt

32. **Definition of debt**: The definition of debt, for the purposes of the TMU, is set out in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), and also includes contracted or guaranteed commitments for which value has not been received. For program purposes, the term "debt" is understood to mean a current, that is, not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debt can take several forms; the primary ones being as follows:

i. Loans, that is, advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchange of

assets that are equivalent to fully collateralized loans, under which the obligor is required to repay the loan funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

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

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

33. **Definition of non-concessional external debt.** Short-, medium-, and long-term debt is considered concessional if it includes a grant element of at least 35 percent[1] and non-concessional if otherwise. The grant element is defined as the difference between the nominal value of the loan and its present value, expressed as a percentage of the nominal value of the loan. The present value of the debt at the date on which it is contracted is calculated as the discounted sum of all future the debt service payments at the time of the contracting of the debt.[2] The discount rate used for this purpose is 5 percent per annum. The ceiling on non-concessional debt applies to the contracting and guaranteeing of debt with nonresidents by the central government, the RBM, and state-owned enterprises, unless an explicit selective exclusion is made. This performance criterion is monitored on a continuous basis. The ceiling applies to debt and commitments contracted or guaranteed for which value has not been received. The ceiling is measured cumulatively from the beginning of the fiscal year.

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

35. **Medium- and long-term debt:** Outstanding stock of debt with a maturity of more than one year.

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

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

36. **Excluded from the limit on non-concessional external debt** is the use of IMF resources, and any kwacha-denominated government security holdings and stock holdings by nonresidents. Excluded from the limit are also (i) debts classified as international reserve liabilities of the RBM; (ii) new debt issued to restructure, refinance, or repay existing debt up to the amount actually used for the above-mentioned purposes; (iii) normal import financing; and (iv) arrangements to pay overtime obligations arising from judicial awards to external creditors. A financing arrangement for imports is considered to be "normal" when the credit is self-liquidating.

REPORTING REQUIREMENTS

37. **For the purpose of program monitoring**, the Government of Malawi will provide the data listed in Table 2 below with monthly data within four weeks of the end of each month, and annual data as available.

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

39. **The authorities will furnish an official communication to the IMF describing program quantitative performance and structural benchmarks within 8 weeks of a test date**. The authorities will, on a regular basis, submit information to IMF staff with the frequency and submission time lag as indicated in Table 2.

Table 2. Summary of Reporting Requirements				
	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Agency
Exchange Rates	D	W	D	RBM
International reserve assets and reserve liabilities of the Monetary Authorities [2]	W	W	M	RBM
Gross international reserves and foreign exchange purchases and sales	D	W	M	RBM
Reserve/base money, OMO transactions, and RBM conversion of ways and means account to government securities	W	W	M	RBM
Broad money	M	M	M	RBM
Central Bank balance sheet	W	W	M	RBM
Consolidated balance sheet of the banking system	M	M	M	RBM
Interest rates [3]	M	M	M	RBM
Excess reserves by banks	M	M	M	RBM
Volume of transactions in the interbank money market and foreign exchange markets and sales of foreign currencies by RBM to commercial banks	D	W	W	RBM
Government securities auction results	W	W	W	RBM

Table 2. Summary of Reporting Requirements (continued)

Spread between exchange bureau midrate and the official exchange midrate	W	M	W	RBM
Central government domestic borrowing	M	M	M	RBM
Holdings of local registered stocks, treasury bills, treasury notes and other government securities	M	M	M	RBM
Detailed issue and maturity profile for all government securities	M	M	M	RBM
Financial soundness indicators by banks	Q	Q	...	RBM
RBM foreign exchange cash flow	M	M	M	RBM
Bank statements of the agricultural SWAp account held at RBM	M	M	...	RBM
Annual financial reports of the 8 major parastatals[4]	A	A	...	MOF
Borrowing of the 8 major parastatals [4]	SA	SA	...	MOF
Quarterly report on government domestic arrears	Q	Q	...	AG
Comprehensive list of tax and non-tax revenues	M	M	M	MOF
Fiscal table (GFS based), including revenue, grants, expenditure, balance and composition of financing of the central government [5, 6, 7]	M	M	M	MOF
Expenditure for domestically financed capital projects	M	M	M	MOF

Table 2. Summary of Reporting Requirements (concluded)

Data on Joint Funds on health and education	M	M	...	MOF
Stocks of public sector and public-guaranteed debt [6]	Q	Q	Q	MOF
New external loans contracted or guaranteed by the government and disbursement schedule [6]	Continuous	Continuous	Continuous	MOF
Quarterly external debt service (actual and projections)	Q	Q	...	MOF
Debt-service payments on domestic debt (outturn and projections)	M	Q	Q	MOF
Accumulation of new domestic government arrears	M, Q	M, Q	M, Q	MOF
Report on IMF program performance	Q	Q	...	MOF
Consumer Price Index and monthly statistical bulletin	M	M	M	NSO
Exports and Imports of Goods and services, and subcomponents.	M	M	Q	NSO
Balance of payments	A	A	A	NSO
GDP/GNP, by activity and expenditure, at constant and current prices	A	I	A	NSO

[1] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Semi-annually (SA); Irregular (I).
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Both market-based and officially-determined, including discount rates, money market rates, interbank money market rate, rates on treasury bills, notes and bonds.
[4] Agriculture Development and Marketing Corporation, Electric Supply Company of Malawi, Electricity Generation Company of Malawi, Malawi Housing Corporation, National Oil Company of Malawi, Northern Regional Water Board, Lilongwe Water Board, and Blantyre Water Board.
[5] Foreign and domestic banks, and domestic nonbank financing.
[6] Detailed information on the amounts, currencies, terms and conditions, including debt contracted or guaranteed by the RBM or any other agency on behalf of the central government.
[7] Provided no more than four weeks after the end of each month.