Malawi: Request for Disbursement Under the Rapid Credit Facility and Request for a Staff Monitored Program with Executive Board Involvement-Press Release; Staff Report; and Statement by the Executive Director For Malawi

INTERNATIONAL MONETARY FUND

IMF Country Report No. [22/352]

MALAWI

November 2022

REQUEST FOR DISBURSEMENT UNDER THE RAPID CREDIT FACILITY AND REQUEST FOR A STAFF MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MALAWI

In the context of the Request for Disbursement Under the Rapid Credit Facility and Request for a Staff Monitored Program with Executive Board Involvement, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on November 21, 2022, following discussions that ended on October 17, 2022, with the officials of Malawi on economic developments and policies underpinning the IMF arrangement under the Rapid Credit Facility. Based on information available at the time of these discussions, the staff report was completed on November 14, 2022.
- A **Debt Sustainability Analysis** prepared by the staff of the IMF and the World Bank.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Malawi.

Letter of Intent sent to the IMF by the authorities of Malawi*
Memorandum of Economic and Financial Policies by the authorities of Malawi*
Technical Memorandum of Understanding*
*Also included in Staff Report

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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International Monetary Fund
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PRESS RELEASE

PR22/404

IMF Executive Board Approves US$88.3 Million in Emergency Financing Support to Malawi

FOR IMMEDIATE RELEASE

- The Executive Board of the International Monetary Fund (IMF) approved today a disbursement of US$88.327 million (SDR 69.40 million) to Malawi under the new Food Shock Window of the Rapid Credit Facility.[1]

- Concurrently, the Executive Board discussed a 12-month Staff-Monitored Program (SMP) for Malawi, which was approved by the Management of the IMF on November 11. With timely implementation of the program, the SMP would help the authorities establish a track record of policy implementation, possibly paving the way to an IMF-supported upper credit tranche (UCT) program.

- The Executive Board, which recently amended the policy for SMPs to allow for Program Monitoring with limited Board involvement (PMB)[2] on October 4, 2022, assessed that Malawi's policy program is sufficiently robust to meet the stated objectives under the SMP and that its implementation is expected to achieve the purpose of building a track record toward a UCT-quality Fund arrangement. The Board noted that the program would benefit from limited Board involvement given concerted international efforts by creditors and donors to provide substantial new financing and debt relief, and Malawi's significant outstanding Fund credit under emergency financing instruments.

Washington, DC – November 21, 2022: The Executive Board of the International Monetary Fund (IMF) approved today a disbursement of US$88.327 million (SDR 69.40 million) under the Food Shock Window of the Rapid Credit Facility to help Malawi address urgent balance of payment needs related to the global food crisis. Food insecurity in Malawi has increased significantly owing to multiple tropical storms, below-average crop production, and increasing prices for food and agricultural inputs such as fertilizer and seed. As a result, about 20 percent of the population is projected to be acutely food insecure during the upcoming 2022/23 lean season (October 2022-March 2023), or more than twice as many people as in 2021.

The authorities also requested the Staff-Monitored Program and Program Monitoring with Board involvement to build a track record of policy implementation, possibly paving the way to an IMF-supported Upper Credit Tranche (UCT)-quality program. The Board and Management

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[1] The Food Shock Window provides, for a period of a year, a new channel for emergency Fund financing to member countries that have urgent balance of payment needs due to acute food insecurity, a sharp increase in their food import bill, or a shock to their cereal exports.

[2] SMPs are informal agreements between national authorities and IMF staff to monitor the authorities' economic program. As such, they do not entail endorsement by the IMF Executive Board. Under recent reforms to the policy on staff monitored programs, the Executive Board, in specified circumstances, has limited involvement, not amounting to endorsement of the policy program. In such cases, the Board's role is limited to (i) opining on the robustness of the member's policy program to meet the objectives stated in the Management approved SMP and to achieve the purpose of building or rebuilding a track record toward a UCT-quality program, and (2) in the context of reviews, to indicate if the member is on track to achieve these objectives.

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welcomed the steps the authorities have taken since the Article IV Consultation in December 2021 to stabilize the economy and build the foundation for inclusive growth.

Following the Executive Board's discussion, Mr. Bo Li, Deputy Managing Director and acting Chair, issued the following statement:

Malawi is facing a challenging economic and humanitarian situation, with foreign exchange shortages and an exchange rate misalignment leading to a sharp decline in imports including fuel, fertilizer, medicine, and food. Emergency financial assistance under the RCF's new food shock window would help address urgent balance-of-payments needs and mitigate the impact of the food shock.

The Management-approved staff monitored program (SMP) is sufficiently robust to meet the authorities' stated objectives, and its implementation is expected to achieve the purpose of building a track record toward an Upper Credit Tranche (UCT) -quality program supported by a Fund arrangement.

Malawi's track-record building SMP will benefit from limited Board involvement given the ongoing concerted international effort by creditors and donors to provide substantial new financing and debt relief to Malawi, as well as Malawi's significant outstanding Fund credit under emergency financing instruments.

Fiscal discipline, supported by a realistic budget, an enhanced Public Financial Management system and timely production of comprehensive fiscal reports, is important. Restoring price stability and ensuring financial sector stability will help build a foundation for private sector-led growth.

Rebuilding external buffers will be critically important to reduce Malawi's vulnerabilities to external shocks. The RBM's commitment to rebuild its foreign exchange reserves, requiring implementation of its strategy to wind down unsustainable policies including excessive use of swaps and trade credit to maintain strategic imports and other quasi-fiscal operations, is welcome.

While debt is sustainable on a forward-looking basis, risks to the program are high. It will be critical to swiftly implement the authorities' debt restructuring strategy, which aims to bring Malawi back to moderate risk of debt distress in the medium term. The credible process underway to restructure the authorities' debt to commercial creditors, which in itself would restore debt sustainability albeit with high risk, is welcome. Swift progress is also needed on the reprofiling of official bilateral debt. A concerted effort among the authorities, their creditors and the international development partners will be crucial to ensure a successful implementation of the debt restructuring strategy.

Addressing weaknesses in governance and institutions and enhancing transparency will be important. In this regard, strong corrective actions to address the issues that led to misreporting under the 2018 ECF, including implementation of the recommendations of the 2021 safeguards assessment, and measures to strengthen foreign exchange reserve management are welcome. The authorities are urged to move to a UCT-quality program as soon as feasible.

INTERNATIONAL MONETARY FUND

MALAWI

November 14, 2022

REQUEST FOR DISBURSEMENT UNDER THE RAPID CREDIT FACILITY AND REQUEST FOR A STAFF MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT

EXECUTIVE SUMMARY

An economic and humanitarian crisis. Foreign exchange shortages together with exchange rate misalignment led to a sharp decline in imports including fuel, fertilizer, medicine, and food. Large fiscal deficits, nearly 10 percent of GDP in FY2021/22, have been largely financed by domestic bank borrowing, resulting in rapid money growth and inflation of 25.9 percent in September 2022. Exchange rate pass-through and hikes in food prices added to inflationary pressure. In addition, food insecurity in Malawi has increased dramatically under the impact of multiple tropical storms, below-average crop production, and increasing prices for food and agricultural inputs such as fertilizer and seeds. The latter are expected to affect the current planting season. As a result of these factors, about 20 percent of the population is projected to be acutely food insecure during the upcoming 2022/23 lean season (October 2022-March 2023), more than twice as many as in 2021.

The authorities' emerging response. Since the Article IV consultation in December 2021, the Malawian authorities have taken steps to stabilize the economy and build the foundations for inclusive growth. The authorities submitted the FY2022/23 budget in March 2022 that aims at fiscal consolidation of about 2½ percentage points of GDP. The Reserve Bank of Malawi (RBM) tightened the monetary policy stance in April 2022 by raising the policy rate by 200 basis points and devalued the Kwacha in May by 25 percent to start correcting for a large real exchange rate overvaluation for the first time since the devaluation of comparable size in 2012. The authorities also hired a debt advisor in May 2022 aiming for a sizeable debt treatment that would bring Malawi back to moderate risk of debt distress in the medium term.

Fund engagement. The authorities have requested a disbursement of 50 percent of quota under the Rapid Credit Facility-Food Shock Window (FSW) to address urgent balance-of-payments needs and mitigate the food shock including through a strengthening of cash transfer programs to vulnerable households. In parallel, they have initiated a comprehensive restructuring of external public debt to restore debt sustainability and have mobilized significant new grant financing from multilateral

and bilateral official partners. To help guide their policy and reform agenda aimed at macroeconomic stabilization, inclusive growth, and more resilience to climate change, as well as to as support the ambitious debt operation, the authorities have also requested a twelve-month Staff Monitored Program with Executive Board Involvement (PMB) to build a track record towards an Extended Credit Facility Arrangement (ECF).

Policy and reform effort. Policies and reforms under the PMB will focus on: (i) socially-conscious fiscal consolidation to contain domestic borrowing while protecting vulnerable households from the impact of the necessary adjustment amid rising prices for food; (ii) moving towards greater flexibility of the exchange rate to help rebuild foreign exchange reserves to reduce Malawi's vulnerabilities to external shocks; (iii) undertaking a debt restructuring to help restore debt sustainability; (iv) achieving price stability and maintaining financial soundness to support private-sector led growth; and (iv) addressing longstanding governance weaknesses to reduce corruption and improve efficient and effective use of limited public resources.

Risks. Risks to the authorities' policy and reform agenda are exceptionally high. Restoring macroeconomic stability and debt sustainability will critically depend on steadfast implementation of policies and reforms, timely progress with the envisaged debt operation, and sustained engagement of donors with grant financing.

Approved By
Costas Christou (AFR) and Björn Rother (SPR)

Missions were held during October 5-8, 2022 in Lilongwe and October 11-17, 2022 in Washington, D.C. The staff team comprised Ms. Saito (head), Ms. Gwenhamo, Mr. Tapsoba, Ms. Yoon, Ms. Shirakawa, (all AFR), and Ms. Hashimoto (SPR). Mr. Banda (local economist), Mr. Anderson (FAD long-term expert) also joined discussions. The team met with H.E. President Chakwera, the Hon. Sosten Gwengwe (Minister of Finance), Dr. Wilson Banda (Governor of the Reserve Bank of Malawi, RBM), other senior government and RBM officials, representatives from the private sector and the international community. Ms. Nainda (OED) joined the discussions. Ms. Farid provided input, Mr. Ahluwalia provided research support, and Ms. Bravo assisted the team in the preparation of this report.

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CONTEXT

1. The democratic change in government in mid-2020 marked a break from the past, but legacy issues have weighed on the current administration. President Lazarus Chakwera's long-term growth strategy "Malawi Vision 2063" aims to address the causes underlying the lack of sustained growth and heavy reliance on aid over decades. The economy has, however, been paralyzed with unsustainable debt with external debt service representing about 56 percent of exports. The accumulation of public debt started after the 2013 "Cashgate"[1] as on-budget support shifted to off-budget support, and the forgone funding of the budget was replaced by domestic borrowing and a gradual increase in external nonconcessional borrowing.[2] The Chakwera administration recognized that a new Extended Credit Facility (ECF) arrangement and its catalytic role would be vital in restoring macroeconomic stability. Responding to the ECF request submitted in April 2021 was, however, not immediately possible due to the need to address unsustainable debt. The authorities have also been taking corrective actions to resolve noncomplying disbursements ("misreporting")[3] under the 2018 ECF arrangement. As such, the country is not in a position to implement an Upper Credit Tranche (UCT)-quality economic program and needs to build a track record for a UCT-quality arrangement.

2. Meanwhile, Malawi's protracted BOP needs snowballed, and the country became extremely vulnerable to external shocks. End-2021 gross official reserves, including encumbered deposits, were projected at US$394 million at the time of the 2021 Article IV consultation. The Special Audit completed in June 2022 reported that gross official reserves after adjusting for encumbered deposits stood at US$72 million, resulting in large negative net international reserves (NIR) of - US$1.3 billion at end 2021.

3. Moreover, Malawi is currently facing acute food insecurity. Following the COVID-19 pandemic, the economy was hit hard by consecutive cyclones in the first half of 2022, highlighting Malawi's vulnerability to weather-related shocks. The government implemented a value-added tax (VAT) exemption on cooking oil in 2022 to mitigate rising food prices—a targeted approach in the face of broad increases in food prices. Limited access to farm inputs due to higher input prices affected production and contributed to high food prices. Food inflation has been on the rise since 2017 and peaked at 33.7 percent in September 2022. The situation will likely worsen further in the months ahead: the current planting season of maize (November through December), the locally produced main staple food, is expected to suffer from high fertilizer and seeds prices. As a result of the multiple shocks, about 20 percent of the population are projected to be acutely food insecure at the "Crisis" level (Integrated Food Security Phase Classification (IPC) Phase 3 or higher) during the 2022/23 lean season (October 2022-March 2023). The population living at the crisis level more than doubled since last year.[4]

[1] "Cashgate", a major corruption case that led to arrests, trials and convictions of a number of civil servants.

[2] IMF Country Report No 21/269.

[3] "Misreporting case" resulted from the provision of inaccurate information on the performance criteria on the floor of Net International Reserves (NIR) under the 2018 ECF arrangement.

[4] World Food Programme, Floods assessment Fact Sheet (10 June 2022) and Famine Early Warning System Network, Malawi Food Security Outlook Update (August 2022).

4. The authorities have already taken measures that demonstrate their commitment to macroeconomic adjustment and structural reforms. Recent actions include the start of fiscal consolidation in the FY2022/23 budget in March 2022, the 200-basis points increase in the monetary policy rate in April (and again in October) and the 25-percent devaluation in the Kwacha. Moreover, a sizeable debt operation, combined with donor support, is expected to bring Malawi back to moderate risk of debt distress in the medium term and help cover urgent balance-of-payments needs. To address governance issues, the authorities completed special audits on foreign exchange reserves, COVID-spending, as well as on public funds related to infrastructure projects. These activities also demonstrate the current administration's strong commitment to fight corruption.

5. Malawi requested US$88.327 million (50 percent of quota) under the Food Shock Window of the Rapid Credit Facility as well as a Staff Monitored Program with Executive Board Involvement (PMB). The financing will help Malawi address urgent balance of payments needs related to the food crisis. The PMB will support the government's macroeconomic adjustment and structural reforms to restore macroeconomic stability and provide the foundation for inclusive growth.

6. Risks to the program are elevated and call for strong implementation of the authorities' policy and reform agenda. The authorities are committed to macroeconomic adjustment and structural reforms as indicated in the Letter of Intent and the Memorandum of Economic and Financial Policies (Appendix I).

RECENT ECONOMIC DEVELOPMENTS

7. A sequence of external shocks has exacerbated Malawi's fragility. Economic growth in 2022 is projected at 0.8 percent (compared with 3.5 percent at the time of the 2021 Article IV consultation). During the first quarter of the year, Malawi faced two tropical cyclones, rising commodity prices, and forex shortages—all contributing to an imminent BOP crisis. Cyclones Ana and Gombe ravaged crops and damaged infrastructure, including the main hydropower plant, thereby increasing fuel import needs to augment electricity sources (Annex I). The war in Ukraine has put pressure on energy and food prices, increasing risks to severe food insecurity. The ongoing energy crisis—chronic fuel shortages and extended electricity blackouts—has further dampened economic activity. Despite the devaluation, a foreign exchange shortage remains and contributes to a de facto rationing of foreign exchange for imports by commercial banks.

8. Pressure on the exchange rate and inflation is mounting. Inflation reached 25.9 percent in September 2020. Rising food and fuel prices, as well the passthrough effect of the kwacha depreciation, contributed to food and nonfood inflation, which accelerated to 33.7 percent and 18.3 percent, respectively. Despite the devaluation, foreign exchange shortages persist and expectations of further devaluation weigh on the exchange rate. Meanwhile, monetary base growth remains high at 24 percent at end-August, largely due to high net domestic financing of fiscal deficit, which averaged 8.6 percent in FY2020/21 and FY2021/22.

9. Gross reserves remain extremely low. Gross reserves at end 2021 stood at US$72 million, a large downward revision from US$394.0 million in the 2021 Article IV Consultation because of the exclusion of encumbered deposits in line with the definition of reserve assets in the Monetary and Financial Statistics Manual. This is precariously low considering high debt service, difficulty in renewing swaps, and further utilization of the TDB facility to sustain fuel imports. To secure more foreign exchange purchases, the RBM implemented a surrender requirement of 30 percent of exports[5] and, in May 2022, devalued the Malawi Kwacha. That said, external debt service in 2022 would be US$719 million. Without debt treatment, debt service is projected at about 55.6 percent of exports of goods and services.

OUTLOOK AND RISKS

10. Economic growth would gradually strengthen. Growth would recover to 2.4 percent in 2023. Medium-term growth is now projected at 4.5 percent (0.4-percentage point higher than in the Article IV consultation) to incorporate the ambitious reform agenda of the government despite the frequency of weather-related shocks assumed in the baseline. Fiscal consolidation, monetary tightening, and reforms that will bring the economy back to a sustainable path are expected to support economic recovery in the medium term. Improvements in agricultural productivity and the services sector, investment in human and physical capital, and adaptation to climate change are assumed in the long-run growth outlook.

11. Inflationary pressures would be contained, helped by re-anchoring expectations in line with the tightening of the monetary and fiscal policy stance. The RBM will contain money growth and align the policy rate with inflation, keeping a positive real rate and raising reserves (¶22). RBM purchases of FX in the market to build reserves will be sterilized accordingly (¶22). At the same time, the envisaged fiscal consolidation (¶14) is expected to contribute to disinflation. Inflation is thus projected to decline to 20.4 percent by end-2023 to further moderate to 6.5 percent over the medium term. The projected level and persistence of inflation in the medium term incorporates vulnerabilities to climate change and natural disasters.

12. Gross reserves would recover to 3.7 months of imports over the medium term. The RBM will accumulate reserves by purchasing foreign exchange, undertaking a debt treatment that would lighten the external debt service burden, and exiting from quasi-fiscal operations. Moreover, a successful implementation of a strict reform program by the authorities, helped by debt restructuring and nondebt-creating flows, is indispensable in allowing the RBM to sustain positive net foreign exchange inflows to build reserves.

13. The balance of risks is tilted to the downside (Annex II). The outlook assumes that sufficient nondebt-creating flows (i.e., debt relief and grants) will help cover urgent balance of payments needs and support the authorities' efforts to restore macroeconomic stability and debt

[5] The RBM reintroduced a surrender requirement (a capital flow management (CFM) measure in accordance with the revised Institutional View) to exporters in August 2021 and tightened the measure in March 2022.

sustainability. The outlook also assumes that the authorities maintain a strong commitment to macroeconomic adjustment and structural reforms. Risks to this outlook include a delay in nondebt-creating inflows as well as weaker-than-expected policy implementation, which would create financing gaps, monetary financing of fiscal deficits, and pressure on inflation and the exchange rate. If these risks materialize, macroeconomic stability may not be restored. The outlook also assumes that weather-related events and other external shocks remain manageable. Other risks to the outlook include supply chain disruptions and a further surge in fuel, food, and fertilizer prices, resulting in additional financing needs and increasing risks of food insecurity. Upside risks to the outlook include the start of mining exports and a successful implementation of export diversification / formalization of informal exports, which could lead to increases in exports relative to the baseline. Continued improvements in tax administration would also be an upside risk to the outlook.

POLICIES SUPPORTING THE PROGRAM

A. Fiscal Policy: Containing Domestic Borrowing and Regaining Fiscal Discipline

14. The revised FY2022/23 budget will support ambitious fiscal adjustment. The budget law will be revised at the mid-year review to reflect the latest projections on revenue performance and the execution of development expenditure. The authorities aim to reduce the domestic primary deficit to about 0.6 percent of GDP, from 4.1 percent of GDP in FY2021/22. Net domestic financing is projected to decline to 5.6 percent of GDP in FY2022/23 from 7.4 percent of GDP in FY2021/22.

15. The significant fiscal tightening is critical to help reach a debt-stabilizing primary balance as quickly as possible. The primary fiscal balance would improve by an annual 1½ percent of GDP over the medium term to stabilize debt dynamics. This fiscal consolidation reflects a comprehensive strategy that places equal weights on expenditure containment and revenue improvement. The authorities also plan to adopt a Medium-Term Expenditure Framework (MTEF) that is consistent with the fiscal anchor.

16. Implementation of the domestic revenue mobilization strategy (DRMS) would contribute significantly to meeting Malawi's large spending needs. Additional income tax brackets and advance income tax were already introduced in 2022. To further boost revenue (currently standing at just 13.4 percent of GDP), the authorities are committed to: introduce the presumptive tax for small businesses, rationalize the list of items subject to preferential General Sales Tax (GST) treatment, review tax incentive regimes to revamp the Taxation Act and Customs and Excise Act, strengthen the withholding tax regime, introduce measures to address Base Erosion and Profit Shifting (BEPS), reform excise tax rates; and continue efforts to improve tax administration such as the online rollout of the Integrated Tax Administration System (ITAS), also called Msokho. The design and implementation of these measures will have to proceed rapidly to deliver the planned consolidation as scheduled. Additional measures are contemplated to improve nontax revenues. These include reviewing fees and charges to ensure that they reflect full cost recovery and ensuring that Ministries, Departments, and Agencies (MDAs) account for their revenue collections in IFMIS and remit nontax revenue collections to Malawi Government consolidated (MG1) account, the main source of funding of all its operations.

17. Expenditure rationalization will be implemented without reducing support to the poor and vulnerable. The authorities are broadly carving out social expenditure from the required fiscal consolidation, including to mitigate the impact of increased food insecurity. To safeguard social protection and protect the vulnerable, including from the impact of higher food price inflation, a floor on social spending is set as an indicative target (IT) under the program. This spending will be audited in the context of annual fiscal reporting to the National Assembly. The IT covers contributions to a number of social safety net spending programs including the Social Cash Transfer Program (SCTP) and the Affordable Inputs Program (AIP). At the same time, steps have been taken to prevent cost overruns from escalating fertilizer prices in the AIP, the Government subsidy program, through augmentations of farmer contributions and capping the Government Subsidy (MEFP ¶22 and MEFP Box 1). In the medium term, with the support of development partners, the AIP is set to be phased out and replaced by the SCTP and public works programs. The wage bill will be rationalized through a hiring freeze (excluding frontline service delivery staff in health and education) and the strengthening of approval processes for payroll and pension changes.

18. Enhanced cash management and commitment controls are the cornerstone of the program. In the past, optimistic revenue projections, coupled with weak commitment controls, led to the accumulation of sizeable arrears particularly from multiyear projects and utility bills. With the Ministry of Finance and Economic Affairs (MOFEA) lacking a full picture of the government's commitments, monthly budget releases incentivized the incurrence of commitments outside of the Integrated Financial Management Information System (IFMIS). This issue has been compounded by limited disciplinary measures to sanction officers who engaged in this practice and concentration of controls at the payments rather than at the commitment stage. There was also a backlog of bank reconciliations that has reduced the credibility of public finances. A flow chart has been elaborated to guide and strengthen the cash management and debt issuance. (MEFP ¶24 and MEFP Text Figure 1).

19. Implementation of the new IFMIS, institutionalizing reporting, and expanding its coverage are critical for improved budget execution and strong commitment controls. The rolling out of the new IFMIS to all MDAs from July 2021 and other Public Financial Management (PFM) reforms including the interim Electronic Funds Transfer (EFT) for government payments will help improve budget preparation, cash management, commitment controls, banking arrangements, accountability, and payment efficiency (MEFP ¶24). The success of the fiscal adjustment program relies heavily on comprehensive and timely reporting, and sound commitment controls. The success of the IFMIS system requires an expansion of its coverage, especially to include all national government cash inflows and outflows.

20. The authorities intend to clear the backlog of arrears. The authorities have verified arrears of national budget entities up to June 30, 2020; and will be verifying those up to March 31, 2022 (SB). The authorities are preparing an arrears clearance strategy so that settlement respects the limits of the fiscal framework and available resources. Going forward, quarterly allotments and contract management would help the government prevent further accumulation of arrears. This will allow MDAs to commit up to this amount through IFMIS. MDA payments will be limited to monthly cash releases, aligned with allotments.

21. Strengthening the oversight of state-owned enterprises (SOEs) is also important. Weak oversight and financial reporting jeopardize adequate monitoring and management of risks to the budget and public debt from SOEs. In compliance with the new PFM Act, the authorities plan to initiate detailed reporting for high-risk SOEs, undertake regular monitoring of the management accounts of relevant SOEs, and prepare an annual consolidated report of all SOEs (MEFP ¶23). This will prevent financial slippages and fiscal risks stemming from public entities.

B. Achieving Price Stability and Maintaining Financial Soundness

22. The RBM will further tighten its monetary policy stance to achieve price stability (MEFP ¶25). Monetary policy will remain anchored at containing reserve money growth while building FX reserves. To this end, the RBM is committed to (i) align the monetary policy rate with inflation to ensure positive real returns on government securities; (ii) raise required reserves if needed; and (iii) raise the discount rate to discourage banks from accessing the discount window. The RBM has demonstrated its commitment by raising the monetary policy rate by 200 basis points in the April monetary policy committee (MPC) meeting; and another 200 basis points to 18 percent (and the discount rate to 20 percent) in the October MPC meeting. Further increases will be implemented as needed to ensure that these rates will move into positive territory in real terms. In the medium term, the RBM is committed to maintaining the real interest rate below the growth rate to support private-sector led growth.

23. The RBM will remain vigilant to ensure financial sector stability. The RBM's and commercial banks' large exposures to government securities pose potential risks to the financial sector given the level of domestic debt. The banking system's exposure to the government through securities and swap operations will be closely monitored through timely submission of Standardized Report Forms (SRFs). In addition, loan and collateral quality will be reassessed to promote financial sector stability (MEFP ¶26).

C. Rebuilding External Buffers

24. The RBM is committed to a reserve accumulation strategy to rebuild a foreign exchange buffer (MEFP ¶27). The strategy comprises several components that aim to wind down unsustainable policies (e.g., excessive uses of currency swaps and trade credit to maintain strategic imports and quasi-fiscal operations) and engage in sustainable policy to enhance price competitiveness (Annex III) and reserve accumulation (e.g., net purchases of foreign exchange from commercial banks). The RBM has already started taking appropriate measures (Box 1).

25. The RBM is committed to allow greater flexibility in the exchange rate by facilitating the price formation processes through small pilot foreign exchange auctions. The inception of this program supported by disbursements of emergency assistance is considered the most optimal timing to facilitate price formation. Developing the forex interbank market will be supported by Technical Assistance (TA) from the Fund.[6]

Box 1. Malawi: Reserve Accumulation Measures, 2022

- The RBM conducted a one-off 25 percent of devaluation in May 2022.
- The RBM began to wind down the quasi-fiscal operation of financing fuel imports in Q3 and intends to cease it by end-2022 and let Petroleum Importers Limited (PIL) take over fuel importation.
- The RBM will wind down the use of short-term borrowing, aiming to reduce outstanding swaps from US$420 million at the end of 2021 to about US$140 million by the end of the medium term.
- The RBM will also actively engage in purchasing foreign exchange from the market to rebuild external buffers. The RBM introduced surrender requirements (a CFM) in August 2021 (further tightened in March 2022), with an intention to wind down the requirements as the forex market normalizes.
- In the process, the RBM will create opportunities for price discovery and enhance transparency in the forex trading, developing the forex market (SB).

D. Restoring Debt Sustainability

26. Malawi's debt is assessed to be unsustainable (MEFP ¶28). At the time of the 2021 Article IV consultation (December 2021) Malawi's external and overall public debt were assessed as high risk of debt distress, and unsustainable under current policies. At this time, Malawi's external and overall public debt are assessed as in debt distress, and both external and overall public debt are unsustainable under current policies. Pre-treatment external debt service would be 55.6 percent of projected exports in 2022 (Text Figure 1). Principal debt service excluding repayments to the IMF would amount to $569 million and interest payments at $119 million in 2022. Of which, the share of commercial debt service, both principal and interest, would amount to $468 million.

27. The authorities hired debt advisors in May and started to engage in debt negotiations with commercial as well as official bilateral creditors (MEFP ¶29). As a first step under Malawi's debt strategy, a sizeable net present value reduction of commercial debt and reprofiling of official bilateral debt (based on the Low-Income Country Debt Sustainability Framework (LIC-DSF) 5 percent discount rate) would be implemented. Since obtaining credible and specific financing assurances from bilateral official creditors is expected to take several months, a reprofiling of official bilateral debt would be expected as a second step, but in any case before a potential UCT-quality

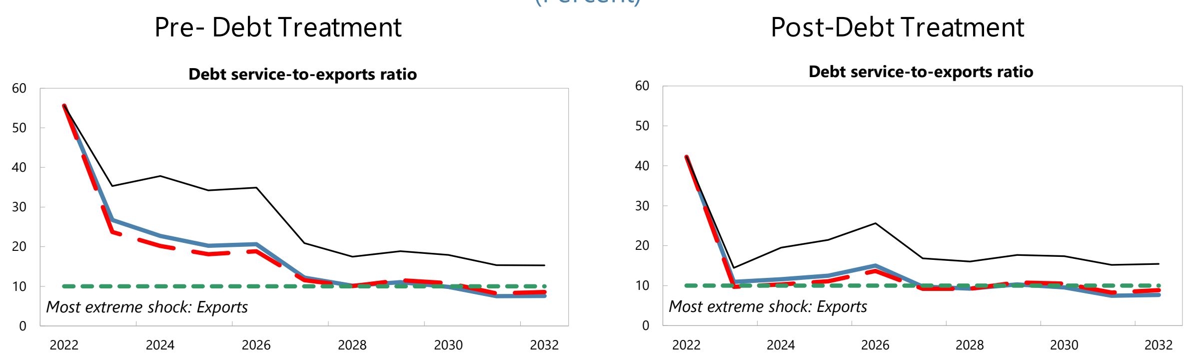
[6] The official exchange rate has been stable (Figure 1) with the daily band applied to banks' bids following Guidelines for Foreign Exchange Trading Activities (IMF Country Report No. 21/269, ¶46).

arrangement is requested. The treatment of private and official bilateral debt would bring external debt service down significantly in the near term and below the 10 percent of exports threshold by end of the medium term (Text Figure 1). Fully implementing the strategy would restore debt sustainability and improve the outlook to moderate risk of debt distress by the end of the medium term (MEFP ¶30).

28. Malawi is also improving debt management, monitoring, recording, and reporting with the support of IMF and the World Bank technical assistance (MEFP ¶31).

Text Figure 1. Malawi: Pre- and Post-Debt Treatment, 2022–32

(Percent)



E. Tackling Governance Challenges

29. The program appropriately focuses on improving data recording, reporting, and monitoring both at the MOFEA and RBM. The implementation of the new IFMIS and publication of strategic imports data are inevitable to ensure efficient use of public resources, for protecting the most vulnerable groups while containing increases in public spending. It helps mitigate governance weaknesses (SB, MEFP ¶24, 32, 37).

30. The authorities are undertaking corrective actions to help address governance weaknesses that emerged under the 2018 ECF misreporting case (MEFP ¶33). They have completed a special audit of RBM's foreign exchange reserves for the first three reviews under the 2018 ECF arrangement in mid-June 2022, which confirmed the noncomplying disbursements under the previous ECF arrangement. In addition, the authorities have implemented corrective measures to strengthen reserve management in accordance with the 2021 Safeguards Assessment recommendations. Other measures include: improvements in PFM (¶18-19); amendments to the RBM Act; and the establishment and operationalization of the Asset Liability Management Committee (ALCO) at the RBM. The presentation of the misreporting case to the Executive Board is planned on November 16, 2022.

31. To address longstanding governance weaknesses, the authorities have been implementing a broader anti-corruption agenda. Their anti-corruption agenda is anchored on 4 Ps: Prosecuting people engaged in corruption; Preventing people from engaging in corruption; Protecting people against corruption; and Preparing for the impact of corruption. Several concrete steps taken recently include the audits which uncovered misappropriation of Covid-19 public funds (MEFP ¶34) and funds at the Export Development Fund (EDF), a wholly owned subsidiary of the RBM (MEFP ¶35). The authorities have started implementing and following up on recommendations of the audits, and are committed to undertaking a governance diagnostic exercise under the PMB, leveraging IMF technical assistance (MEFP ¶36).

F. Building the Foundation for Inclusive Growth and Resilience to Climate Shocks

32. The "Malawi Vision 2063" strategy aims for Malawi to reach upper-middle income status by 2063. It focuses on inclusive economic growth on three fronts: (i) poverty reduction, (ii) investing in human capital, and (iii) resilience in physical capital to climate shocks, including the agricultural sector. However, lack of sustained economic growth, partly due to frequent climate shocks and fast population growth, has left per capita income stagnant. These challenges are further complicated by multiple shocks, such as the COVID-19 pandemic and spillovers from the war in Ukraine.

33. Prioritizing physical and human capital investment while safeguarding the fiscal envelope is critical to achieve strong and inclusive growth. Malawi has significant and competing development needs, including strengthening the social safety net while creating fiscal space and restoring debt sustainability. Policy measures, such as raising educational attainment and financing and investing in climate change resilience, form a foundation for drivers of growth.[7] The authorities' strict adherence to the policy and reform agenda is crucial especially in the current situation (Annex I) to put Malawi's economy on a path that delivers stronger and more inclusive growth.

PROGRAM MODALITIES

34. Objectives and duration of the PMB. The Staff-Monitored Program with Executive Board Involvement will help Malawi build a track-record during the debt restructuring process with its commercial and bilateral official creditors towards a policy and reform program that could be supported by an ECF arrangement. The PMB is planned for a 12-month period and will span the period November 2022 to November 2023.

35. Qualification for the Food Shock Window and PMB. Malawi faces an urgent BOP need of US$841 million over the next 12 months, which is related with the food-price shock. Malawi

[7] IMF Country Report 21/269, Annex VI and VII.

qualifies for the food shock window as it was identified by the Global Report on Food Crises (GRFC) as a country experiencing a food crisis and is also expected to experience a negative shock to its current account in 2022 exceeding the qualification threshold of 0.3 percent of GDP. The IMF would cover 10 percent of the external financing need for the next 12 months (Text Table 1). Due to the time needed to progress sufficiently with the debt restructuring (obtaining credible and specific financing assurances especially from bilateral official creditors, expected to take several months), Malawi is currently not in a position to immediately implement an ECF arrangement to cover its urgent financing needs. Malawi qualifies for a PMB as the country is benefiting from an ongoing concerted international effort by the international community to provide substantial new financing in support of Malawi's economic program.

36. Access. Disbursement under the Food Shock Window of the Rapid Credit Facility would be set at 50 percent of quota (about US$88.3 million) to help cover Malawi's large urgent financing needs (Table 7). 100 percent of access is proposed to be allocated to budget support to facilitate Malawi's large and upfront fiscal adjustment. A respective Memorandum of Understanding between the RBM and the Ministry of Finance was signed to clarify their responsibilities for timely servicing of Malawi's financial obligations to the IMF.

Text Table 1. Malawi: Financing Gap, 2022Q4–2023Q4[1]

(Millions of U.S. dollars)

	Next 12 months	
	mil US$	% of total
Financing Gap	841	100
Prospective Debt relief	396	47
Prospective RCF	88	10
Prospective Grants	318	38
IDA	238	
MDTF and Other Support	80	
Residual Gap	39	5

Sources: Malawian authorities; and staff estimates.

[1]Grants figures are preliminary and further discussions are ongoing. Tentative donors for the Multi-Donor Trust Fund are EU, US, UK, AfDB, Ireland, and Germany.

37. Policy commitments under the PMB. The policy commitments included under the PMB will cover the period between November 2022 and November 2023. Quantitative targets are set for end-December 2022 and end-June 2023. Program performance under a PMB would be monitored through semi-annual program reviews based on quantitative targets, indicative targets (MEFP Table 1), structural benchmarks (MEFP Table 2), and prior actions (MEFP Table 3).

38. Safeguards assessment. An update safeguards assessment in 2021 found deterioration of safeguards at the RBM since the 2018 assessment, reflecting *inter alia* findings on misreporting. This included weakened governance and oversight arrangements. A comprehensive governance reform is required to strengthen the RBM's internal "checks and balances" and the internal controls by (i) establishing the Board as de facto main decision-making body responsible for oversight and policy formulation, and (ii) strengthening collegiality in executive management. Moreover, the RBM's operational autonomy should be safeguarded including by prohibiting it from conducting quasi-fiscal activities. The RBM will also need to strengthen its foreign reserves management practices.

39. Capacity to Repay the Fund. Malawi's capacity to repay the Fund would become adequate—but with significant risks—subject to full program implementation under the PMB and debt restructuring. All of the indicators on capacity to repay remain above the top quartile of past UCT-quality arrangements for PRGT programs during most of the program period (Figure 5). Total outstanding credit based on existing and prospective drawings to the IMF is projected at about 329.2 percent of quota by end-2022, equivalent to 33.7 percent of exports, and about 253.9 percent of gross official reserves. Total repayments to the IMF are also significant in 2022 (1.0 percent of exports and 7.5 percent of gross official reserves) (Table 7). Commitments by official creditors to provide additional concessional financing or grants, the authorities' track record of servicing debt obligations to the Fund, and strong commitment of the authorities to implement the needed macroeconomic adjustment are all critical to mitigate risks.

40. Assurances from private creditors and arrears. Malawi has arrears vis-à-vis Trade Development Bank (TBD) while it is current on its obligations towards AFREXIM Bank.[8] With respect to TBD's claims, staff assesses that the requirements of the Lending Into Arrears (LIA) Policy are met, given that (i) prompt Fund support is considered essential for the successful implementation of Malawi's adjustment program, and (ii) Malawi is pursuing appropriate policies and it is making a good faith effort to reach a collaborative agreement with its private creditors. With respect to AFREXIM Bank's contribution to restore debt sustainability, assurances are derived from staff's judgment that a credible process for debt restructuring is underway and such restructuring will likely deliver an outcome that restores debt sustainability to moderate risk in the medium term. With respect to both these creditors, Malawi has hired debt advisors, engaged in early discussions with its creditors on a restructuring strategy that is consistent with restoration of debt sustainability, has shared relevant information on its financial situation and its debt situation, and has given creditors an early opportunity to give input into the restructuring.

41. Risks to the Program. Reducing Malawi's macroeconomic vulnerabilities requires a sizeable debt operation, which is risky, including due to potential delays in obtaining financing assurances especially from bilateral official creditors and comprehensive collateralization of the borrowing from AFREXIM bank. Additional risks stem from possible delays in: (i) strengthening the PFM and cash management control, (ii) scaling up of foreign exchange purchases by the RBM, (iii) scaling down of the excessive use of short-term instruments by the RBM, and (iv) addressing governance issues identified in the special audit on foreign exchange reserves or the 2021 Safeguards Assessment Report. Climate shocks represent an additional risk. Although many of the corruption cases (e.g., the misreporting case and COVID funding incident) occurred under the former government, risks to the program associated with corruption remain high. Mitigating factors include: significant fiscal tightening, the RBM's strong commitment for further efforts for greater flexibility in the foreign exchange market, and the authorities' implementing recommendations from the special audit, and the 2021 safeguards assessment along with undertaking a proposed governance diagnostic exercise. Staff also see that further restraining nominal wage growth while fully utilizing an increase in revenue (inflation tax) could be a fiscal contingency measure.

[8] Malawi has also not incurred any arrears on bilateral official claims.

STAFF APPRAISAL

42. **The authorities' policy and reform program are sound**. The authorities' objectives under the PMB are to address immediate BOP needs, put the country back on a sustainable path and set a strong foundation for achieving their long-term objective of attaining inclusive growth and building resilience to climate shocks. To achieve these objectives, the authorities' policies will focus on ambitious fiscal consolidation to contain domestic borrowing, moving towards greater flexibility of the exchange rate, rebuilding foreign exchange reserves, undertaking a debt treatment to help restore debt sustainability, achieving price stability, maintaining financial soundness, and addressing longstanding governance weaknesses.

43. **The strategy envisages an adequate mix of adjustment, financing, and debt relief**. The burden sharing envisaged under the program will put Malawi on a recovery path while protecting the vulnerable and poor population. The authorities' fiscal adjustment plan, complemented by an ambitious debt treatment, adjustment in external policies and on-budget development assistance from development partners, will help to restore debt sustainability by the end of the medium term. In the absence of fiscal space, it is critical for the authorities to prioritize expenditures to support the vulnerable, and safeguard human and physical capital accumulation through improving the efficiency of public sector investment.

44. **Fiscal discipline supported by the approval of a realistic budget, an enhanced PFM system and timely production of comprehensive fiscal reports will be critical**. The revised FY2022/23 budget would further reduce the domestic primary deficit. The fiscal consolidation plans, anchored on enhanced revenue mobilization, expenditure rationalization and mobilization of grants, will need to be supported by much stronger cash management and commitment controls than in the past, as well as improvements in fiscal reporting to enhance budget execution.

45. **Restoring price stability and ensuring financial sector stability will help build a foundation for private-sector led growth**. In this regard, the RBM needs to persist in its efforts to reduce inflation and anchor inflation expectations by containing reserve money growth and standing ready to align the monetary policy rate with inflation to ensure positive real returns on government securities, as well raising the required reserves if needed. The RBM should also remain vigilant to ensure financial sector stability given the banking sector's large exposures to government securities and associated potential risks.

46. **Rebuilding external buffers is critically important to reduce Malawi's vulnerabilities to external shocks**. The RBM's commitment to rebuild its foreign exchange reserves requires implementation of its strategy to unwind down unsustainable policies including excessive use of swaps and trade credit to maintain strategic imports and other quasi-fiscal operations. The RBM will also need to start engaging in sustainable policies to enhance price competitiveness and reserve accumulation through net purchases of foreign exchange in relation to commercial banks.

47. **Upfront debt treatment will help to bring Malawi back to moderate risk of debt distress in the medium term**. The authorities' debt restructuring strategy aims to bring external

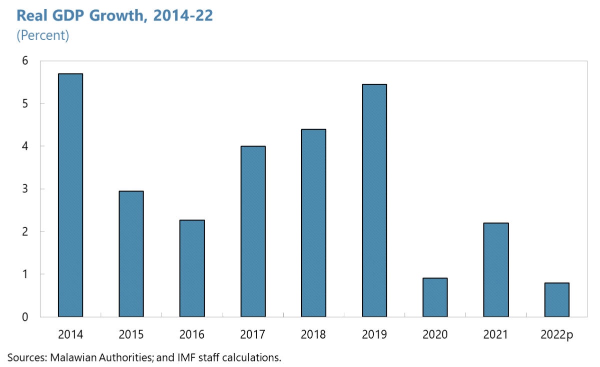
debt service down substantially through a significant treatment of commercial debt and an eventual reprofiling of official bilateral debt. A concerted effort among the authorities, their creditors and the international development partners will be crucial to ensure successful implementation of the debt restructuring strategy.

48. Addressing weakness in governance and institutions will be important priorities. In this regard, the authorities are undertaking strong corrective actions to address the misreporting under the 2018 ECF including through the special audit of RBM's foreign exchange reserves completed in June 2022 and decisively implementing several corrective measures to strengthen foreign exchange reserve management. To address other longstanding governance weaknesses, it will be critical for the authorities to press ahead with implementation of their anti-corruption agenda anchored on the 4 Ps. The authorities have taken some specific actions thus far, including audits of Covid-19 public funds and the EDF, which uncovered misappropriation of funds, and the restructuring of ADMARC. The government should follow through with a strong implementation of the audit recommendations in order to decisively stamp out corruption. To support these efforts, the authorities are committed to undertaking a governance diagnostic exercise under program, leveraging IMF TA.

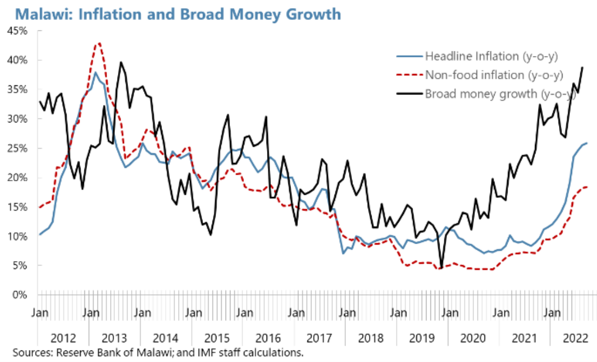
49. Staff supports the authorities' request for a disbursement under the Rapid Credit Facility—Food Shock Window—with access equivalent to SDR 69.40 million (50 percent of quota) and a Staff Monitored Program with Executive Board Involvement. In the context of an on-going food crisis, and on the basis of a concerted effort among the authorities, their creditors and the international development partners to support Malawi, staff supports this request. Risks to the program are high but can be mitigated by the authorities' commitment, measures taken thus far, and the government's efforts to address socio-economic fragility and to maintain political stability.

Figure 1. Malawi: Real Sector Developments, 2010–22

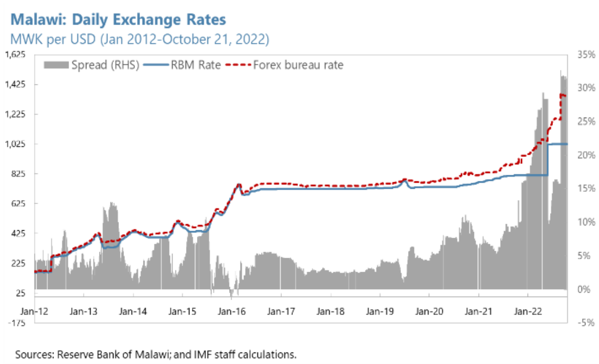
Real GDP, hard hit by COVID-19, recurring cyclones, and spillovers from the war in Ukraine, slows down to 0.8 percent in 2022 from 5.4 percent in 2019 …



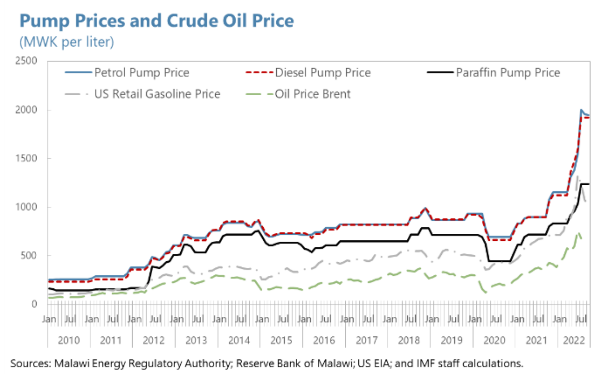
Inflationary pressures are rising given the surge in fuel, food and fertilizers prices, and broad money growth.



In turn, pressure on the exchange rate is mounting with the spread between the Forex bureau rate and the RBM rate at 32 percent at end-September 2022…



Along with the Kwacha depreciation, rising international crude oil prices also contributed to higher fuel prices.

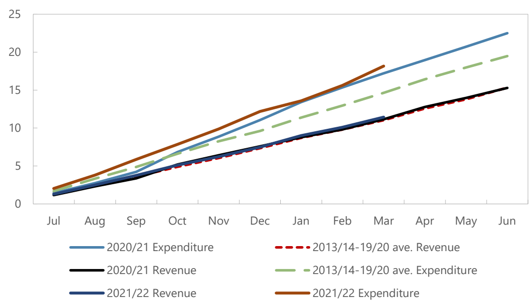


Sources: Reserve Bank of Malawi; Ministry of Finance; and IMF staff estimates.

Figure 2. Fiscal Sector Developments, 2005–22

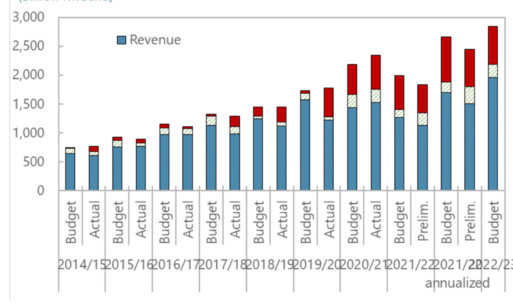
Revenues are holding up, while expenditure is exceeding previous years' average due to emergency response and fuel and fertilizers price hikes but also slippages

Revenue and Expenditure, 2013-22
(percent of GDP)



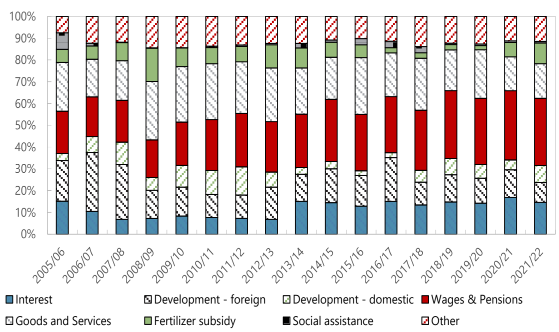
Overly optimistic budget revenue projections and lack of commitment control have led to domestic financing

Malawi: Budget versus Outturn, 2014-22
(Billion Kwacha)



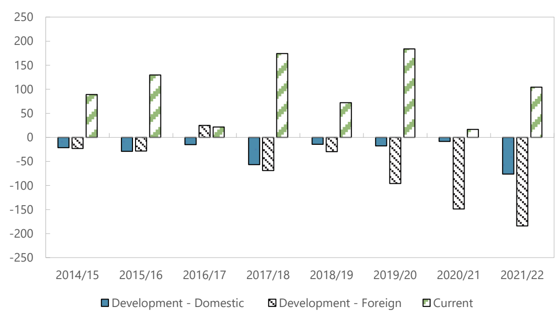
Interest payments and other recurrent spending have increased crowding out social spending…

Composition of Expenditure



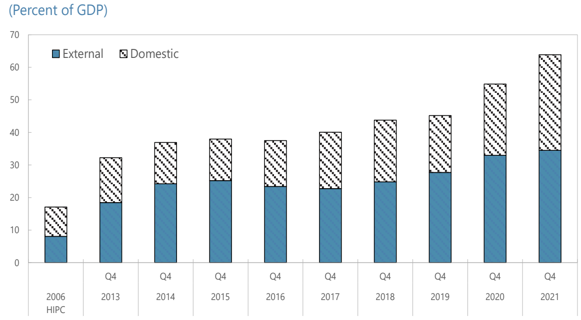
… while capital spending has been under executed.

Difference Between Execution and Budgeted
(MWK Billion)



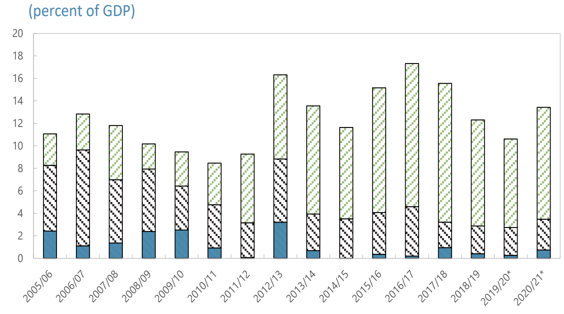
Public debt to reach historically high levels…

Public Debt, 2006-21
(Percent of GDP)



Looking ahead, on-budget support comparable to pre-2013 levels will be crucial for Malawi meet development needs and sustain growth.

Official Development Assistance, 2005-21
(percent of GDP)

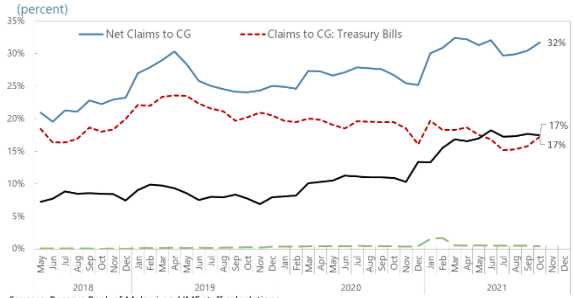


Sources: Ministry of Finance; Reserve Bank of Malawi; and IMF staff estimates.

Figure 3. Malawi: Monetary Sector Developments, 2012–22

The banking sector is highly exposed to the public sector, and its capacity to absorb securities may be maxed out…

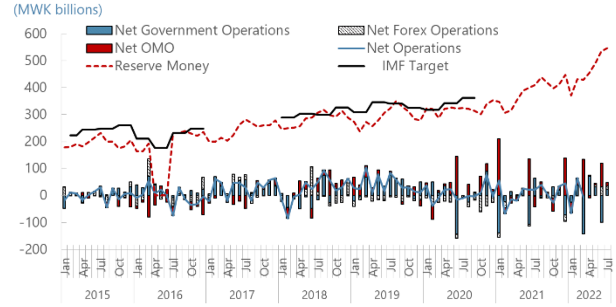
ODC Claims to the Central Government to Total Assets
(percent)



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

… by looking at the RBM's liquidity injections accompanying sovereign security issuances in 2021.

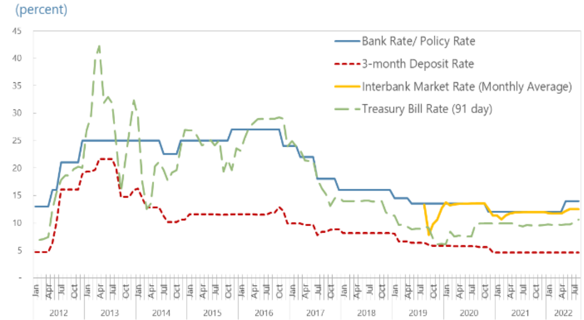
RBM Market Operations
(MWK billions)



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

The monetary policy rate was raised to 14 percent in May 2022…

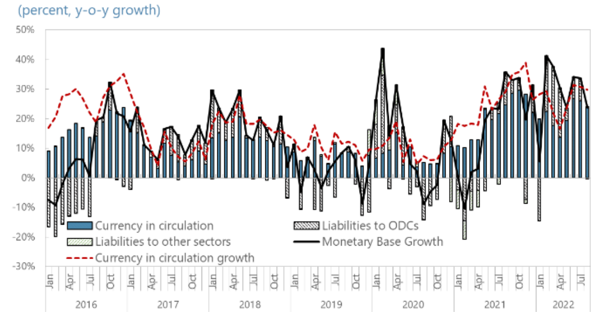
Interest Rate Developments
(percent)



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

but policy stance has become de facto much loser with a rapid growth in currency in circulation…

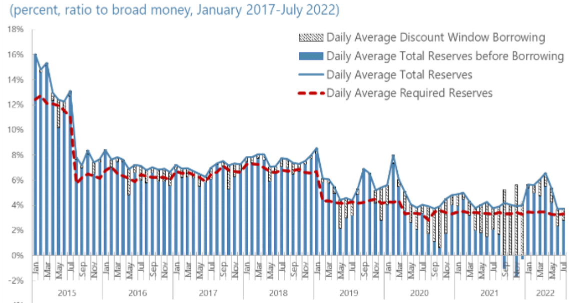
Contribution to Monetary Base Growth
(percent, y-o-y growth)



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

… and banks barely meeting prudential regulations …

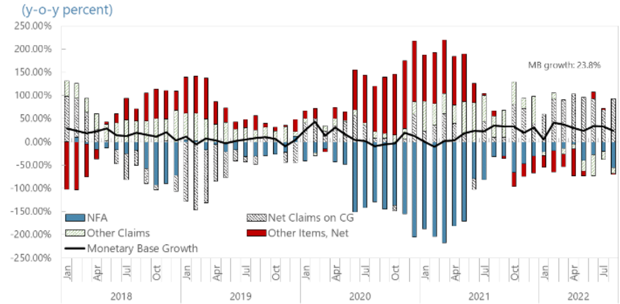
Bank Reserves Developments
(percent, ratio to broad money, January 2017-July 2022)



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

Monetary base growth is associated with growth in net claims to the central government and claims to ODCs, offsetting contraction in net foreign assets

Contribution to Monetary Base Growth
(y-o-y percent)



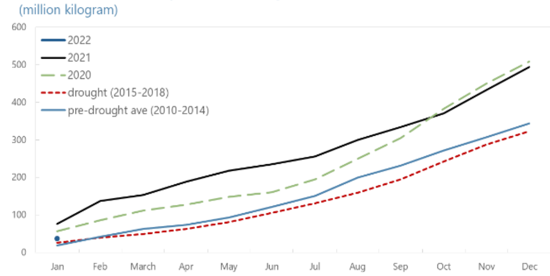
Sources: Reserve Bank of Malawi; and IMF staff calculations.

Sources: Reserve Bank of Malawi; Ministry of Finance; and IMF staff estimates.

Figure 4. Malawi: External Sector Developments, 2010–22

Imports add strain to scarce foreign exchange reserves. Notably, fertilizer import volume has increased relative to previous years.

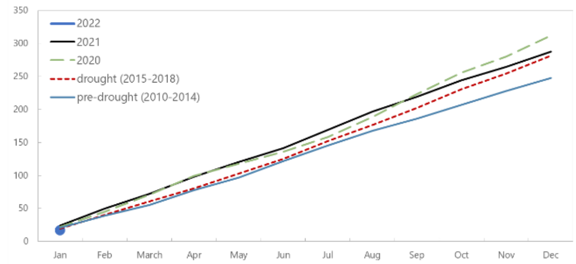
Cumulative Monthly Fertilizer Import Volume
(million kilogram)



Sources: National Statistics Office of Malawi; and IMF staff calculations.

Fuel import volumes in 2020 and 2021 are higher than historical average levels.

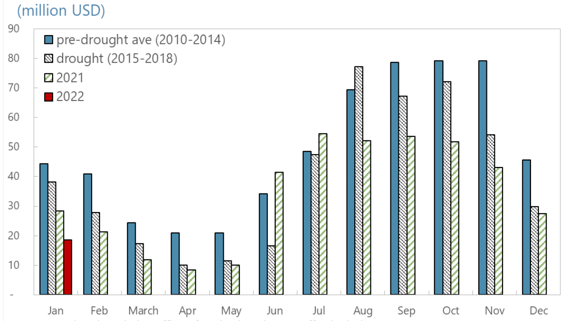
Cumulative Monthly Fuel Import Volume
(million liters)



Sources: National Statistics Office of Malawi; and IMF staff calculations.

Meanwhile, tobacco exports have not returned to its pre-drought average earnings.

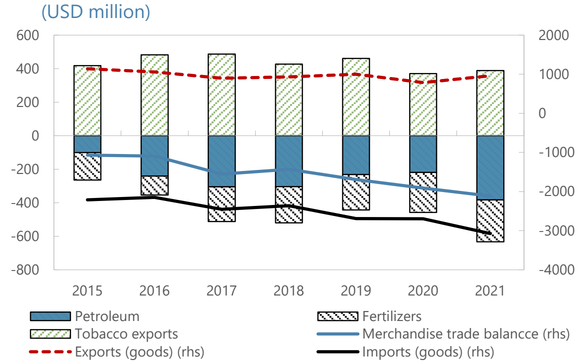
Monthly Tobacco Exports
(million USD)



Sources: National Statistics Office of Malawi; and IMF staff calculations.

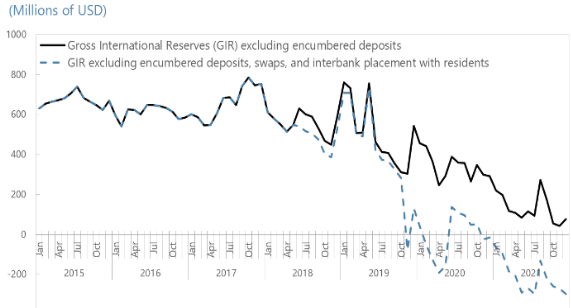
Spillovers from war in Ukraine are adding to Fuel and fertilizers imports, with stagnant exports, weigh on widening trade and current account balances

Exports and Imports, 2015-22
(USD million)



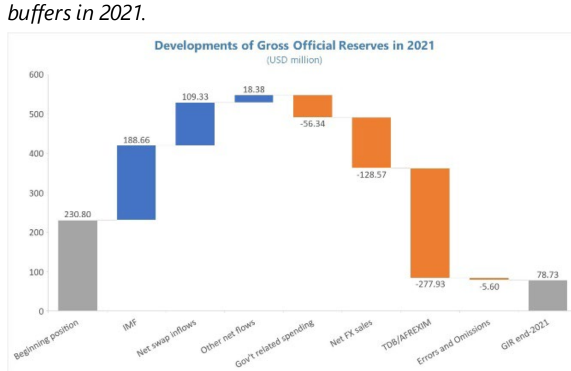
External buffers are depleted.

Malawi: International Reserves
(Millions of USD)



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

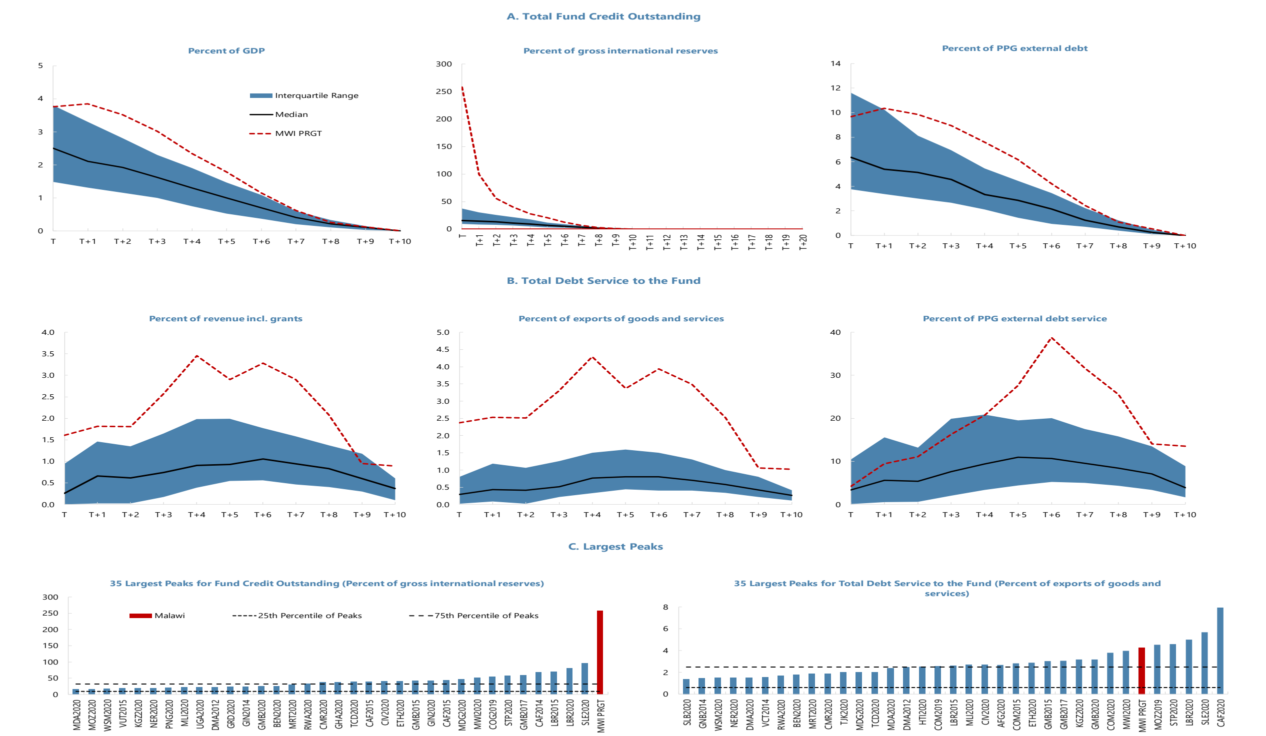
Sales of FX to authorized dealers along with non-concessional loan repayments to regional development banks drained FX buffers in 2021.



Sources: Reserve Bank of Malawi; Ministry of Finance; and IMF staff estimates.

Figure 5. Malawi: Capacity to Repay Indicators Compared to EF Arrangements for PRGT Countries

(In Percent of the Indicated Variables)



Notes:

1) T= date of arrangement approval. PPG = public and publicly guaranteed.
2) Red lines/bars indicate the CtR indicator for the arrangement of interest.
3) The median, interquartile range, and comparator bars reflect all UCT arrangements (including blends) approved for PRGT countries between 2010-2020.
4) PRGT countries in the control group with multiple arrangements are entered as separate events in the database.

Table 1. Malawi: Selected Economic Indicators, 2021–27

	2021	2022	2023	2024	2025	2026	2027
	Prel.			Proj.			
National accounts and prices (percent change, unless otherwise indicated)							
GDP at constant market prices	2.2	0.8	2.4	3.2	3.8	4.3	4.5
Nominal GDP (billions of Kwacha)	9,599	11,354	14,018	16,684	19,278	21,641	24,048
GDP deflator	6.5	17.3	20.6	15.3	11.3	7.6	6.3
Consumer prices (end of period)	11.5	26.0	20.4	15.2	9.9	7.6	6.5
Consumer prices (annual average)	9.3	20.8	22.7	17.1	12.1	8.1	6.8
Investment and savings (percent of GDP)							
National savings	-5.4	-4.8	-3.6	-3.1	-4.1	-2.7	-2.1
Government	-6.1	-5.1	-7.8	-5.2	-4.4	-3.7	-2.3
Private	0.7	0.3	4.2	2.1	0.4	1.0	0.3
Gross investment	9.2	9.9	10.1	11.2	9.0	8.5	7.5
Government	6.6	6.9	7.3	8.5	6.3	5.8	4.9
Private	2.6	3.0	2.8	2.7	2.7	2.7	2.6
Saving-investment balance	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Central government (percent of GDP on a fiscal year basis)[1, 2]							
Revenue	14.9	15.4	15.5	17.0	18.1	17.5	16.9
Tax and nontax revenue	13.1	13.4	13.9	14.9	15.7	15.9	16.1
Grants	1.7	1.9	1.6	2.1	2.4	1.6	0.8
Expenditure and net lending	22.3	24.3	24.6	25.8	25.6	24.2	23.1
Overall balance (excluding grants)	-9.2	-11.6	-10.6	-10.5	-9.2	-7.2	-5.8
Overall balance (including grants)	-7.5	-9.7	-9.0	-8.4	-6.8	-5.6	-5.0
Foreign financing	1.3	2.8	-0.6	0.2	0.4	0.4	0.2
Total domestic financing	8.2	7.4	5.6	3.8	4.4	3.4	4.1
Financing gap/residual gap	0.0	0.0	4.1	4.5	2.1	1.9	0.8
Discrepancy	-0.1	-0.8	0.0	0.0	0.0	0.0	0.0
Primary balance	-3.7	-5.4	-3.3	-1.7	-0.2	0.7	0.8
Domestic primary balance[3]	-2.5	-4.1	-0.6	0.8	2.2	2.7	2.4
Money and credit (change in percent of broad money at the end of the period, unless otherwise indicated)							
Broad money	30.0	27.5	23.5	19.0	15.5	12.3	10.6
Net foreign assets	-3.9	42.1	19.1	20.9	13.8	11.1	5.0
Net domestic assets	33.9	-14.6	4.3	-1.9	1.8	1.2	5.6
o/w Net claims on the government	41.0	28.0	26.0	22.0	18.7	19.9	10.9
Credit to the private sector (percent change)	18.6	27.9	14.7	10.9	8.2	7.4	5.2
External sector (US$ millions, unless otherwise indicated)							
Exports (goods and services)	1,262	1,294	1,421	1,477	1,544	1,638	1,792
Imports (goods and services)	3,255	3,406	3,173	3,292	3,265	3,217	3,261
Gross official reserves[4]	429	172	409	682	835	980	1,039
(months of imports)	1.6	0.6	1.5	2.5	3.1	3.6	3.7
Net international reserves[4]	-1,308.1	-584.1	-312.2	-4.1	193.9	444.8	596.9
Current account (percent of GDP)	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Current account, excl. official transfers (percent of GDP)	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Current account, excl. project related imports (percent of GDP)	-12.4	-12.3	-10.8	-11.0	-10.7	-9.4	-8.1
Real effective exchange rate (percent change)	...	...	...	...	...	...	...
Overall balance (percent of GDP)	0.0	-1.7	-2.4	0.2	-0.1	0.0	0.5
Financing gap (percent of GDP)	0.0	2.8	4.9	2.6	1.9	1.8	0.5
Terms of trade (percent change)	-19.0	-14.9	-0.5	-1.3	3.9	3.1	2.0
Debt stock and service (percent of GDP, unless otherwise indicated)							
External debt (public sector)	32.8	38.9	37.1	35.6	33.6	30.9	28.8
NPV of public external debt (percent of exports)	235.5	202.3	176.6	164.9	153.3	137.7	124.0
Domestic public debt	31.2	37.7	37.5	38.8	40.2	41.7	42.2
Total public debt	64.0	76.6	74.6	74.5	73.8	72.6	71.0
External debt service (percent of exports)	14.4	55.6	26.7	22.7	20.2	20.6	12.2
External debt service (percent of revenue excl. grants)	4.9	43.2	24.6	20.2	17.8	18.3	11.1

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

[1] The current financial year, 2021, runs from July 1, 2020 to June 30, 2021. FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year.

[2] Please note that government fiscal statistics are reported following the Government Finance Statistics Manual (2014) starting 2020 projections and going forward.

[3] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and nontax revenues.

[4] Gross official reserves figures include encumbered deposits in 2021; all figures from 2022 onwards do not include encumbered deposits. Readily available gross official reserves were US$71.7 million in 2021.

Table 2a. Malawi: Central Government Operations, 2020/21–26/27[1]

(Billions of Kwacha)

	2020/21	2021/22	2022/23			2023/24	2024/25	2025/26	2026/27
	Actual	Prel.	Budget	Revised Budget (proposed)	Proj.		Proj.		
REVENUE	1,363.8	1,186.5	1,955.8	2,035.0	1,845.4	2,474.2	3,111.0	3,468.1	3,742.0
Taxes	1,136.0	978.3	1,534.8	1,561.3	1,561.3	2,050.1	2,566.5	3,004.2	3,408.5
Taxes on income profits and capital gains	539.9	451.3	731.4	717.5	717.5	916.7	1,132.3	1,326.3	1,507.7
Taxes on goods and services	502.7	439.1	665.6	696.5	696.5	951.3	1,216.2	1,423.9	1,612.0
Taxes on international trade and transaction	92.5	86.8	136.2	145.7	145.7	180.1	215.5	251.1	285.4
Other taxes	0.9	1.1	1.6	1.7	1.7	2.1	2.5	2.9	3.3
Grants	157.9	149.8	320.3	379.3	189.7	311.1	412.4	317.4	174.0
Current	16.0	0.0	0.0	189.6	0.0	0.0	0.0	0.0	0.0
Capital	141.9	149.8	320.3	189.7	189.7	311.1	412.4	317.4	174.0
Project grants	116.7	123.2	...	142.2	142.2	242.5	338.7	243.7	92.8
Dedicated Grants	25.2	26.6	...	47.4	47.4	68.6	73.7	73.8	81.1
Other Revenue	69.9	58.5	100.7	94.4	94.4	113.0	132.1	146.5	159.5
EXPENDITURE	2,049.7	1,920.6	2,839.9	2,877.2	2,921.7	3,696.1	4,280.0	4,579.6	4,858.7
EXPENSE	1,695.6	1,530.5	2,021.0	2,248.1	2,291.5	2,868.7	3,292.1	3,695.4	3,966.4
Compensation of employees	552.9	496.4	688.8	767.5	767.5	898.7	1,016.0	1,134.7	1,269.7
Purchase of goods and services	329.6	310.9	363.6	368.3	368.3	442.4	507.2	623.1	630.6
Generic goods and services	212.2	181.7	225.7	228.1	228.1	270.8	304.1	331.6	371.4
Health Sector	57.5	61.5	70.4	63.6	63.6	77.9	92.0	105.7	118.3
Agriculture Sector	7.3	12.4	9.2	18.6	18.6	22.7	26.9	30.8	34.5
Education Sector	34.2	32.0	41.3	40.6	40.6	49.7	58.7	67.4	75.5
Expenditure for arrears	2.9	3.1	1.0	0.8	0.8	0.0	0.0	0.0	0.0
Storage levy expenses	1.6	1.2	1.0	1.0	1.0	1.8	2.2	2.5	2.8
Maize purchases	10.4	19.0	12.0	15.1	15.1	18.5	21.8	25.1	28.1
Other	3.6	0.0	3.0	0.5	0.5	1.0	0.0	0.1	0.0
Interest	348.3	271.2	520.7	645.1	688.5	976.2	1,143.2	1,246.6	1,296.4
To non-residents	17.7	12.6	19.7	33.2	73.1	74.0	72.0	68.2	64.0
To residents other than general government	330.6	258.5	501.1	612.0	615.4	902.2	1,071.2	1,178.3	1,232.4
Grants	191.2	172.7	219.1	260.0	260.0	308.5	352.0	389.6	432.1
Current	168.9	157.2	207.1	220.5	220.5	262.8	306.3	343.9	386.5
Road fund Administration	32.9	37.6	40.3	44.5	44.5	54.4	64.3	73.8	82.7
Transfers to MRA	31.5	30.6	45.6	45.6	45.6	61.5	77.0	90.1	102.3
Transfers to public entities	104.4	89.1	121.2	130.5	130.5	146.9	165.0	179.9	201.5
Capital	22.3	15.5	12.0	39.5	39.5	45.7	45.7	45.7	45.7
Rural electrification programme	13.3	6.5	...	27.5	27.5	33.7	33.7	33.7	33.7
Net Lending	9.0	9.0	12.0	12.0	12.0	12.0	12.0	12.0	12.0
Social Benefits	244.4	248.8	213.6	192.4	192.4	233.8	263.1	289.3	323.9
Social assistance benefits	141.2	171.1	112.2	76.2	76.2	98.7	108.1	116.7	130.6
Fertiliser payments[2]	121.1	156.6	100.8	69.8	69.8	88.5	96.9	104.5	117.0
Maize seed subsidy[2]	17.0	12.3	8.8	4.4	4.4	7.7	8.4	9.2	10.3
Social Cash Transfer-Government	3.0	2.3	2.6	2.0	2.0	2.4	2.8	3.1	3.3
Pensions and gratuities	103.3	77.7	100.9	116.3	116.3	135.2	155.0	172.6	193.3
Other Expenses	29.2	30.5	15.3	14.7	14.7	9.0	10.7	12.2	13.7
Acquisition of Non-Financial Assets (Development Expenditure)	354.1	390.1	818.9	629.1	630.2	827.4	987.9	884.2	892.4
Foreign (Part I)	261.6	246.7	580.9	506.4	507.5	680.3	817.4	714.8	531.3
Domestic (Part II)	92.6	143.4	237.9	122.7	122.7	147.2	170.5	169.4	361.1
Discrepancy	-4.8	-58.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall Balance (incl. grants and discrepancy)	-690.7	-792.1	-884.0	-842.2	-1,076.3	-1,221.9	-1,169.1	-1,111.5	-1,116.8
Primary Balance	-337.6	-462.9	-363.3	-197.1	-387.8	-245.6	-25.8	135.1	179.6
Domestic Primary Balance[3]	-233.9	-366.0	-102.7	-70.0	-70.0	123.5	379.2	532.4	536.9
NET FINANCING (Repayment if negative)	690.7	792.1	884.0	842.2	1,076.3	1,221.9	1,169.1	1,111.5	1,116.8
Net Incurrence of Liabilities	759.6	844.5	884.0	842.2	1,076.3	1,221.9	1,169.1	1,111.5	1,116.8
Total Financing	759.6	844.5	884.0	842.2	594.1	570.3	815.1	744.3	942.7
Foreign financing (net)	119.8	213.9	230.1	183.8	-68.8	22.1	62.8	72.5	45.6
Loans	119.8	213.9	230.1	183.8	-68.8	22.1	62.8	72.5	45.6
Programme Borrowing	51.7	0.0	41.4	98.6	0.0	0.0	0.0	0.0	0.0
Project Loans	110.1	96.9	260.6	363.6	363.6	369.1	405.0	397.3	357.3
Other concessional loans	0.0	151.8	...	0.0	0.0	0.0	0.0	0.0	0.0
Non-concessional loans	0.0	0.0	...	0.0	0.0	0.0	0.0	0.0	0.0
Amortisation	-42.0	-34.8	-72.0	-278.4	-432.4	-347.0	-342.3	-324.8	-311.7
Domestic financing (net)	749.3	570.3	654.0	658.4	662.9	548.2	752.3	671.7	897.0
Debt Instruments	637.3	630.6	...	...	...	...	...	...	...
Banking system	...	...	...	...	...	...	...	...	...
Gross borrowing Monetary	...	...	...	...	...	...	...	...	...
Gross borrowing Commercial banks	...	...	...	...	...	...	...	...	...
Nonbank sector	...	...	...	...	...	...	...	...	...
Zero coupon promissory notes	109.6	30.0		0.0	0.0	0.0	0.0	0.0	0.0
Amortization	0.0	90.3		-81.2	-1,017.6	-1,371.4	-1,681.6	-1,507.6	-1,800.5
Financing Gap				0.0	482.2	651.6	354.0	367.2	174.1
RCF budget support (prospective)					98.6	...	...	...	...
Unidentified financing gap[4]					383.6	651.6	354.0	367.2	174.1

Memorandum items:

Sources: Malawi Ministry of Finance; and IMF staff projections.

[1] FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year starting from FY2022/23

[2] Farm Input Subsidy Program prior to FY20/21

[3] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and non-tax revenues.

[4] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

Table 2b. Malawi: Central Government Operations, FY 2020/21–2026/27[1]
(Percent of GDP)

	2020/2	2021/22	2022/23			2023/24	2024/25	2025/26	2026/27
	Actual	Prel.	Budget	Revised Budget (proposed)	Proj.	Proj.			
REVENUE	14.9	15.4	17.1	17.1	15.5	17.0	18.1	17.5	16.9
Taxes	12.4	12.7	13.5	13.1	13.1	14.1	14.9	15.2	15.4
Taxes on income profits and capital gains	5.9	5.9	6.4	6.0	6.0	6.3	6.6	6.7	6.8
Taxes on goods and services	5.5	5.7	5.8	5.9	5.9	6.5	7.1	7.2	7.3
Taxes on international trade and transaction	1.0	1.1	1.2	1.2	1.2	1.2	1.3	1.3	1.3
Other taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	1.7	1.9	2.8	3.2	1.6	2.1	2.4	1.6	0.8
Current	0.2	0.0	0.0	1.6	0.0	0.0	0.0	0.0	0.0
Capital	1.5	1.9	2.8	1.6	1.6	2.1	2.4	1.6	0.8
Project grants	1.3	1.6	…	1.2	1.2	1.7	2.0	1.2	0.4
Dedicated Grants	0.3	0.3	…	0.4	0.4	0.5	0.4	0.4	0.4
Other Revenue	0.8	0.8	0.9	0.8	0.8	0.8	0.8	0.7	0.7
EXPENDITURE	22.3	24.3	24.9	24.2	24.6	25.8	25.6	24.2	23.1
EXPENSE	18.5	19.2	17.7	18.9	19.3	20.1	19.9	19.7	19.0
Compensation of employees	6.0	6.4	6.0	6.4	6.4	6.2	5.9	5.7	5.7
Purchase of goods and services	3.6	4.0	3.2	3.1	3.1	3.0	2.9	3.2	2.8
Generic goods and services	2.3	2.4	2.0	1.9	1.9	1.9	1.8	1.7	1.7
Health Sector	0.6	0.8	0.6	0.5	0.5	0.5	0.5	0.5	0.5
Agriculture Sector	0.1	0.2	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Education Sector	0.4	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.3
Expenditure for arrears	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Storage levy expenses	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Maize purchases	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest	3.8	3.5	4.6	5.4	5.9	7.1	7.4	7.3	7.0
To non-residents	0.2	0.2	0.2	0.3	0.6	0.5	0.4	0.3	0.3
To residents other than general government	3.6	3.4	4.4	5.1	5.2	6.6	7.0	7.0	6.7
Grants	2.1	2.2	1.9	2.2	2.2	2.1	2.0	2.0	2.0
Current	1.8	2.0	1.8	1.9	1.9	1.8	1.8	1.7	1.7
Road fund Administration	0.4	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Transfers to MRA	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.5	0.5
Transfers to public entities	1.1	1.2	1.1	1.1	1.1	1.0	1.0	0.9	0.9
Capital	0.2	0.2	0.1	0.3	0.3	0.3	0.3	0.2	0.2
Rural electrification programme	0.1	0.1	…	0.2	0.2	0.2	0.2	0.2	0.2
Net Lending	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Social Benefits	2.7	2.7	1.9	1.6	1.6	1.6	1.5	1.5	1.5
Social assistance benefits	1.5	1.7	1.0	0.6	0.6	0.7	0.6	0.6	0.6
Fertiliser payments[2]	1.3	1.5	0.9	0.6	0.6	0.6	0.6	0.5	0.5
Maize seed subsidy[2]	0.2	0.1	0.1	0.0	0.0	0.1	0.0	0.0	0.0
Social Cash Transfer-Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pensions and gratuities	1.1	1.0	0.9	1.0	1.0	0.9	0.9	0.9	0.9
Other Expenses	0.3	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Acquisition of Non-Financial Assets (Development Expenditure)	3.9	5.1	7.2	5.3	5.3	5.7	5.7	4.5	4.0
Foreign (Part I)	2.9	3.2	5.1	4.3	4.3	4.7	4.7	3.6	2.4
Domestic (Part II)	1.0	1.9	2.1	1.0	1.0	1.0	1.0	0.9	1.6
Discrepancy	-0.1	-0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall Balance (incl. grants and discrepancy)	-7.5	-9.7	-7.8	-7.1	-9.0	-8.4	-6.8	-5.6	-5.0
Primary Balance	-3.7	-5.4	-3.2	-1.7	-3.3	-1.7	-0.2	0.7	0.8
Domestic Primary Balance[3]	-2.5	-4.1	-0.9	-0.6	-0.6	0.8	2.2	2.7	2.4
NET FINANCING (Repayment if negative)	7.5	10.3	7.8	7.1	9.0	8.4	6.8	5.6	5.0
Net Incurrence of Liabilities	8.3	11.0	7.8	7.1	9.0	8.4	6.8	5.6	5.0
Total Financing	8.3	11.0	7.8	7.1	5.0	3.9	4.7	3.8	4.3
Foreign financing (net)	1.3	2.8	2.0	1.5	-0.6	0.2	0.4	0.4	0.2
Loans	1.3	2.8	2.0	1.5	-0.6	0.2	0.4	0.4	0.2
Programme Borrowing	0.6	0.0	0.4	0.8	0.0	0.0	0.0	0.0	0.0
Project Loans	1.2	1.3	2.3	3.1	3.1	2.5	2.4	2.0	1.6
Other concessional loans	0.0	2.0	…	0.0	0.0	0.0	0.0	0.0	0.0
Non-concessional loans	0.0	0.0	…	0.0	0.0	0.0	0.0	0.0	0.0
Amortisation	-0.5	-0.5	-0.6	-2.3	-3.6	-2.4	-2.0	-1.6	-1.4
Domestic financing (net)	8.2	7.4	5.7	5.5	5.6	3.8	4.4	3.4	4.1
Debt Instruments	6.9	8.2	…	…	…	…	…	…	…
Banking system	…	…	…	…	…	…	…	…	…
Gross borrowing Monetary	…	…	…	…	…	…	…	…	…
Gross borrowing Commercial banks	…	…	…	…	…	…	…	…	…
Nonbank sector	…	…	…	…	…	…	…	…	…
Zero Coupon Promissory Note	1.2	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	0.0	1.2	0.0	-0.7	-8.6	-9.4	-9.8	-7.6	-8.1
Financing Gap				0.0	4.1	4.5	2.1	1.9	0.8
RCF budget support (prospective)					0.8	…	…	…	…
Unidentified financing[4]					3.2	5.5	3.0	3.1	1.5

Sources: Malawi Ministry of Finance; and IMF staff projections.

[1] FY2021/22 covers 1 July 2021 to 31 March 2022, to accommodate the transition to an April - March fiscal year starting from FY2022/23.

[2] Farm Input Subsidy Program prior to FY20/21

[3] Domestic primary balance is calculated by subtracting current expenditures (except interest payment) and domestically-financed development expenditures from tax and nontax revenues.

[4] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

Table 3a. Malawi: Monetary Authorities' Balance Sheet, 2021–27

(Billions of Kwacha, Unless Otherwise Indicated)

	2021				2022				2023	2024	2025	2026	2027
	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Dec.					
	Actual				Actual		Proj.		Proj.				
Monetary base	318	400	419	449	461	532	536	573	707	842	973	1,092	1,214
Currency in circulation	257	341	349	359	313	448	…	…	…	…	…	…	…
Liabilities to other depository corporations	58	58	-4	-39	-69	-105	…	…	…	…	…	…	…
Liabilities to other sectors	3	1	0	0	0	0	…	…	…	…	…	…	…
Net foreign assets (NFA) [1]	-575	-564	-519	-569	-619	-673	-46	207	587	1,124	1,515	1,884	2,093
Claims on nonresidents	328	353	436	361	307	438	…	…	…	…	…	…	…
Official reserve assets	47	93	141	73	49	38	…	…	…	…	…	…	…
Other foreign assets	281	260	295	287	289	289	…	…	…	…	…	…	…
Liabiliites to nonresidents	-903	-917	-955	-930	-926	-1,110	…	…	…	…	…	…	…
Short -term foreign liabilities	-313	-314	-332	-298	-298	-298	…	…	…	…	…	…	…
Other foreign liabilities	-589	-604	-623	-631	-635	-637	…	…	…	…	…	…	…
NFA (US$ millions)	-685	-694	-631	-694	-752	-651	-45	172	408	680	833	977	1,036
Net domestic assets	893	964	938	1,018	1,080	1,205	582	366	120	-282	-542	-791	-880
Net claims on central government	440	355	415	541	730	730	…	…	…	…	…	…	…
Claims on central government	2,983	3,026	3,267	3,671	4,176	4,551	…	…	…	…	…	…	…
Liabilities to central government	2,542	2,671	2,852	3,130	3,446	3,821							
Claims on other depository corporations	10	9	46	33	34	34	…	…	…	…	…	…	…
Claims on public nonfinancial corportions	186	189	174	146	143	170	…	…	…	…	…	…	…
Claims on private sector	697	776	806	822	803	927	…	…	…	…	…	…	…
Other items (net)	-440	-366	-549	-557	-664	-690	-1,407	-1,668	-2,162	-2,798	-3,271	-3,795	-4,133
Memorandum items:													
Money multiplier	5.1	4.4	4.3	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5
Annual growth of reserve money (percent)	2.0	23.6	33.0	31.3	45.0	32.8	27.7	27.5	23.5	19.0	15.5	12.3	11.1
91-day treasury bill rate	10.0	10.0	9.6	9.6	9.7	9.7	…	…	…	…	…	…	…
NFA of the central bank (US$ millions)	-685	-694	-631	-694	-752	-651	-45	172	408	680	833	977	1,036
Foreign assets (US$ millions)	431	435	530	440	373	423	239	172	409	682	835	980	1,039
Foreign liabilities (US$ millions)	-1,116	-1,129	-1,161	-1,134	-1,125	-1,075	-284	0	-1	-2	-2	-3	-3

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

[1] Including SDR allocation and the entire assets and liabilities of the RBM.

Table 3b. Malawi: Monetary Survey, 2021–27

(Billions of Kwacha, Unless Otherwise Indicated)

	2021				2022				2023	2024	2025	2026	2027
	Mar.	June.	Sept.	Dec.	Mar.	June.	Sept.	Dec.					
	Actual				Actual		Proj.		Proj.				
Broad money liabilities	1,614	1,744	1,817	2,004	2,058	2,372	2,389	2,556	3,155	3,755	4,339	4,871	5,413
Currency outside depository corporations	959	1,096	1,124	1,218	1,270	1,540	...	...	...	...	...	...	...
Transferable deposits	655	648	694	787	788	832	...	...	...	...	...	...	...
Other deposits	0	0	0	0	0	0	...	...	...	...	...	...	...
Net foreign assets (NFA)	-471	-438	-413	-406	-494	-489	153	439	928	1,589	2,106	2,588	2,667
Monetary authorities	-575	-564	-519	-569	-619	-673	-46	207	587	1,124	1,515	1,884	2,093
Gross foreign assets	328	353	436	361	307	438	...	...	...	...	...	...	...
Foreign liabilities	-903	-917	-955	-930	-926	-1,110	...	...	...	...	...	...	...
Commercial banks (net)	103	125	105	163	125	184	199	231	340	465	592	704	820
NFA of the commercial banks (US$ millions)	128	154	128	199	152	178	193	192	237	282	325	365	406
Gross foreign assets (US$ millions)	203	255	221	302	277	300	305	306	378	450	519	583	648
Foreign liabilities (US$ millions)	-76	-101	-93	-102	-126	-122	-111	-114	-141	-168	-194	-218	-242
Domestic Claims	2,085	2,182	2,231	2,410	2,552	2,861	2,237	2,117	2,227	2,167	2,233	2,283	2,500
Net claims on central government	1,211	1,186	1,190	1,609	1,747	1,824	1,997	2,171	2,835	3,529	4,232	5,098	5,856
Claims on central government	2,983	3,026	3,267	3,671	4,176	4,551	...	...	...	...	...	...	...
Liabilities to central government	2,542	2,671	2,852	3,130	3,446	3,821	...	...	...	...	...	...	...
Claims on other sectors	892	975	1,026	1,001	980	1,131	...	...	...	...	...	...	...
Claims on other financial corporations	10	9	46	33	34	34	...	...	...	...	...	...	...
Claims on public nonfinancial corporations	186	189	174	146	143	170	...	...	...	...	...	...	...
Claims on private sector	697	776	806	822	803	927	1,001	1,051	1,206	1,338	1,448	1,555	1,652
Other items (net)	-440	-366	-549	-557	-664	-690	-1,407	-1,668	-2,162	-2,798	-3,271	-3,795	-4,133
Memorandum items:													
Velocity of money (annualized GDP divided by broad money)	5.6	5.3	5.2	4.8	4.8	4.4	4.5	4.4	4.4	4.4	4.4	4.4	4.4
Annual growth of broad money (percent)	22.3	23.7	24.8	30.0	27.5	36.0	31.5	27.5	23.5	19.0	15.5	12.3	11.1
Annual growth of credit to the private sector (percent)[1]	18.9	27.0	21.7	18.6	15.2	19.4	24.2	27.9	14.7	10.9	8.2	7.4	5.2
NFA of the commercial banks (US$ millions)	127.7	154.5	128.3	199.0	151.8	177.9	193.5	191.6	236.5	281.5	325.3	365.2	405.8
Gross foreign assets (US$ millions)	203.4	255.5	220.8	301.5	277.4	300.4	304.8	306.0	377.7	449.6	519.5	583.1	648.0
Foreign liabilities (US$ millions)	-75.7	-101.0	-92.5	-102.5	-125.6	-122.4	-111.4	-114.4	-141.2	-168.0	-194.2	-218.0	-242.2
Nominal GDP (billions of Kwacha)	9,599	9,599	9,599	9,599	11,354	11,354	11,354	11,354	14,018	16,684	19,278	21,641	24,048

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

[1] Different treatment of external debt of reserve bank of Malawi between the past and projection periods leads to a surge in credit to private sector in 2021. This will be fixed after TA mission on the treatment of external debt.

Table 4a. Malawi: Balance of Payments, 2021–27
(Millions of U.S. Dollars, Unless Otherwise Indicated)

	2021	2022	2023	2024	2025	2026	2027
	Prel.			Proj.			
Current account balance	-1,750.7	-1,740.3	-1,447.0	-1,549.3	-1,455.9	-1,294.9	-1,167.6
Merchandise trade balance	-1,914.3	-1,995.7	-1,684.4	-1,741.0	-1,610.6	-1,498.6	-1,376.4
Exports	1,076.3	1,107.5	1,229.3	1,279.2	1,338.9	1,424.4	1,568.6
Of which: Tobacco	408.4	424.2	439.0	455.2	472.0	489.9	503.6
Imports	-2,990.6	-3,103.2	-2,913.7	-3,020.2	-2,949.5	-2,923.0	-2,945.0
Of which: Petroleum products	-223.0	-270.7	-260.3	-284.7	-295.7	-307.5	-313.1
Of which: Fertilizers	-282.0	-284.1	-309.7	-315.5	-318.7	-327.1	-339.5
Of which: Project related	-266.2	-290.4	-299.8	-363.3	-267.6	-205.4	-175.7
Services balance	-471.1	-407.5	-324.6	-328.3	-365.1	-338.5	-357.9
Interest public sector	-38.7	-98.4	-58.4	-49.3	-42.1	-36.7	-33.8
Other factor payments (net)	-191.3	-192.8	-197.7	-204.2	-212.1	-221.4	-231.5
Nonfactor (net)	-79.1	-116.3	-68.6	-74.8	-110.9	-80.4	-92.6
Unrequited transfers (net)	634.7	663.0	562.0	520.0	519.8	542.2	566.7
Private (net)	635.8	664.2	563.2	521.2	521.0	543.4	567.9
Official (net)	-1.1	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2
Receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Budget support	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Payments	-1.1	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2
Capital account balance[1]	1,127.4	1,577.8	1,031.1	1,358.4	1,204.1	1,048.5	967.0
Project and dedicated grants	232.0	156.1	190.2	295.6	179.2	112.5	125.2
Off-budget project support[2]	895.4	1,421.7	840.9	1,062.8	1,024.9	936.0	841.8
Financial account balance[1]	572.2	-39.1	164.3	215.6	240.7	248.5	255.8
Financial account balance[1]	572.2	-39.1	164.3	215.6	240.7	248.5	255.8
Foreign direct investment (net)	93.0	94.3	110.0	126.9	145.5	161.3	180.0
Portfolio investment (net)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Medium- and long-term loans (net)	233.9	-190.9	9.3	40.8	42.5	26.6	11.3
SDR allocation	190.0	0.0	0.0	0.0	0.0	0.0	0.0
Disbursements	185.8	290.7	271.1	263.3	232.4	203.5	145.0
Budget support and other program loans	8.2	0.0	0.0	0.0	0.0	0.0	0.0
Project support loans	177.6	290.7	271.1	263.3	232.4	203.5	145.0
Other medium-term loans (official)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	-141.9	-481.6	-261.7	-222.5	-189.9	-176.9	-133.7
Other inflows	245.3	57.5	45.0	47.9	52.6	60.7	64.4
Overall balance	-159.1	-201.6	-251.6	24.7	-11.2	2.1	55.2
Financing	159.1	201.6	251.6	-24.7	11.2	-2.1	-55.2
Gross reserves (- increase)	159.1	-100.0	-237.4	-272.7	-153.5	-144.3	-59.7
IMF (net)	0.0	-30.8	-33.9	-35.1	-49.2	-69.0	-59.3
Purchases/drawings	0.0						
Repurchases/repayments	26.2	36.2	33.9	35.1	49.2	69.0	59.3
Exceptional financing (CCRT)	26.2	5.4					
Financing gap	0.0	332.4	522.9	283.0	213.9	211.2	63.8
RCF (prospective)		88.3					
Unidentified financing gap[3]	0.0	244.1	522.9	283.0	213.9	211.2	63.8
Memorandum items:							
Gross official reserves[4]	429.2	171.7	409.1	681.8	835.3	979.6	1,039.3
Months of imports[5]	1.6	0.6	1.5	2.5	3.1	3.6	3.7
Net international reserves[6]	-1,308.1	-584.1	-312.2	-4.1	193.9	444.8	596.9
Current account balance (percent of GDP)	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Excluding official transfers	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Excluding project related imports	-12.4	-12.3	-10.8	-11.0	-10.7	-9.4	-8.1
Excluding official transfers and project related ir	-12.4	-12.3	-10.8	-11.0	-10.7	-9.4	-8.1
Import price index (2005 = 100)	151.6	181.8	177.6	177.1	168.8	163.4	160.0
Import volume (percent change)	-11.1	-16.4	-3.9	4.0	2.5	2.3	2.9
REER (percent change)	…	…	…	…	…	…	…
Overall balance (percent of GDP)	0.0	-1.7	-2.4	0.2	-0.1	0.0	0.5
Terms of trade (percent change)	-19.0	-14.9	-0.5	-1.3	3.9	3.1	2.0
Nominal GDP (millions of U.S. dollars)	12,004	11,781	10,619	10,809	11,116	11,554	12,182

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

[1] The IMF has adopted the Malawi National Statistics Office (NSO)'s capital and financial account data following adoption of the NSO's current account data in 2019. Previously, the IMF's reported series was based on staff estimates. Consequently, the IMF's reported capital account balance increased from 3.8 percent of GDP to 11.7 percent of GDP in 2018 while financial account balance including net errors and omission decreased from 16.5 percent of GDP to 8.6 percent of GDP.

[2] Includes estimate for project grants not channeled through the budget.

[3] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

[4] Gross official reserves figures include encumbered deposits in 2021; all figures from 2022 onwards do not include encumbered deposits. Readily available gross official reserves for 2021 were US$71.7 in 2021.

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

[6] 2021 NIR is calculated as gross official reserves minus a sum of Use of Fund Credit, repamyments projection of medium term debt by remaining maturity, and short-term swap outstanding. From 2022 and onward, they are calculated as defined in TMU.

Table 4b. Malawi: Balance of Payments, 2021–27
(Percent of GDP)

	2021	2022	2023	2024	2025	2026	2027
	Prel.			Proj.			
Current account balance	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Merchandise trade balance	-15.9	-16.9	-15.9	-16.1	-14.5	-13.0	-11.3
Exports	9.0	9.4	11.6	11.8	12.0	12.3	12.9
Of which: Tobacco	3.4	3.6	4.1	4.2	4.2	4.2	4.1
Imports	-24.9	-26.3	-27.4	-27.9	-26.5	-25.3	-24.2
Of which: Petroleum products	-1.9	-2.3	-2.5	-2.6	-2.7	-2.7	-2.6
Of which: Fertilizers	-2.3	-2.4	-2.9	-2.9	-2.9	-2.8	-2.8
Of which: Project related	-2.2	-2.5	-2.8	-3.4	-2.4	-1.8	-1.4
Services balance	-3.9	-3.5	-3.1	-3.0	-3.3	-2.9	-2.9
Interest public sector	-0.3	-0.8	-0.5	-0.5	-0.4	-0.3	-0.3
Other factor payments (net)	-1.6	-1.6	-1.9	-1.9	-1.9	-1.9	-1.9
Nonfactor (net)	-0.7	-1.0	-0.6	-0.7	-1.0	-0.7	-0.8
Unrequited transfers (net)	5.3	5.6	5.3	4.8	4.7	4.7	4.7
Private (net)	5.3	5.6	5.3	4.8	4.7	4.7	4.7
Official (net)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital account balance[1]	9.4	13.4	9.7	12.6	10.8	9.1	7.9
Project and dedicated grants	1.9	1.3	1.8	2.7	1.6	1.0	1.0
Off-budget project support[2]	7.5	12.1	7.9	9.8	9.2	8.1	6.9
Financial account balance[2]	4.8	-0.3	1.5	2.0	2.2	2.2	2.1
Foreign direct investment (net)	0.8	0.8	1.0	1.2	1.3	1.4	1.5
Portfolio investment (net)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	1.9	-1.6	0.1	0.4	0.4	0.2	0.1
SDR allocation	1.6	0.0	0.0	0.0	0.0	0.0	0.0
Disbursements	1.5	2.5	2.6	2.4	2.1	1.8	1.2
Budget support and other program loans	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Project support	1.5	2.5	2.6	2.4	2.1	1.8	1.2
Other medium-term loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	-1.2	-4.1	-2.5	-2.1	-1.7	-1.5	-1.1
Other inflows	2.0	0.5	0.4	0.4	0.5	0.5	0.5
Errors and omissions	-0.9	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-1.3	-1.7	-2.4	0.2	-0.1	0.0	0.5
Financing	1.3	1.7	2.4	-0.2	0.1	0.0	-0.5
Gross reserves (- increase)	1.3	-0.8	-2.2	-2.5	-1.4	-1.2	-0.5
IMF (net)	0.0	-0.3	-0.3	-0.3	-0.4	-0.6	-0.5
Purchases/drawings	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases/repayments	0.2	0.3	0.3	0.3	0.4	0.6	0.5
Exceptional financing (CCRT)	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	2.8	4.9	2.6	1.9	1.8	0.5
RCF (prospective)		0.7					
Unidentified financing[3]	0.0	2.1	4.9	2.6	1.9	1.8	0.5
Memorandum items:							
Gross official reserves[4]	3.6	1.5	3.9	6.3	7.5	8.5	8.5
Months of imports[5]	1.6	0.6	1.5	2.5	3.1	3.6	3.7
Net international reserves[6]	-10.9	-5.0	-2.9	0.0	1.7	3.8	4.9
Current account balance (percent of GDP)	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Excluding official transfers	-14.6	-14.8	-13.6	-14.3	-13.1	-11.2	-9.6
Excluding project related imports	-12.4	-12.3	-10.8	-11.0	-10.7	-9.4	-8.1
Excluding official transfers and project related imports	-12.4	-12.3	-10.8	-11.0	-10.7	-9.4	-8.1
Import price index (2005 = 100)	151.6	181.8	177.6	177.1	168.8	163.4	160.0
Import volume (percent change)	-11.1	-16.4	-3.9	4.0	2.5	2.3	2.9
REER (percent change)	…	…	…	…	…	…	…
Overall balance (percent of GDP)	0.0	-1.7	-2.4	0.2	-0.1	0.0	0.5
Terms of trade (percent change)	-19.0	-14.9	-0.5	-1.3	3.9	3.1	2.0
Nominal GDP (millions of U.S. dollars)	12,004.4	11,781.1	10,619.4	10,809.2	11,116.4	11,554.2	12,182.4

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

[1]The IMF has adopted the Malawi National Statistics Office (NSO)'s capital and financial account data following adoption of the NSO's current account data in 2019. Previously, the IMF's reported series was based on staff estimates. Consequently, the IMF's reported capital account balance increased from 3.8 percent of GDP to 11.7 percent of GDP in 2018 while financial account balance including net errors and omission decreased from 16.5 percent of GDP to 8.6 percent of GDP.

[2]Includes estimate for project grants not channeled through the budget.

[3] The remaining financing gap would be filled by prospective concessional support and exceptional financing.

[4]Gross official reserves figures include encumbered deposits in 2021; all figures from 2022 onwards do not include encumbered deposits. Readily available gross official reserves for 2021 were US$71.7 in 2021.

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

[6] 2021 NIR is calculated as gross official reserves minus a sum of Use of Fund Credit, repayments projection of medium term debt by remaining maturity, and short-term swap outstanding. From 2022 and onward, they are calculated as defined in TMU.

Table 5. Malawi: Selected Banking Soundness Indicators, 2019–22
(Percent of GDP)

Key ratios	Dec-19	Dec-20	Dec-21	2022	
				Q1	Q2
Capital Adequacy					
1. Regulatory Tier 1 capital to risk weighted assets	17.0	17.4	17.2	18.9	18.3
2. Total regulatory capital to risk weighted assets	21.0	20.8	20.7	22.3	21.5
3. Total capital to total assets[1]	16.4	13.1	14.3	13.6	12.3
Asset composition and quality					
1. Non-performing loans to gross loans and advances	6.3	6.3	4.5	4.9	6.1
2. Provisions to non-performing loans	38.6	32.9	32.5	40.7	34.7
3. Total loans and advances to total assets	33.2	31.2	29.2	28.8	30.8
4. Foreign currency loans to total loans and advances	20.9	14.7	11.3	10.0	13.3
Earnings and profitability					
1. Return on assets (ROA)	2.7	3.0	3.4	3.9	3.5
2. Return on equity (ROE)	20.5	22.8	26.0	31.8	28.2
3. Non-interest expenses to gross income	51.8	49.0	43.7	40.9	41.7
4. Interest margin to gross income	59.6	65.6	49.7	47.8	49.3
5. Non-interest income to revenue	33.6	34.4	31.6	32.6	32.2
6. Net interest income to assets	8.4	8.0	7.9	2.3	4.4
7. Personnel expenses to non-interest expenses	43.0	€ 42.50	43.4	44.7	42.1
Liquidity					
1. Liquid assets to deposits and short-term liabilities	58.9	57.5	52.5	46.8	49.0
2. Total loans to total deposits	54.2	50.0	47.9	44.7	47.0
3. Liquid Assets to total assets	39.8	39.6	37.3	33.6	35.8
4. Foreign exchange liabilities to total liabilities	15.8	16.1	14.2	13.7	16.0

Source: Reserve Bank of Malawi.

[1]In the total capital to total assets series, total capital refers to regulatory capital.

Table 6. Malawi: External Financing Requirement and Source, 2022–27

(Millions of U.S. Dollars; Unless Otherwise Indicated)

	2022	2023	2024	2025	2026	2027
Total requirement	-2,321	-1,945	-2,043	-1,798	-1,615	-1,360
Current account, excluding official transfers	-1,739	-1,446	-1,548	-1,455	-1,294	-1,166
Debt amortization	-482	-262	-222	-190	-177	-134
Gross reserves accumulation (- increase)	-100	-237	-273	-153	-144	-60
Total sources	1,988	1,422	1,760	1,584	1,404	1,296
Expected disbursements (official)	1,867	1,301	1,620	1,435	1,251	1,111
Grants	1,577	1,030	1,357	1,203	1,047	966
Medium- and long-term loans	291	271	263	232	203	145
Private sector (net)	152	155	175	198	222	244
IMF (net)	-31	-34	-35	-49	-69	-59
Drawings	0	0	0	0	0	0
Repayments	31	34	35	49	69	59
Financing gap	332	523	283	214	211	64
Gross official reserves	172	409	682	835	980	1,039
Months of imports	0.6	1.5	2.5	3.1	3.6	3.7

Source: IMF staff estimates.

Table 7. Malawi: Indicators of Capacity to Repay the Fund, 2022–34[1]

(In Percent; Unless Otherwise Indicated)

	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035
Fund Obligations based on Existing Drawings:														
(SDR millions)														
Principal	21.9	22.4	23.1	33.5	47.8	40.5	37.4	34.1	21.1	0.0	0.0	0.0	0.0	0.0
Charges and interest	0.91	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65
Fund Obligations based on Prospective Drawings:														
(SDR millions)														
Principal	0	0	0	0	0	0	14	14	14	14	14	0	0	0
Charges and interest	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Obligations based on Existing and Prospective Drawings:														
SDR millions	22.82	27.02	27.76	38.11	52.49	45.12	55.94	52.59	39.64	18.53	18.53	4.65	4.65	4.65
US$ Millions	30.73	35.92	37.14	51.28	71.07	61.44	76.17	71.61	53.98	25.23	25.23	6.33	6.33	6.33
Percent of exports of goods and services	2.37	2.53	2.51	3.32	4.34	3.43	4.01	3.56	2.57	1.07	1.03	0.25	0.24	0.23
Percent of debt service	4.27	9.46	11.08	16.43	21.02	28.08	39.45	32.23	25.99	14.30	13.69	3.85	3.82	3.68
Percent of quota	16.44	19.47	20.00	27.46	37.82	32.51	40.30	37.89	28.56	13.35	13.35	3.35	3.35	3.35
Percent of gross official reserves	17.89	8.78	5.45	6.14	7.25	5.91	6.63	5.91	4.27	1.74	1.60	0.37	0.35	0.33
Percent of GDP	0.26	0.34	0.34	0.46	0.62	0.50	0.59	0.53	0.38	0.17	0.16	0.04	0.04	0.03
Projected Level of Credit Outstanding based on Existing and Prospective Drawings:														
SDR millions	329.2	306.9	283.7	250.3	202.5	162.0	110.7	62.8	27.8	13.9	0.0	0.0	0.0	0.0
US$ Millions	436.0	409.1	380.6	337.7	274.8	221.1	151.1	85.7	37.9	18.9	0.0	0.0	0.0	0.0
Percent of exports of goods and services	33.7	28.8	25.8	21.9	16.8	12.3	7.9	4.3	1.8	0.8	0.0	0.0	0.0	0.0
Percent of debt service	60.6	107.8	113.5	108.2	81.3	101.0	78.3	38.6	18.2	10.7	0.0	0.0	0.0	0.0
Percent of quota	237.2	221.1	204.4	180.3	145.9	116.7	79.7	45.2	20.0	10.0	0.0	0.0	0.0	0.0
Percent of gross official reserves	253.9	100.0	55.8	40.4	28.1	21.3	13.1	7.1	3.0	1.3	0.0	0.0	0.0	0.0
Percent of GDP	3.7	3.9	3.5	3.0	2.4	1.8	1.2	0.6	0.3	0.1	0.0	0.0	0.0	0.0
Net Use of Fund Credit	47.5	-22.4	-23.1	-33.5	-47.8	-40.5	-51.3	-47.9	-35.0	-13.9	-13.9	0.0	0.0	0.0
(SDR milions)														
Disbursement and purchases	69.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayment and repurchases	21.9	22.4	23.1	33.5	47.8	40.5	51.3	47.9	35.0	13.9	13.9	0.0	0.0	0.0
Memorandum items:														
Exports of goods and services (millions of U.S. dollars)	1,294	1,421	1,477	1,544	1,638	1,792	1,901	2,014	2,103	2,347	2,441	2,539	2,629	2,724
Debt service (millions of U.S. dollars)	719.2	379.5	335.2	312.1	338.1	218.8	193.1	222.2	207.7	176.4	184.3	164.6	165.7	172.1
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)	172	409	682	835	980	1,039	1,149	1,212	1,264	1,447	1,574	1,710	1,831	1,933
GDP (millions of U.S. dollars)	11,781	10,619	10,809	11,116	11,554	12,182	12,866	13,600	14,387	15,202	16,096	17,049	18,049	19,114

Source: IMF staff projections.

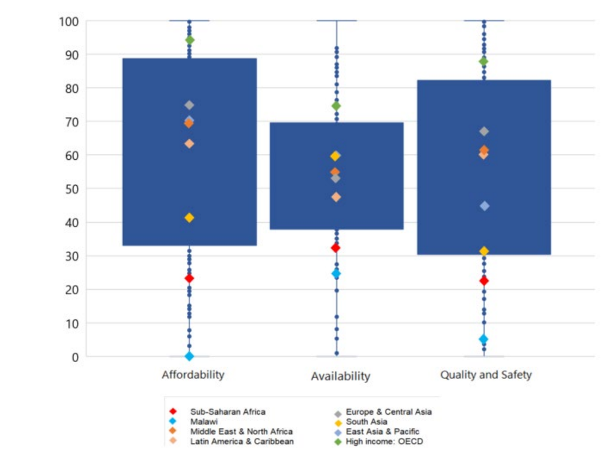
[1]Financing support from the IMF CCRT is recorded as a grant for debt relief.

Annex I. Food Insecurity in Malawi

Malawi's exposure to recurring cyclones and spillovers from war in Ukraine have further exacerbated pre-existing food insecurity risks. The authorities have adopted various measures in the recently passed FY2022/23 to contain the cost of living and adopted other humanitarian relief measures in response to the Tropical Storm Ana with support from Development Partners (DPs).

1. **Malawi stands to be among the countries at most risk of food insecurity ranked at the bottom quartile of the food security index**. Food insecurity is a serious challenge facing SSA, and particularly in Malawi. Using the Global Food Security Index (GFSI) (2021), Malawi is ranked at the bottom quartile across three of the sub-components of the GFSI (Text Figure A.1). Malawi is particularly vulnerable to: (i) food *affordability* given exposure to food price shocks—due to natural disasters shocks and exchange rate passthrough, especially fuel and fertilizer prices, (ii) food *quality and safety* which measures nutritional quality of average diets; and (iii) food *availability* which assesses the sufficiency of national food supply.[1]

Text Figure A.1. Food Insecurity in SSA and Malawi (Global Food Security Index)



Source: https://foodsecurityindex.eiu.com/Home/Methodology. Please note that the higher the ranking in the index, the more food secure a country is based on the GFSI index.

2. **Malawi's exposure to recurring cyclones and spillovers from war in Ukraine have further exacerbated pre-existing food insecurity risks through various channels**. In the first quarter of 2022, Malawi was hit by tropical storm Ana and tropical cyclone Gombe. The former resulted in flash floods, setting the highest recorded rainfall levels since the 1960s in Southern region and resulted in crop losses of 94,000 hectares (e.g., maize, sorghum, millet, rice). Vulnerability to natural disasters has aggravated food insecurity by further depressing food production, and other exported agricultural products (tobacco) which provided sources of foreign exchange to purchase other necessary food imports. In this context and given that Malawi is a net food importer, together with spillovers from war in Ukraine resulting in increasing food and fertilizer imports prices and supply chain disruptions, Malawi's food availability is at risk. Put together, inflationary pressures

[1] The Economist's Global Food Security Index (GFSI) assesses countries' food security outlook. It includes 28 SSA countries and measures performance across four pillars of the food security metric: availability, affordability, quality and safety, and natural resources and resilience. We focus on the first three pillars, which are defined as follows: (i) **availability** measures the sufficiency of the national food supply, the risk of supply disruption, national capacity to disseminate food and research efforts to expand agricultural output; (ii) **affordability** measures the ability of consumers to purchase food, their vulnerability to price shocks and the presence of shock-mitigation programs and policies, and (iii) **quality and safety** measure the variety and nutritional quality of average diets, as well as the safety of food.

reached double digit, are eroding the purchasing power of the poor, thus further increasing the risk of food affordability (Figure 1). For example, prices of bread and flour have spiked by 50 percent and 25 percent, respectively; and prices of cooking oil and margarine have increased by 55 percent and 40 percent, respectively. Furthermore, fuel prices are rapidly increasing, as the authorities have been actively increasing domestic energy prices, including diesel, petrol and kerosene by 31, 20 and 14, respectively.

3. The government has adopted various measures in the recently passed FY2022/23 to contain the cost of living and other social protection measures in response to cyclones with the support of Development Partners (DPs). Measures adopted in FY22/23 budget include the removal of: (i) VAT on cooking oil and drinking water; (ii) middlemen in the fertilizer procurement; and (iii) solar panel import duty. In addition, development partners are stepping in through vertical and horizontal expansion of social protection programs to support the most vulnerable; through food assistance programs, top-up to existing Social Cash Transfer Programme (SCTP) or an in-kind contribution (maize) with a cash top-up, and expanding of the distribution of the SCTP to other areas. [2]

[2] World Food Program, March 2022. *Food Security Brief*.

Annex II. Risk Assessment Matrix[1]

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Global Risks			
Intensifying spillovers from Russia's war in Ukraine	High	High Further sanctions resulting from the war and related uncertainties exacerbate trade and financial disruptions and commodity price volatility, with Europe, LICs, and commodity-importing EMs among the worst hit.	Strengthen intra-regional trade among sub-Saharan African countries to overcome supply chain disruptions.
Commodity price shocks	High	High A combination of continuing supply disruptions (e.g., due to conflicts and export restrictions) and negative demand shocks causes recurrent commodity price volatility and social and economic instability.	Tighten monetary policy, increase exchange rate flexibility, strengthen FX reserve buffer, apply the automatic fuel price adjustment mechanism and replenish the fuel price stabilization to ensure adequate energy supplies and contain fiscal cost/contingent liabilities.
Systemic social unrest	High	Low Rising inflation, declining incomes, and worsening inequality amplify social unrest and political instability, causing capital outflows from EMDEs, slowing economic growth, and giving rise to economically damaging populist policies (e.g., preserving fossil fuel subsidies).	Encourage the authorities and development partners to increase social priority spending to build the resiliency of vulnerable populations. Undertake promised reforms in a transparent and equitable manner. Strengthen governance measures.
Local Covid-19 outbreaks	Medium	Medium Outbreaks in slow-to-vaccinate countries or emergence of more contagious vaccine-resistant variants force new lockdowns or inhibit commerce. This results in extended supply chain disruptions, slower growth, capital outflows, and debt distress in some EMDEs.	A faster containment of the pandemic following an effective rollout of vaccines domestically to build health system capacity.
De-anchoring of inflation expectations and stagflation	Medium	Medium Supply shocks to food and energy prices sharply increase headline inflation and pass through to core inflation, de-anchoring inflation expectations and triggering a wage-price spiral in tight labor markets. Central banks tighten monetary policy more than	Upfront action to address debt sustainability and avoiding external non-concessional borrowing. Resorting to debt management strategy which relies on grants and highly concessional loans.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path. The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. The conjunctural shocks and scenario highlight risks that may materialize over a shorter horizon (between 12 to 18 months) given the current baseline. Structural risks are those that are likely to remain salient over a longer horizon.

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
De-anchoring of inflation expectations and stagflation	Medium	envisaged leading to weaker global demand, currency depreciations in EMDEs, and sovereign defaults. Together, this could lead to the onset of stagflation.	
		Regional and Domestic Risks	
Delay in debt work out	High	**High** Further delays in debt workout can reduce access to trade credit, forex swaps, and other short-term loans, worsen foreign exchange shortages and result in difficulties in importing key commodities (fuel, medicine and food) and servicing debt; which would in turn exacerbate dire macroeconomic conditions, poverty, and food insecurity.	Continue the implementation of the debt strategy in collaboration with the debt advisor and take decisive policy action that is needed to restore debt sustainability and close financing gap.
Governance weaknesses	High	**High** Overly ambitious capital investment beyond the country's absorptive capacity and weak institutions can result in a misuse of public resources, resulting in a rise in debt with little impact on growth. Conflicting signals on policy intentions can also adversely affect market participants' confidence.	Strengthen institutions to address weaknesses in governance, roll out of IFMIS, supported by the authorities' credible reforms. Further strengthen public investment management (PIM), including through project readiness considerations.
Delayed PFM reforms and lack of expenditure control	Medium	**High** Uneven progress of PFM reform and deficient expenditure control undermine confidence in budgetary processes and efforts to effectively and transparently manage expenditure. Re-emergence of arrears resulting from delays in PFM reforms will add to debt distress.	Accelerate implementation of PFM reform programs, strengthen corruption control, and communicate regularly and transparently
Fiscal dominance resulting in deficient conduct of monetary policy	Medium	**High** Inability to keep reserve money growth in line with nominal GDP growth can result in pressure on the exchange rate, the RBM's foreign exchange reserves, and inflation. Conflicting signals on policy intentions can also adversely affect market participants' confidence.	Further strengthen RBM independence. Continue adopting clear and effective monetary operational framework.
Natural disasters related to climate change	Medium	**High** More frequent natural disasters deal severe damage to infrastructure (especially in smaller vulnerable economies) and amplify supply chain disruptions and inflationary pressures, causing water and food shortages and reducing medium-term growth.	Build economic resilience, through human capital investment, and addressing deforestation.

Annex III. External Sector Assessment

Overall Assessment: In 2021, Malawi's external position was substantially weaker than the level implied by fundamentals and desirable policies. The current account (CA) deficit widened in 2021, reflecting a sharp increase in oil and commodity import prices while export recovery was marginal. The large CA deficit has been financed by very expensive external non-concessional loans and swaps, and its high external debt level raises debt sustainability concerns and large debt-service burden jeopardizes the already low gross reserves level. The SDR allocation in 2021 was used for repayment obligations and did not help build reserves or finance productive investment needs.

Potential Policy Responses: Addressing Malawi's external sector imbalances in the near term requires significant efforts to develop a diversified and competitive export sector. Aligning the official exchange rate to market rate as well as developing the exchange rate market is crucial. In the medium term, the authorities' strong commitment to a coherent package of policies only can restore confidence for Malawi and lead to non-debt-creating grants and FDIs recovery. These policies include fiscal consolidation, monetary tightening, FX market development, financial supervision strengthening, improving governance issues and reducing corruption. Further improvement in data compilation and reporting is also essential.

Current Account

Background. The 2021 CA deficit further widened to 14.6 percent from 13.6 percent in 2020 that saw a significantly large increase in value and volume of imports. CA deficit in 2020 had to do with an increase in the COVID-19 pandemic related imports. Exports of goods in 2021 were expected to increase marginally, reflecting a minor recovery in tobacco exports towards December, but not to the level before the pandemic. Goods import in 2021 increased further. Fuel (petroleum products, paraffin, diesel, coal) and fertilizers are the main goods of strategic imports, and increasing fuel and fertilizer imports reflects the government's energy and agricultural strategy. The sharp increase in oil and other commodity prices after the war directly affected the import value. The CA deficit in 2022 is expected to increase further to 14.8 percent, reflecting the continued increases in oil and commodity import prices as well as a large one-off exchange rate devaluation, while benefits in exports were relatively small in goods trade. Very large interest payments for non-concessional external borrowing weigh on top of large trade deficits.

Assessment. The EBA-Lite 3.0 CA model suggests that the external sector position is substantially weaker than the level implied by medium-term fundamentals and desirable policies. Based on the CA model, the cyclically adjusted CA deficit after COVID-19 adjustor (0.1) and natural disaster (-0.2) adjustors stood at 14.8 percent of GDP in 2021. This points to a large gap of -10.2 percent of GDP compared to a cyclically adjusted CA norm of -4.6 percent of GDP. Of which, the total policy gap is 2.0 percent and the sizable negative residual potentially captures structural impediments, which are addressed in the section of Tackling Governance challenges in the main text.

Malawi: Model Estimates for 2021 (In percent of GDP)

	CA model 1/	REER model 1/
	(in percent of GDP)	
CA-Actual	**-14.6**	
Cyclical contributions (from model) (-)	0.2	
COVID-19 adjustor (-) 2/	0.1	
Additional temporary/statistical factors (-)	0.0	
Natural disasters and conflicts (-)	-0.2	
Adjusted CA	**-14.8**	
CA Norm (from model) 3/	**-4.6**	
Adjustments to the norm (-)	0.0	
Adjusted CA Norm	**-4.6**	
CA Gap	**-10.2**	**0.6**
o/w Relative policy gap	2.0	
Elasticity	-0.28	
REER Gap (in percent)	**36.9**	**-2.3**

1/ Based on the EBA-lite 3.0 methodology

2/ Additional cyclical adjustment to account for the temporary impact of the tourism (0.1 percent of GDP) and remittances (0 percent of GDP).

3/ Cyclically adjusted, including multilateral consistency adjustments.

Real Exchange Rate

Background. The real effective exchange rate (REER) in 2021 has shown a slight depreciation compared to a strong appreciation in 2020. REER appreciated about 24.8 percent since 2016, partially due to limited movement in the nominal exchange rate. The spread between the official rate and market (forex bureau) rate continues widening through April 2022. The Reserve Bank of Malawi took a decisive action to devalue Kwacha in May by 25 percent to correct a large overvaluation for the first time since the devaluation of comparable size in 2012. The spread narrowed after the devaluation, however it started widening sharply from September reflecting the continued inflation pressure and FX shortage.

Assessment. The EBA-Lite CA model suggests that the REER is substantially overvalued relative to the level implied by fundamentals and desirable policy settings. Staff assesses the 2021 REER to be overvalued by about 37 percent based on the CA model. Given a continued widening of the spread in recent months after the devaluation and depleting gross reserves, the exchange rate needs to play a key role as shock absorber. Development of the exchange rate market and more flexible exchange rate system are a key to narrow the current account deficit.

Capital and Financial Accounts: Flows and Policy Measures

Background. Malawi receives project loans and off-budget support at about 8 percent of GDP in the past years, although with a caveat of data weakness. They are mostly project loans provided by donors to finance their projects. Foreign direct investment is very weak (estimated to be less than 1 percent of GDP), and the financial account balance consists of mostly non-official sector flows. The SDR allocation contributed to about one third of the financial account balance in 2021. The RBM reintroduced a surrender requirement (assessed as a CFM) to exporters in August 2021 and tightened the measure in March 2022.

Capital and Financial Accounts: Flows and Policy Measures
Assessment. Malawi faces significant FX drains related to a large external debt and non-concessional external borrowing. The gross reserves level is extremely low, at 0.3 months of import coverage at end-2021 and is estimated to have reduced further by end-April. The use of the surrender requirement would be justified given the imminent crisis situation: However the authorities have to continue to pursue warranted macroeconomic, financial and exchange rate policies to restore domestic and external sector positions. Data reporting to the Fund also needs to be improved further.
FX Intervention and Reserves Level
Background. Gross reserves continued to decline throughout 2021, and it went down to below $80 million at the end of 2021. This is equivalent to only 0.3 months of imports of next year. SDR allocations, about USD190 million, of August in 2021 was converted to U.S. dollars immediately and used for repayment obligations within months. To help increase foreign currency liquidity in the market, the Reserve Bank of Malawi reintroduced a 30 percent of surrender requirement for proceeds from exports in August 2021, which has been further tightened in March 2022 so that all exporters have to surrender. Staff sees that the measure has not been successful to replenish foreign currency in the market. The main source of declining gross reserves come from a large principal and interest repayments obligations to non-concessional external loans and rolling over ST swaps. **Assessment.** The reserve adequacy model for credit constrained economies suggests that the level of foreign reserves considered adequate to withstand external shocks for Malawi is around 3.9 months of imports. Given a very low level of gross reserves currently and unsustainably high debt levels, staff's view is that it would take time to increase gross reserves to 3.9 months of imports. Still, staff recommends accumulating gross reserves to about 3.7 months of imports within a few years would be necessary, considering several country specific factors such as large import dependency and vulnerability to climate events.

Appendix I. Letter of Intent

November 11, 2022

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

Dear Madame Kristalina Georgieva,

In 2020, following the assumption of office by His Excellency the President Dr. Lazarus McCarthy Chakwera, we requested for a new Fund-supported Extended Credit Facility (ECF) arrangement and cancelled the existing ECF approved in April 2018, primarily going off-track at the time, to align with our developmental agenda. Since then, we have directed our efforts towards addressing the legacy of unsustainable policies and stumbling blocks that have delayed the conclusion of negotiations for the successor ECF, including unsustainable public debt and misreporting of RBM's net international reserves under the 2018 ECF.

Following a series of shocks including the impact of the Covid-19 pandemic, two cyclones in early 2022 and spillovers from the Russia-Ukraine conflict, economic growth has slowed, foreign exchange reserves have declined to very low levels and inflation has accelerated, standing at 25.9 percent as of end-September 2022. The challenging economic conditions and erosion of purchasing power are being felt particularly by the most vulnerable Malawians, many of whom are already facing a high risk of food insecurity. Addressing this situation is our top priority in line with our long-term vision to create an inclusively wealth nation under Malawi 2063.

Against the background, we are undertaking macroeconomic adjustment and structural reforms to restore macroeconomic stability and provide the foundation for an inclusive recovery. To help achieve our objectives, we are requesting for emergency financing under the Rapid Credit Facility (RCF) -- Food Shock Window, in the amount equivalent to 50 percent of Malawi's IMF quota, approximately US$88.3 million, to help address urgent balance of payments needs related to the global food crisis. We are also requesting the Staff Monitored Program with Executive Board Involvement (PMB) to support our efforts. This will allow us to continue to make progress on the comprehensive debt restructuring process we initiated to restore debt sustainability and build a track record with the PMB towards an IMF-supported economic program financed under an ECF.

A memorandum of understanding will be signed between the RBM and the Ministry of Finance to clarify their responsibilities for timely servicing of Malawi's financial obligations to the IMF.

The attached Memorandum of Economic and Financial Policies (MEFP) describes recent developments in the Malawian economy and sets out in detail the economic and financial policies we intend to implement under the PMB to restore macroeconomic stability, set the foundation for inclusive growth and improve the life of Malawians. Our policies to restore macroeconomic stability will focus on measures to enhance fiscal discipline, maintain price stability and financial soundness, rebuild external buffers, and restore debt sustainability. These reforms will be implemented alongside efforts to address longstanding governance weakness and corruption. Given our limited fiscal space, we will prioritize expenditure to ensure adequate support to the vulnerable by safeguarding Government's contribution to social safety net programs such as the Social Cash Transfer Program (SCTP), and to protect investment in infrastructure.

We are confident that through the implementation of measures and policies described in the attached MEFP, we will attain the objectives of the PMB. That said, we stand ready to take additional measures that may be needed over and above those articulated in the MEFP in consultation with IMF staff in accordance with the Fund's policy. We also assure you that we will submit all program monitoring information outlined in the attached Technical Memorandum of Understanding (TMU) on a regular and timely basis and will also share any other information that may be necessary to evaluate progress made under the PMB. We intend to make public the contents of the IMF staff report, including this letter, the attached MEFP, the TMU, the informational annex, and the debt sustainability analysis carried out by IMF and World Bank staff. As such, we authorize the IMF to publish these documents accordingly.

Yours sincerely,

/s/
Honorable Sosten Alfred Gwengwe
Minister of Finance and Economic Affairs

/s/
Dr. Wilson T. Banda
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

INTRODUCTION

1. **The Government of Malawi requested for a Fund-supported Extended Credit Facility (ECF) in early-2021, but is not in a position to implement a UCT-quality economic program.** After assuming office in June 2020, the Government canceled the existing ECF initiated in April 2018, under the previous government, and requested for a new ECF arrangement to align with the new development agenda and vision to create a self-reliant nation and upper-middle income country. However, key stumbling blocks surfaced during initial engagements with the Fund staff team on a prospective ECF. These include (i) surfacing of noncomplying disbursements ("misreporting") resulting from the provision of inaccurate information on the performance criteria on the floor of Net International Reserves (NIR) under the 2018 ECF arrangement First Review completed in November 2018 and combined Second and Third Reviews completed in November 2019 and (ii) the reclassification of Malawi's overall and external public debt from moderate risk of debt distress and sustainable to high risk of debt distress and unsustainable. Upfront actions have since been taken to address debt sustainability to ensure that fiscal space is created for the much needed social and development spending. Furthermore, we have started implementing corrective measures to enhance transparency in RBM's management and reporting of official foreign exchange reserves and realigning the exchange rate with market fundamentals.

2. **Today, Malawi is facing a dire macroeconomic situation, necessitating bold reforms and international support to avert a full-blown Balance of Payments (BoP) crisis.** The country has experienced two major additional exogenous shocks, on the back of a weak recovery from the Covid-19 pandemic, namely: (i) tropical cyclones Ana and Gombe hit Malawi in 2022 Q1, damaging crops and infrastructure, including one of the main hydropower plants whose rehabilitation is underway until end-2022, putting additional pressure on already constrained fuel imports and (ii) war in Ukraine is putting pressure on energy and food prices, increasing risks to already high food insecurity. Furthermore, pressure from unstainable public debt continues to erode fiscal space. This calls for new policies to break away from a legacy of unsustainable policies and to help restore macroeconomic stability.

3. **This Memorandum presents the economic and financial policies that the Government intends to implement under the Staff Monitoring Program with Executive Board Involvement (PMB) to build a track record for a UCT-quality arrangement within the next 12 months.** The Government's overarching objective is to restore macroeconomic stability to build the foundation for sustainable and inclusive growth as envisaged in Malawi 2063. In the near term, BoP pressure is mounting, calling for immediate government action and forging ahead with ambitious reform efforts to help improve the lives of the Malawian people. In this regard, the proposed two step approach involving emergency financing under

the RCF --Food Shock Window, combined with PMB, followed by a request for an ECF once debt restructuring assurance are in place, provides a credible path forward. We recognize that this will require a credible debt restructuring treatment, deep enough to firmly restore debt sustainability, accompanied by strong fiscal and external adjustment. Notably, execution of a revised FY2022/23 budget that is based on realistic revenue estimates will be key while aligning of external policies to economic fundamentals and maintaining an appropriate monetary stance to contain inflation will be essential. We will step up our efforts to address governance weaknesses and reduce vulnerabilities to corruption, including through enhancing transparency and accountability of public financial management (PFM), strengthening autonomy and governance of the Reserve Bank of Malawi (RBM), and strengthening of its foreign exchange reserves management.

RECENT ECONOMIC DEVELOPMENTS

4. Malawi's economic recovery remains extremely fragile. After a moderate recovery from 0.9 percent in 2020 to an estimated 2.2 percent in 2021, on the back of a good harvest. Real GDP growth is projected to decline to 0.8 percent in 2022. This reflects the effect of the two tropical storms that hit Malawi in the first quarter of 2022, delayed and early cessation of 2021/22 agricultural season rains, intermittent electricity power supply and spill-over effects of the war in Ukraine. While Malawi's direct trade exposure to Russia and Ukraine is limited, higher fuel, fertilizer and food prices are expected to continue to affect domestic consumption and investment adding to food-security concerns.

5. Fiscal policy faced challenges in FY2021/22[1]. The deficit in FY2021/22 is MWK 792 billion (9.7 percent of GDP), compared to a budgeted MWK 724 billion. On the back of the lingering impact of the Covid-19 pandemic, execution of the FY2021/22 budget faced the perennial problem of revenue underperformance, pressure on recurrent expenditure coupled with the under-execution of development expenditure.

6. Gross official reserves are low and pressure on the exchange rate is high. Foreign exchange market liquidity remains significantly tight, with insufficient supply to finance the existing FX demand. Supply has been further constrained by underperformance of exports and mounting servicing of external debt. As a result, readily available gross reserves turned to be at $71.7 million at end-2021. Spillovers from the war in Ukraine has put further strain on gross reserves, leaving the level of gross reserves low. The exchange rate depreciated by 25 percent at end-May 2022 following a policy decision to re-align the exchange rate with market fundamentals to help improve FX availability.

7. Inflationary pressure is mounting. Inflation has continued to deviate further away from the medium-term objective of 5.0 percent, since returning to the double-digit range in November 2021.

[1] FY2021/22 runs for three quarters from 2021Q3-2022Q1 because the authorities shifted the fiscal year from F2022/23 henceforth to begin on the second quarter of the calendar year.

Headline inflation has doubled from 7.6 percent at end-2020 to 25.9 percent at end-September 2022. This reflects exchange rate pass-through, lingering impact of expansionary fiscal stance in FY21/22 accompanied by accommodative monetary policy stance and increases in prices of fuel, fertilizer and imported food amid prolonged global supply disruptions.

8. **The banking sector is broadly stable, well capitalized, with sufficient liquidity and profitable but exposure to the public sector has continued to increase.** The banking sector meets the minimum regulatory requirements for capital adequacy and the liquidity ratios. However, since the Covid-19 pandemic, industry-wide non-performing loans generally remained marginally above the recommended limit of 5.0 percent, and stood at 5.7 percent in September 2022, up from 5.0 percent in September 2021.

9. **Risks to food security increased on account of climate-induced shocks and spillovers from the war in Ukraine.** Vulnerability to natural disasters has aggravated food insecurity by further depressing food production, and other exported agricultural products (tobacco) which provided sources of foreign exchange to purchase other necessary food imports. Given that Malawi is a net food importer, supply chain disruptions linked to the war in Ukraine and the resulting increase in food and fertilizer imports prices have affected Malawi severely. Consequently, the World Food Program (WFP) estimates that 3.8 million Malawians will experience acute food insecurity and in need of food assistance during upcoming lean season (October 2022-January 2023), representing more than double the number of households last year.

OUTLOOK

10. **Despite the dire macroeconomic situation, implementation of bold policy actions outlined in this MEFP is expected to lead to a favorable medium-term outturn.** We are confident that a PMB will help anchor our macroeconomic policies to address macroeconomic sustainability. In this regard, we will implement bold policies and reforms, accompanied by strategies to restore debt sustainability. Furthermore, we will advance structural reforms to support sustainable and inclusive growth and address the impact of the Covid-19 pandemic, spillovers from war in Ukraine and climate-related shocks, with a view to improve lives of the Malawian people.

11. **We are cognizant that in the short term, economic adjustment will be difficult, but this is necessary to address the current situation and set the foundation for sustainable and inclusive growth.**

- We expect that growth will recover from 0.8 percent projected in 2022 to 2.4 percent in 2023 as confidence in our policies and economic stability is restored. Specifically, we will pursue prudent fiscal policies and ensure that non-concessional external financing will be replaced by grants, other non-debt creating flows and adjustments under the proposed reform program. Medium term growth is projected to hover around 4 percent supported entrenchment of macroeconomic stability and implementation of structural reforms.

- Year-on-year inflation is expected at 26 percent at end-2022 and projected to decline thereafter towards about 6.5 percent by the end of the medium term, supported by well anchored monetary and fiscal policy stance, taking into account the anticipated movements of the currency and passthrough to inflation as the RBM builds up foreign reserves and winds down currency swap operations.

- Gross reserves are projected to recover to 3 months of imports by the end of the medium term. With external and fiscal policy adjustments, current account deficits are projected to decline over time. The reserve accumulation path assumes that the external financing gap will be filled with non-debt creating flows, either debt relief or grants.

12. Risks to the outlook are significant. While the risk of a sudden stop of existing trade credit facilities and forex swaps, if realized, could trigger an imminent BoP crisis, another COVID-19 wave and weather-related events remain relevant. In addition, the war in Ukraine could compound risks to the outlook due to supply chain disruptions and the surge in fuel, food and fertilizer prices resulting in additional financing needs and increasing risks to food insecurity.

ECONOMIC AND FINANCIAL POLICIES FOR THE PROGRAM PERIOD

13. Economic and financial policies for the program period will be anchored by the Malawi 2063. Our program objectives include, (i) restoring macroeconomic stability, (ii) enhancing fiscal discipline, (iii) maintaining price stability and financial soundness, (iv) rebuilding external buffers (v) restoring debt sustainability and closing the financing gap, and (vi) addressing weaknesses in governance. The remainder of this MEFP outlines in detail the specific policies we have adopted or intend to adopt to achieve our program goals.

A. Fiscal Policy

14. Our fiscal policy stance will aim to regain fiscal discipline and restore debt sustainability. This will be supported by measures to enhance revenue collection and manage expenditures and improve transparency and monitoring of budget execution.

15. Our revised FY2022/23 budget foresees measures to reduce the fiscal deficit to 7.1 percent of GDP, in line with the macro-framework under the PMB. The revised FY22/23 budget is anchored on realistic revenue estimates and a rationalization of expenditure, while protecting essential spending, to achieve an upfront fiscal adjustment of about 3¾ ppts of GDP in FY2022/23. This implies an envisaged reduction of the domestic primary deficit to 0.6 percent of GDP in FY2022/23 compared to 4.1 percent of GDP in FY2021/22 and a reduction in the Net Domestic Financing by 2⅓ percent of GDP to 5.5 percent of GDP in FY22/23 relative to FY21/22 (Text Table 1). In the medium-term, a primary surplus of 0 percent is needed to stabilize public debt, representing a cumulative fiscal consolidation of 4.0 percentage points (in terms of domestic primary balance) over the next four years. To achieve fiscal discipline and move towards a sustainable debt path our fiscal consolidation efforts during the remainder of FY2022/23 will focus on, (i) stepping up implementation of our domestic revenue mobilization strategy (DRMS) in a timely manner (ii) rationalizing and prioritizing expenditures, (iii) introducing and implementing sound commitment controls measures and (iv) implementing well targeted measures to support low-income households.

Text Table 1. Malawi: Fiscal Adjustment, 2022/23–2025/26
(Percent of GDP)

	2022/23	2023/24	2024/25	2025/26	Total
Domestic Revenue	**0.5**	**1.0**	**1.0**	**0.4**	**2.9**
Policy measures	0.4	0.9	0.9	0.2	2.3
Import withholding tax	0.1	-	-	-	0.1
VAT base broadening	0.2	0.5	0.5	0.1	1.2
PIT reform	0.2	0.2	0.2	-	0.6
CIT base broadening	-	0.1	0.1	0.1	0.3
Excise and Carbon Tax	-	0.1	0.1	-	0.2
Tax administration measures	0.1	0.1	0.2	0.2	0.6
Expenditure measures	(1.5)	(0.5)	(0.3)	(0.2)	(2.6)
Wage bill	(0.3)	(0.3)	(0.3)	(0.1)	(1.0)
AIP	(0.6)	(0.3)			(0.9)
General goods and services	(0.5)	(0.2)	(0.1)	(0.1)	(0.9)
Social protection		0.2			0.2

16. To align our FY2022/23 budget with the program macro-framework, we will implement the following measures.

17. The revised FY2022/23 budget (PA) has been submitted to the Cabinet on November 9, 2022. The revised budget will align spending to revenue projections so that net domestic financing is contained.

18. We will announce quarterly allotments aligned with the macro-framework and the outturns for revenue, grants and expenditure and allow Ministries Departments and Agencies (MDAs) to commit up to this amount through IFMIS. MDA payments will be limited to monthly cash releases, aligned with allotments, to demonstrate our commitment to stronger expenditure control reforms, reducing the risk of accumulating new payment arrears. The measures will also support compliance with our updated PFM Act. The introduction will be piloted in the Ministries of Finance (Treasury), Gender, Trade and Industry, Agriculture, Office of President and Cabinet, National Intelligence Service, Office of the Vice President, National Assembly, Department of Asset Declaration, with effect from November 2022 with the aim of extending the practice to all MDAs through announcement in the 2023-24 budget speech.

19. Our revenue mobilization efforts will be driven by the timely implementation of revenue measures announced in the Domestic Revenue Mobilisation Strategy (DRMS) and FY2022/23 budget statement. We launched the DRMS in December 2021 with the objective to increase revenue by 5 percent of GDP in the five years of implementation. To step up implementation, we have incorporated the DRMS in Malawi Revenue Authority's (MRA) strategic plan and formulated a DRMS Monitoring Committee comprising MoFEA, MRA, Accountant General, Immigration Department, Malawi Police Service and Registrar General in FY2022/23 and envisage to implement the following measures:

- **PAYE Brackets:** we introduced additional income tax brackets in April 2022, partly reversing the loss in revenue from previous changes in rates and brackets.

- **Advance income tax:** we rolled out full implementation of the advance income tax in May 2022 which raised additional revenue amounting to MWK 6 billion.

- **Tax stamps on beverages:** we are in the process of introducing the requirement for affixing or printing of electronic tax stamps on alcohol (spirits, whiskey, malt beer, opaque beer), energy drinks, flavored water, carbonated soft drinks and opaque non-alcoholic drinks. We expect this to be operational in the last quarter of FY2022/23.

- **Taxes for small businesses**: we are in the process of introducing the presumptive tax for small businesses whose turnover is less than MWK12.4 million. The gazetting process of the presumptive tax regulations is currently underway. Furthermore, once these regulations are in place by end November 2022, we will roll out the block management system in full to all commercial centers for the efficient management of revenue collection from small business. So far, we have commenced implementation of block management in Lilongwe, Blantyre and Mzuzu.

- **Tax Incentives**: the FY2022/23 budget announced establishment of Special Economic Zones, to help catalyze the much-needed foreign investment in Malawi. As far as tax incentives are concerned, we are reviewing the system with a view to streamline the incentives. The recommendations of the report will be incorporated in the new Taxation Act and Customs and Excise Act that are currently under review.

- **The revised budget will incorporate additional reforms** to those announced in March 2022, which include VAT base broadening, and repealing tax exemptions to the Special Economic Zones.

20. To strengthen tax administration, we are on track with the go-live launching of the Integrated Tax Administration System (ITAS), also called Msonkho online December 2022 with all modules by March, 2023.

21. To improve non-tax revenues, we will implement measures including reviewing fees and charges to ensure that they, where possible, reflect full cost recovery; automating the payment systems and business processes of the MDAs; enforcing the dividend and surplus policy and ensure that the SOEs comply with the PFM Act by opening a holding account with the RBM; and ensuring that MDAs remit non-tax revenue collection to MG1 account through their departmental receipts accounts.

22. Expenditure prioritization is more critical than ever given the need to support the vulnerable and invest in infrastructure. We will endeavor to improve efficiency of public spending and to reduce non-critical spending.

- **Continue to rationalize the Affordable Input Program**. We are implementing the first phase of reform to the fertilizer and seed subsidy program (Affordable Input Program (AIP)) by having a Consolidated Social Protection Program using the Unified Beneficiary Register to reduce duplication of access hence bringing in efficiency in beneficiary targeting. We have taken necessary measures to prevent cost overrun in the AIP from escalating fertilizer prices and kwacha depreciation including through increment to farmer contribution while capping the Government Subsidy and fast-tracking beneficiary reform. In subsequent phases of the AIP reform, we have adopted a plan to phase out the AIP in five years by reducing the number of beneficiaries by 20 percent every fiscal year. Furthermore, we have moved farmers at the lowest end of the income spectrum to social protection programs and those at the higher end of the spectrum to commercial agriculture programs, supported by development partners.

- **Rationalize the wage bill**. The Personnel Audit was carried out in 2021 which provided a number of recommendations and the Government of Malawi is committed to manage its wage bill by freezing on new hiring to the public service, except in critical areas such as health and education sector, strengthening approval processes to payroll and pension changes within the existing Human Resource Management Information System (HRMIS).

- **To safeguard social protection and to protect the vulnerable, we will establish a floor on social spending as an indicative target (IT) under the program**. This will comprise of Government contribution to health and basic and secondary education spending, as well as a number of social safety net spendings, including the social cash transfer program (SCTP) and AIP. Fiscal measures are put in place to mitigate food insecurity (Box 1).

Box 1. Malawi: Fiscal Measures to Mitigate Food Insecurity, FY2022/23

Proposed Areas	Amount Proposed (K billion)	Justification	Reporting
Social Cash Transfer	2	To help the vulnerable groups such as the elderly, children, disabled by providing them with social cash transfers. The additional resources to be used for scaling up the program under Ministry of Gender	Social Spending Tracker
Affordable Inputs Program	69.8	This will enable Government to cushion farmers from high/increased prices of fertilizers	Line item in the budget, monthly reports and social spending tracker
Maize/Other Food Stuffs Purchase-Lean season response	12.6	To procure additional maize and other food stuffs under Disaster Affairs Department for lean season response (December 2022 - March 2023)	Social Spending Tracker
Livestock Development Initiatives	0.5	To target livestock farms such as Dwambadzi for goat, cattle and other livestock in the Ministry of Agriculture	Social Spending Tracker
Maize Seed subsidy	4.4	To provide good quality seeds to vulnerable population in order to enhance maize production.	Social Spending Tracker
Agriculture Sector	8.6	To support Ministry of Agriculture in Agricultural extension services and land conversation agricultural measures	Line item in the budget through monthly budget execution reports
Sub-Total	**97.9**		

23. **We plan to step up measures to enhance the oversight of state-owned enterprises (SOEs).** Weak oversight and financial reporting are a challenge to adequate monitoring and management of risks to the budget and public debt from the SOEs. In this regard, we will keep close track of government guaranteed debt of SOEs. We will also undertake detailed reporting for high-risk SOEs, including Blantyre Water Board, ESCOM, ADMARC, NOCMA, EGENCO. On a quarterly basis, we will monitor the management accounts of the relevant SOEs. In compliance with the new PFM Act, we will prepare an annual consolidated report of all SOEs.

24. **Implementation of the new IFMIS, institutionalizing reporting and controls are key for execution of the budget and commitment control.** We will exploit the new IFMIS, which was rolled out to all MDAs from July 2021, to build upon recent and enable future Public Finance Management (PFM) reforms, including the interim Electronic Funds Transfer (EFT) for government payments, to improve our budget preparation, cash management, commitment control, banking arrangements, accountability, and payment efficiency. The success of the fiscal adjustment program relies heavily on comprehensive and timely reporting, and sound commitment controls. Our measures are as follows:

- **Arrears**: We have completed the verification of arrears of the national budget entities from 1st July 2017 to 30th June, 2020. We are in discussion with the Auditor General on the stock of the unverified arrears to agree on how these will be treated and in addition, on the stock of arrears that have been submitted from the MDAs up to March, 2022. We are committed to settle the arrears within the limits of the fiscal framework and available resources and to avoid further accumulation of arrears through implementation of quarterly allotment and contract management.

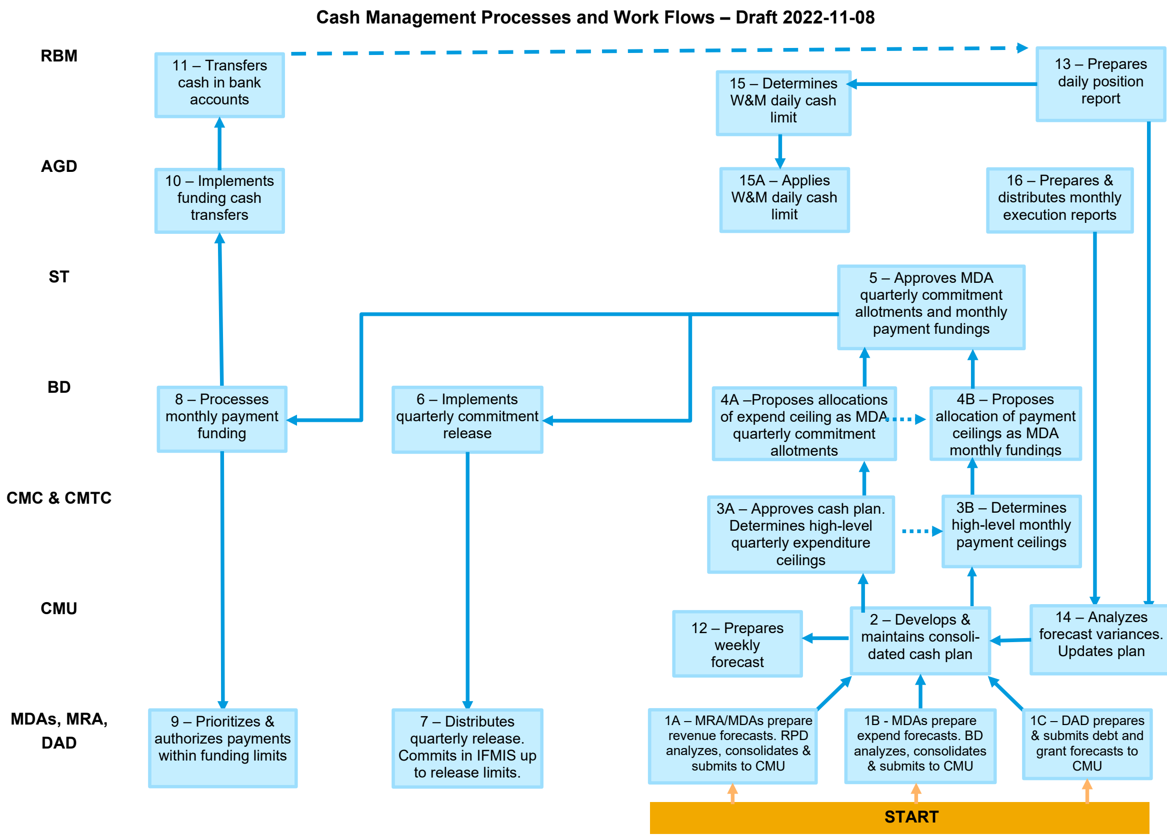
- **Contract Management module of IFMIS-** starting mid November 2022**,** we will implement quarterly commitment limits (backed by monthly payment fundings) and roll out the IFMIS contract management module starting with two MDAs, including the Ministries of Health and Transport. These will be our cornerstones for firm commitment control and management of multi-annual contracts. Implementation will include i) capturing all existing contracts/commitments in IFMIS, ii) issuance of quarterly spending limits and monthly payment funding, iii) requiring all financial transactions to be entered through IFMIS at the commitment (contract signing/purchase order issuance stage). We envisage to run the pilot phase until March 2023 and to roll out the functionalities in full to all MDAs from 1st April 2023.

- **Expand the coverage of transactions recorded in IFMIS** to include items that are currently transacted outside of IFMIS including revenue, and from 1st April, 2023 the budgets and actuals of all debt issuance receipts and servicing payments, transfers to local councils, and advances to embassies. We will review the bank account structure used for public debt to ensure compliance with the new PFM Act and facilitate the recording of transactions.

- **Cash management and debt issuance**: to strengthen our cash management and debt issuance, we will strictly adhere to the budget execution process stipulated in the flow chart, Text Figure 1.

Text Figure 1. Malawi: Cash Management Processes and Work Flows, 2022

To enhance commitment control and cash management, the Ministry of Finance reviewed the work flows to ensure unplanned spending and unplanned borrowing will be eliminated going forward.



RBM: Reserve Bank of Malawi; AGD: Accountant General's Department; ST: Secretary to Treasury; BD: Budget Director; CMC: Cash Management Committee; CMTC: Cash Management Technical Committee; CMU: Cash Management Unit; MDA: Ministries, Departments, and Agencies; DAD: Debt and Aid Department.

- **Electronic Funds Transfer (EFT)**: We will move to the exclusive use of EFT for government payments across all MDAs in FY2023/24 or as soon as the planned RBM upgrade of its core banking system is completed. The GOM will cease to act as a participating bank in the interbank payment system.

- **Consolidated fiscal reports**: IFMIS coverage has expanded to include all national government cash inflows and outflows, including all MG1 and public debt issuance and servicing transactions from July 2021. Auto-reconciliation of government's bank statements has started, enabling us to commence compiling IFMIS-generated monthly fiscal reports. So far, we have compiled the domestic budget execution data for April through to September 2022. Going forward, we will continue to improve the in-year comprehensive monthly fiscal reports with the ultimate goal to publish the quarterly audited IFMIS-generated comprehensive fiscal reports starting in FY2023/24. These reports will be backed by reconciled bank statements submitted within three weeks from the end of each month to the Cash Management Committee, MDAs and IMF staff.

- **PFM Act:** We passed the new PFM Act in March 2022 to align the legal framework with ongoing PFM reforms. We are drafting the regulations and Treasury instructions to support the implementation of the new Act. The regulations and instructions will be finalized by March 2023 and June 2023 respectively.

B. Maintaining Price Stability and Financial Soundness

25. Monetary policy will focus on containing inflationary pressures. To anchor inflation expectations, we stand ready to tighten monetary policy as needed. In this respect, our monetary program will remain anchored on containing reserve money growth. This will call for measures to contain money growth against excess liquidity created through sizeable foreign exchange purchases from the market that we envisage to build up FX reserves. Our measure will include:

- Tightening the monetary policy stance by raising the monetary policy rate to tame inflation with the objective of attaining positive real interest rates.

- Draining excess liquidity through various instruments including raising required reserves, RBM's sales of government securities, and Open Market Operations (OMO) should be considered for sterilization purposes.

26. Financial sector stability will continue to be safeguarded. The further increase in the exposure of the banking sector to the public sector and hikes in the interest rates may pose potential risks to the soundness of the financial sector. We will therefore remain vigilant to these risks and continue to strengthen financial sector oversight. To promote financial stability, we will:

- Monitor closely the banking system's exposure to the government through securities and swap operations.

- Reassess loan and collateral quality needs of commercial banks.

C. Rebuilding External Buffers

27. Our external policies will support rebuilding of FX buffers, in a sustainable manner, and maintaining a market determined exchange rate. To achieve this objective,

- We took action to realign the exchange rate with the market clearing rate through a 25 percent one-off exchange rate adjustment at end-May 2022. The realignment narrowed the exchange spread with the forex bureau rate from over 28 percent at end-April 2022 to 2 percent at end-May 2022, but the spread has since widened due to continuing speculation and forex shortages. Subsequently, we will aim to maintain the value of the kwacha market driven.

- We will implement the agreed path towards accumulating foreign exchange reserves with the view of rebuilding the country's reserve assets. We will slow down direct foreign exchange sales to the market in support of imports. In any event, the RBM will become a net purchaser of foreign exchange. Concurrently, we will gradually wind down the existing swap open position as guided by the foreign exchange accumulation path. We believe that pursuing this reserve accumulation strategy will help achieve a 3-months import cover by the end of the medium term. Moreover, we will also monitor reserve liabilities so that the RBM's net international reserves (NIR) will reach an adequate level as quickly as possible.

- We will facilitate the price formation processes in the market by arranging small pilot foreign exchange auctions. This will help determine the market-clearing exchange rate and facilitate development of the interbank FX market. (**SB**).

We will ensure that coordination between the government and the RBM will help achieve the external sector policy goals. In particular, the government will review its policies and their implications on foreign exchange to help contain the current account deficit.

D. Restoring Debt Sustainability and Closing the Financing Gap

28. Malawi's overall and external public debt is assessed to be in debt distress and both external and public debt are assessed as unsustainable under current policies. This mainly reflects legacy debts that we inherited, driven by unsustainable fiscal and external policies. Restoring public debt sustainability is our top priority to support macroeconomic stability and to lay the foundation for sustainable and inclusive growth.

29. We have developed a debt restructuring strategy which will serve as our cornerstone for restoring debt sustainability. We have engaged a debt advisor to support a credible process for restructuring based on adequate creditor engagement to ensure the approach taken delivers the necessary contributions in a sustainable manner. All our creditors were approached early in the process and we are committed to achieve a debt treatment that puts our debt back on a sustainable path consistent with the macroeconomic parameters of the program

30. Our debt strategy is designed to achieve debt sustainability and to close the financing gaps. The strategy relies on the following pillars to overcome current external debt challenges, including solvency and liquidity concerns:

- Bringing external public debt back to a moderate risk of debt distress in the medium term through a combination of policy adjustment and the necessary debt treatment. The debt strategy targets all external DSA solvency and liquidity ratios to cross their respective thresholds under the baseline in the next five years. This means (i) the baseline of the present value of debt-to-GDP ratio to reach below 30%, (ii) the present value of debt-to-exports ratio below 140%, (iii) the external debt service-to-exports ratio below 10%, and (iv) the external debt-to-revenue ratio below 14% in the medium-term

- Mobilization of non-debt creating flows to ensure the external and fiscal financing gaps are closed over the program period, including through the debt treatment and the mobilization of external grant support from development partners

31. We are committed to pursue public finances consistent with debt sustainability and implement measures to strengthen debt management, monitoring and recording and reporting. To ensure our debt remains on a sustainable path, we will implement measures articulated below.

- To enhance public debt management, we will update our medium-term debt strategy (MTDS) to take into account on-budget externally and domestically financed projects either contracted or expected as reflected in the macro-fiscal framework. The MTDS will also reflect the ceiling on new non-concessional external debt contracted or guaranteed [performance criterion] that will apply to Malawi as required by the Fund's Debt Limit Policy.

- We will adopt best practices in terms of data reporting and transparency, as well as fulfil our reporting duty to the Fund during the Staff's program review or upon request. In particular, we reiterate our commitment to continue to integrate public debt data into IFMIS. We will also further enhance transparency around Malawi's debt data by publishing regular reports on outstanding debt figures on our official websites. Finally, we are dedicated to building capacity around debt management and financing and to seeking technical assistance from the IMF and other partners.

- To further support debt sustainability, we will undertake a strong fiscal adjustment while limiting the impact on economic growth and protecting vulnerable populations through our revenue mobilization efforts

- Finally, to rebuild our external buffers over the medium term and improve liquidity, we will pursue our export diversification strategy. Our strategy aims to reduce Malawi's dependance on agricultural exports, thereby building resilience to climate shocks while supporting economic growth over the medium term.

E. Tackling Governance Challenges Structural Reforms

32. Strengthening RBM's autonomy, governance arrangements, and reserve management are cornerstones of our program. In this regard, we

- Have established RBM's gross reserve management strategy in accordance with recommendations of the 2021 Safeguards Assessment Report (corrective action prior to presenting the misreporting case to the Board).

- The RBM Board has established an Asset Liability Management Committee (ALCO) in accordance with recommendations of the 2021 Safeguards Assessment Report; and ALCO is fully operationalized (**SB**)
- Prepare, in consultation with Fund staff, and submit the amendments to the RBM Act to the Parliament as recommended by the 2021 safeguards assessment (**SB**).
- To strengthen accuracy of RBM's program monitoring data, will (i) institute a policy to have our external auditors verify NIR data within 10 weeks after each test date, and (ii) submit monetary data through standard reporting forms to the Fund on a regular basis.

33. Misreporting of NIR: A special audit of RBM's foreign exchange reserves for the first three reviews under the 2018 ECF was completed mid-June 2022 and confirmed the noncomplying disbursements under the previous ECF (corrective action prior to presenting the misreporting case to the Board). In addition, we have implemented several corrective measures, including (i) the RBM now submits to the Fund staff monetary and financial statistics (MFS) using the Standard Reporting Form (SRF), supported by Fund Technical Assistance; (ii) submitting terms of existing foreign exchange swaps and other reserve liabilities to Fund staff on a regular basis; and (iii) published RBM's restated financial statements for 2018-2021 in accordance with the 2021 Safeguards Assessment recommendations and iv) realigned value of the kwacha with the market determined rates at end-May 2022. Going forward, we will continue taking a set of remedial measures aimed at rebuilding external buffers, addressing macroeconomic imbalances, and improving the quality of data submitted to the IMF as articulated in paragraph 31 and listed below:

- Continuous and timely reporting to Fund staff of reconciled sources and uses of foreign exchange reserves of the RBM;
- Establishing a registry to ensure consolidating records of all liabilities and contracted facilities, including pledges, encumbrances to strengthen transparency, recording and monitoring of RBM's liabilities; and
- Committing to fiscal discipline to ensure fiscal and external sustainability over the medium-term

34. The misappropriation of COVID-19 public funds is a stark reminder of the urgent need to address longstanding governance weaknesses. We have completed audits of three tranches of public funds released from the Ministry of Finance to different COVID-19 clusters in MDAs. The audit report for MWK 6.2 billion was completed by the National Audit Office (NAO) in March 2021, made public in April 2021 and the government is implementing the recommendations of the report which has led to recovery of some of the misappropriated funds. The implicated officials have faced disciplinary actions and criminal charges. The audit of the other two tranches amounting MWK 17.2 billion and MWK 5.0 billion, outsourced to external auditors, have been completed and submitted to the Ministry of Finance and Parliament in April 2022. Preparations are underway for specific follow-up actions needed to implement audit recommendations for the two tranches

35. Governance weaknesses at the Export Development Fund (EDF) pose a risk to the government in terms of contingent liabilities. EDF is a wholly owned subsidiary of RBM but the Government is working on modalities to merge EDF with Malawi Agricultural and Industrial Investment Corporation, PLC (MAIIC).

36. Broader governance agenda. Mindful of the obvious fact that corruption harms society, undermines national economic development, and threatens democracy, the Government adopted a strategy to combat corruption. His Excellency the President Lazarus McCarthy Chakwera, from the outset of his administration, set out the 'golden thread of conditions' with the objective to ensure that the Malawi economy is put on a path to economic recovery and strives. Among the conditions, the rule of law, the presence of law enforcement institutions, and the absence of corruption stood out. The Government's strategic response to corruption includes four components used to combat serious and organised crime. These include: (a) prosecuting and disrupting people engaged in corruption (Pursue); (b) preventing people from engaging in corruption (Prevent); (c) increasing protection against corruption (Protect); and (d) reducing the impact of corruption where it takes place (Prepare). The plan will be reviewed on a regular basis, as part of the Government's commitment to open partnership with all key stakeholders in combating the scourge. To facilitate implementation of the strategy,

- Office of the Director of Public Asset Declarations will digitise asset declarations for easy access and transparency. This to include the establishment of an interface system between ODPOD and ACB to facilitate lifestyle audits by September 2023.

- Strengthen collaboration among the Financial Intelligence Agency (FIA), the Director of Public Prosecutions (Asset Forfeiture Unit) and ACB in tracing assets belonging to suspects for freezing and subsequent confiscation by September 2023.

- Operationalization of the Financial Crimes Court

- The ACB will establish and sign a Memorandum of Understanding of cooperation with a selected MDAs by June 2023 to facilitate data and information sharing for combating corruption purposes.

- We will request for a governance diagnostic technical assistance from the IMF.

F. Enhancing Transparency and Accountability of Strategic Imports

37. The Government will ensure publication of strategic imports data on a timely manner. More specifically, MERA will publish monthly volume, value, and prices of fuel importation by importer; Ministry of Agriculture, with the support of Malawi Fertilizer Association, will publish those of fertilizers for the AIP; and Central Medical Stores Trust (CMST) will publish those of medical supplies.

PROGRAM MONITORING, PRIOR ACTIONS AND STRUCTURAL BENCHMARKS UNDER THE PMB

38. The macroeconomic policies supported by the PMB 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 November 2022-November 2023 will anchor our structural reform agenda during the course of the program (Table 3). The quantitative targets (QTs) and indicative targets (ITs) under the PMB are outlined in Table 1.

Table 1. Malawi: Quantitative and Indicative Targets, 2022–23

	Target type [2]	2022	2023		
		End-Dec.	End-Mar.	End-Jun.	End-Sep.
		QT	IT	QT	IT
I. Monetary targets (billions of kwacha)					
Monetary base (ceiling on stock) (upper bound)[3]	QT	590.2	607.6	662.2	674.2
Monetary base (ceiling on stock)[3]		573.0	589.9	642.9	654.6
Monetary base (ceiling on stock) (lower bound)[3]		555.8	572.2	623.6	634.9
II. Fiscal targets (billions of kwacha)					
Domestic revenue (floor)[6]	IT	1,202.7	1,603.5	2,130.6	2,657.6
Domestic primary fiscal balance (floor)[4,6]	QT	-17.1	-70.0	54.9	104.0
RBM financing of central government (ceiling)[6,7]	QT	0	0	0	0
New domestic arrears (ceiling)[6]	IT	0	0	0	0
Social spending (floor)[6,8]	IT	503.7	669.3	203.2	409.8
III. External sector targets (US$ millions, unless otherwise indicated)					
Change in net international reserves of the RBM (floor)[5]	QT	141.3	7.0	209.0	54.7
Accumulation of external payments arrears (ceiling)[6,9]	QT	0	0	0	0
Contracting or guaranteeing of non-concessional external debt (ceiling)[6,9,10]	QT	0	0	0	0
Contracting or guaranteeing of concessional external debt (ceiling)[6]	IT	15	30	15	30
Memorandum items:					
Program exchange rate (kwacha per US$)		1,026.4	1,026.4	1,026.4	1,026.4

Source: IMF staff projections.

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

[2] "QT" means Quantitative Target and "IT" means Indicative Target. The QT test date for the 1st Review is end-December 2022. Test dates for future reviews will be end-June 2023. End-March and end-September 2023 targets are ITs.

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

[4] Targets are subject to an adjustor for general budget support, as specified in the TMU.

[5] Targets are subject to an adjustor for (i) debt service and fees and (ii) general budget support, as specified in the TMU.

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

[7] Targets are subject to an adjuster equivalent to 10 percent of the average of the inflation adjusted domestic revenues of the previous three fiscal years, as specified in the TMU.

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

[9] Evaluated on a continuous basis.

[10] For program purposes, a limited exception on NCB may be allowed only in the exceptional circumstance that it is used to wind down maturing swaps and for debt management operation that improves the overall debt profile.

Table 2. Malawi: Structural Benchmarks under the Staff Monitored Program		
Actions	**Timing**	**Objectives**
Fiscal reforms		
• Roll out full functionalities of IFMIS to all MDAs. The full functionalities will include: (i) capturing all existing contracts/commitments in IFMIS, (ii) issuance of quarterly spending limits and monthly payment funding, (iii) requiring all financial transactions to be entered through IFMIS at the commitment.	• End-March 2023	• Interconnectedness; internal control over transactions; eliminate unnecessary duplications; achieve comprehensive coverage in IFMIS; reduce vulnerabilities to corruption. • Ensure new IFMIS delivers on accountability and efficiency in the execution of PFM reforms.
• Submit the audited fiscal report of FY2021/22 to IMF staff.	• End-December 2022	• Foster accountability and monitoring.
• Notify the FY2022/23Q3 quarter allotment to the pilot MDAs that is in line with the macroeconomic framework and allow MDAs to commit up to this amount through IFMIS.	• End-December 2022	• Demonstrate capacity to monitor and control commitments.
• Publish the quarterly audited IFMIS-generated comprehensive monthly fiscal reports.	• Continuous, starting in FY2023/24	• Foster fiscal transparency and monitoring. • Improve the in-year comprehensive monthly fiscal reports.
• Complete verification of arrears of national budget entities from July 1, 2020 to March 31, 2022 certified by the Auditor General, including compensations and utilities.	• End-December 2022	• Foster financial discipline
• Approval by the Cabinet of an arrears clearance and prevention strategy for national budget entities that has been prepared in consultation with staff.	• End-February 2023.	• Foster financial discipline.
Monetary and Financial sector reforms		
• Pre-announcement of forex purchases to allow for a period of market-price formation	• End-November 2022	• Deepen the interbank FX market, improve market functioning, efficiency in intermediation with improved liquidity.

Table 2. Malawi: Structural Benchmarks under the Staff Monitored Program (concluded)		
Actions	**Timing**	**Objectives**
Monetary and Financial sector reforms		
• Prepare, in consultation with Fund staff, and amend the RBM Act as recommended by the 2021 safeguards assessment; and submit amendments to Parliament.	• End-June 2023	• Strengthen RBM governance.
• Establish an executive Asset Liability Management Committee (ALCO) in accordance with recommendations of the 2021 Safeguards Assessment Report; and fully operationalize the ALCO.	• End-March 2023	• Strengthen oversight of foreign reserve assets.
Governance		
• Follow-up action report on the COVID-spending audit report and EDF's audit report. Publish a follow-up report related to the COVID-spending audit report, detailing the corrective actions and measures to pursue and respond to audit findings, including the follow-up of alleged misappropriation of funds as well as the coverage of a second audit findings.	• End-October 2023	• Strengthen governance and data transparency.

Table 3. Malawi: Prior Actions Under the Staff Monitored Program		
Actions	**Objective**	**Status**
Governance		
• Completion of special external audit of the foreign exchange reserves of the RBM, based on terms of reference prepared in consultation with IMF staff, to be conducted by a reputable international auditing company.	• Strengthen governance and data accuracy and address one of the corrective actions on the misreporting case under the 2018 ECF program.	• Conducted from March through June 2022; and • Completed on June 17, 2022.
Fiscal reform		
• Submit the FY2022/23 Revised Budget that is in line with the macroeconomic framework to the Cabinet.	• Demonstrate commitment to reform.	• Submitted on November 9, 2022

Attachment II. Technical Memorandum of Understanding

A. INTRODUCTION

1. **This memorandum sets out the understandings between the Malawian Authorities and the International Monetary Fund (IMF) regarding the definitions of the structural benchmarks (SBs), and indicative targets (ITs) for the Staff Monitored Program with Executive Board Involvement (PMB) as described in the Memorandum of Economic and Financial Policies (MEFP) for the period November 2022 through November 2023, and sets out the data reporting requirements.** It also describes the methods to be used to assess the program performance and the information requirements to ensure adequate monitoring of the targets. The authorities will inform the Fund before modifying measures contained in this memorandum, or adopting new measures that would deviate from the goals of the program, and provide the Fund with the necessary information for program monitoring.

B. COVERAGE

2. **The government is defined as the budgetary central government of Malawi, extra-budgetary units of the central government, and transfers to local government.** It excludes public nonfinancial corporations, public financial corporations, operations of local councils and social security funds. The budgetary central government is defined as central government entities with budgets controlled by the Ministry of Finance and Economic Affairs (MOFEA).

3. **The coverage of the financial sector includes the Reserve Bank of Malawi (RBM) and other depository corporations (ODC).** Monetary aggregates under the program are based on the central bank survey, other depository corporations survey, and depository corporations survey, in accordance with the Monetary and Financial Statistics (MFS) 2016 manual.

C. PROGRAM EXCHANGE RATES

4. **For the purpose of evaluating the ITs, all foreign currency-related assets, liabilities, and flows will be evaluated at "program exchange rates" as defined below, with the exception of items affecting government fiscal balances, which will be measured at the current RBM exchange rates.** The program exchange rates are those that prevailed on end-September 2022. Accordingly, the exchange rates for the purposes of the program are shown in Table 1.

Table 1. Malawi: Cross rates for Nominal Exchange Rate and Gold Price for the 2022 PMB, 2022–23

	30-Sep-22
Gold bullion LBM[1] US$/troy ounce	1660.61
SDR to US$ exchange rate	0.78
Euro to US$ exchange rate	0.97
Yuan to US$ exchange rate	7.10
Yen to US$ exchange rate	144.74
Sterling UK to US$ exchange rate	1.11
Australian $ to US$ exchange rate	0.65
Canadian $ to US$ exchange rate	1.38
Swiss Franc to US$ exchange rate	0.98
Kuwaiti dinar to US$ exchange rate	0.31
Saudi Arabian riyal to US$ exchange rate	3.76
UAE dirham to US$ exchange rate	3.67
South African rand to US$ exchange rate	17.98
Malawian kwacha to US$ exchange rate	1026.4

Sources: IMF (International Financial Statistics); and Reserve Bank of Malawi

[1] LBM connotes London Bullion Market.

D. QUANTITATIVE AND INDICATIVE TARGETS

5. **Quantitative Targets are established for December 31, 2022 and June 30, 2023; and Indicative Targets are established for March 31, 2023 and September 30, 2023 with respect to:**

- Monetary base (ceiling);
- Domestic revenue (floor)
- Domestic primary balance of the government (floor);
- RBM financing of the central government (ceiling);
- New domestic arrears (ceiling);
- Social spending (floor);
- Change in net international reserves (NIR) of the RBM (floor);
- Accumulation of external payments arrears (ceiling);
- Contracting or guaranteeing of non-concessional external debt (ceiling); and

- Contracting or guaranteeing of concessional external borrowing (ceiling).

E. DEFINITIONS

A. Targets for Monetary Aggregates

- **Ceiling on the Stock of Monetary Base**

6. A ceiling applies to the upper bound of a monetary base band (set +/-3 percent) around the monetary base target.

7. Definition. The monetary base is defined as currency in circulation, ODCs' deposit holdings at the RBM, and those deposits of money-holding sectors at the RBM that are also included in broad money as defined in the Monetary and Financial Statistics (MFS) Manual (2016).

B. Targets for Fiscal Sector

- **Floor on Domestic Revenue**

8. A floor applies to the cumulative flow of domestic revenue since the beginning of the fiscal year.

9. Definition of domestic revenue: The program domestic revenue is tax and nontax revenue, or other revenue as defined in GFSM 2014 Chapter 5, recorded on a cash basis. External loans and grants are excluded. Transfers from extra-budgetary funds, proceeds from the sale of financial assets, revenue from privatizations or from the granting or renewal of licenses, and investment proceeds on government assets are not considered domestic revenue for the purposes of this program.

- **Floor on Domestic Primary Fiscal Balance**

10. A floor applies to the cumulative flow of domestic primary fiscal balance since the beginning of the fiscal year.

11. Definition of the domestic primary fiscal balance. Domestic primary fiscal balance is defined (i) domestic revenue less (ii) the sum of recurrent budget expenditure (net of domestic and foreign interest payments), and domestically-financed budget development expenditure.

12. Definition of net foreign borrowing of the government: Net foreign borrowing is defined as the sum of project and program loan disbursements from official creditors (both multi- and bilateral creditors), holdings of government securities by non-residents, and commercial borrowing from non-residents, minus amortization due.

13. Definition of general budget support: General budget support includes all grants and foreign financing not directly linked to externally financed projects. Excluded from this definition are external project financing to fund particular activities, BOP support from the IMF as defined in the Memorandum of Understanding between the MOFEA and RBM, and donor inflows (in kwacha) from the foreign currency-denominated donor pool accounts for the Joint Funds (e.g. health, education, and agriculture), held in financial institutions.

14. Adjustors:

- Adjustor on domestic primary fiscal balance – general budget support: In the event of a general budget support shortfall (or excess), the floor on domestic primary fiscal balance will be adjusted downward (or upward) by the full amount by which the foreign currency-denominated inflows from the general budget support falls short of (or exceed) the program baseline. The kwacha value of the cumulative shortfall (or excess) will be calculated at the program exchange rate. General budget support is measured as the cumulative flow from the beginning of the fiscal year.

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

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

16. Adjustors:

- For cash management purposes, the ceiling on RBM financing of the central government for December 31, 2022, March 31, 2023, June 30, 2023, and September 2023 is subject to an upward adjustment of up to 10 percent of the average inflation adjusted annual domestic revenue of the government for the past three fiscal years.

- **Ceiling on New Domestic Arrears**

17. Definition of domestic arrears: Arrears are defined in PFM Act means all unpaid bills, inclusive of contractual and statutory obligations, after the end of financial year. For the purpose of this TMU, payments on wages and salaries, transfers, and compensations are deemed to be 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, following receipt of the goods or services, they have not been made beyond the fiscal year, or – if a grace period has been agreed – within the contractually agreed grace period. For the purpose of the monthly reporting, the outstanding purchase orders, payables, and cash expenses on goods and services will be reported. New pensions arrears are deemed to exist if the stock of pension increases during the end of the fiscal year. For the purpose of the monthly reporting, outstanding pension payments in the last quarter due will be reported.

- **Floor on Social Spending**

18. Definition of social spending. Social spending is defined as on-government spending on social protection[1] using the Unified Beneficiary Register, education expenditure[2], and health expenditure[3].

C. Targets for External Sector

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

19. Definition of net international reserves (NIR) of the RBM: The Net International Reserve (NIR) of the RBM is defined as reserves assets (RA) of the RBM minus foreign currency drains (FCD) of the RBM. The values of all foreign assets and FCD will be converted into U.S. dollars at each test date using the program cross exchange rates listed in Table 1. Change in NIR on each test date is calculated on a quarterly basis: that is, the change is calculated between the stock of the NIR on the test date and that of the end-date of the previous quarter.

20. Definition of reserve assets of the RBM. 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). 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.

21. Foreign currency drains (FCD) of the RBM are defined as the sum of the following:

(i) outstanding medium and short-term liabilities of the RBM to the IMF. SDR allocations are excluded from foreign currency drains of the RBM; and

(ii) all foreign currency liabilities of the RBM and the RBM as an agent of the government to come due within the next 12 months (4 quarters). These liabilities include (a) foreign currency debt service falling due in the next 12 months (4 quarters) and (b) swap outstanding with remaining maturity of less than one year.

[1] To include social cash transfer, climate-smart public works, and AIP.

[2] Expenditure on early childhood education, primary, and secondary education services.

[3] Expenditure on basic health care package provided by primary and tertiary facilities.

22. Adjustors Applied to change in NIR Program Floor:

- **Adjustment clause on NIR- debt service and fees**: The program floor on change in NIR will be adjusted upward by the full amount by which the debt restructuring reduces debt service, or downward by which debt service increases or if fees related to debt restructuring incur. The debt service adjustment includes the changes in the debt repayment schedule due to the restructuring relative to the baseline.

- **Adjustment clause on NIR- general budget support**: The program floor on change in NIR will be adjusted upward by the full amount by which the foreign currency-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 change in NIR floor by the full amount by which the foreign currency-denominated inflows from the budget support falls short of the program baseline. They will be recorded in the original currency of payment and then converted to U.S. dollars using the above defined program cross exchange rates.

- **Ceiling on Accumulation of External Payment Arrears**

23. Definition of external payment arrears: External payment arrears consist of debt service obligations (principal and interest) of the government or the RBM to nonresidents that have not been paid at the time they are due, or if a grace period has lapsed, as specified in contractual agreements. External debt subject to rescheduling or restructuring based on the official announcement of the debt restructuring strategy is exempted from being included as external payment arrears. This performance criterion will be monitored on a continuous basis.

- **Ceiling on Contracting or Guaranteeing Non-Concessional and Concessional External Debt**

24. Definition of public and publicly guaranteed 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. For program purposes, a debt is considered contracted when all conditions for its entrance into effect have been met, including approval by the National Assembly. Contracting of credit lines with no predetermined disbursement schedules or with multiple disbursements will be also considered as contracting of debt. 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.

Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

25. Definition of concessional and non-concessional external debt. Short-, medium-, and long-term debt is considered concessional if it includes a grant element of at least 35 percent[4] 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 debt service payments at the time of the contracting of the debt.[5] The discount rate used for this purpose is 5 percent per annum. The ceiling on concessional and non-concessional debt applies to the contracting and guaranteeing of debt with nonresidents by the 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.

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

[4] 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.

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

27. Medium- and long-term debt: Outstanding stock of debt with an original maturity of more than one year.

28. Excluded from the limit on non-concessional external debt is the use of IMF resources.

29. Swaps in debt service: In line with definition of debt (Para.5), debt service payments should include swaps based on the net change in the position.

30. Foreign exchange swaps: contracting or renewing foreign currency swaps with non resident banks beyond the program amount would be subject to the ceiling of non-concessional external debt since they pose fiscal risks.

REPORTING REQUIREMENTS

31. For the purpose of program monitoring, the Government of Malawi will provide the data listed in Table 2 below. For all bi-weekly submissions, data should be reported with a lag of one week. For all monthly and quarterly submissions, data should be reported within 3 weeks. For data submissions requiring audit, data is reported within 8 weeks. Annual data will be provided within six months after the end of the year.

32. The authorities will inform the IMF staff in 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), development agreements, wage policy, and financial support to public and private enterprises. The authorities will similarly inform the IMF staff of any concessional or non-concessional external debt contracted or guaranteed by the government, the RBM, or any statutory bodies, and any accumulation of new external payments arrears on the debt contracted or guaranteed by these entities.

33. The authorities will furnish an official communication to the IMF describing program quantitative performance, structural benchmarks, and indicative targets within 8 weeks of a test date.

Table 2. Malawi: Summary of Reporting Requirements				
	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Agency
Exchange Rates, Spread between exchange bureau midrate and the official exchange midrate	D	2W	D	RBM
Volume of transactions in the interbank money market and Lombard Facility, including banking system liquidity	D	2W	M	RBM
Foreign Exchange Cashflow (including Reserve Assets, Sources and Uses of foreign currency) (Telex Table 14)	D	2W	M	RBM
RBM intervention and ADB's Sales and Purchases of FX	D	2W	M	RBM
Foreign Exchange Swaps	continuous	2W	M	RBM
Reserve/base money, FMO transactions, and RBM conversion of ways and means account to government securities	M	M	M	RBM
Monetary and Financial Statistics Standard Report Forms (1SR, 1SG, 2SR, 2SG, 3SG, 5SR in Telex Table 1)	M	M	M	RBM
Consumer Price Index and monthly statistical bulletin (Telex Table 5)	M	M	M	RBM
Detailed issue and maturity profile for all government securities (Telex Table 6 & 7)	M	M	M	RBM
Central government domestic borrowing (Holdings of local registered stocks, treasury bills, treasury notes and other government securities) (Telex Table 8, 13, 20)	M	M	M	RBM
RBM financing of the central government	M	M	M	RBM
Government Project Funds through the RBM (Telex Table 9)	M	M	M	RBM
Interest rates [2] (Telex Table 12)	M	M	M	RBM
RBM foreign exchange cash flow and intervention (Telex Table 14, 27)	M	M	M	RBM
ADBs FCDA Balances (Telex Table 15)	M	M	M	RBM
Banking System Liquidity (Required and Excess Reserves) (Telex Table 16)	M	M	M	RBM

Table 2. Malawi: Summary of Reporting Requirements (continued)

RBM Holding of Treasury Bills and Conversion of Ways and Means Advances (Telex Table 17)	M	M	M	RBM
Reserve Assets of the Monetary Authorities (as defined in Chapter 1 of International Reserves and Foreign Currency Liquidity: Guidelines For A Data Template)[3] (Telex Table 19)	M	M	M	RBM
Foreign Currency Drains of the Monetary Authorities (as defined in Chapter 3 of International Reserves and Foreign Currency Liquidity Guidelines For A Data Template)[3,4] (Telex Table 19)	M	M	...	RBM
Government securities auction results (Telex Table 20)	M	M	M	RBM
Bank statements of the Ministry of Health Swap account, agricultural Swap account, NAC account held at RBM (Table 24, 25, 26)	M	M	...	RBM
Sectoral Allocation of Private Sector Credit (Telex Table 28)	M	M	M	RBM
RBM Foreign Exchange Deposits (Telex Table 32)	M	M	M	RBM
Financial soundness indicators by banks (Telex Table 34)	M	M	...	RBM
Forex Bureau Trade Volume (Telex Table 35)	M	M	M	RBM
Balance of payments	A	A	A	RBM / NSO
New external loans contracted or guaranteed by the government and disbursement schedule [5]	Continuous	Continuous	Continuous	MOFEA
Revenue collected by MRA, by major revenue line	D	2W	M	MOFEA
Accumulation of new domestic government arrears[6]	M	M	M	MOFEA
Strategic Imports (value, volume, and prices)	M	M	M	MOFEA
Fiscal table (GFS based), including revenue, grants, expenditure, balance, and composition of financing of the central government[5, 7]	M	M	...	MOFEA
In-year comprehensive monthly fiscal reports	M	M	Q	MOFEA
Exports and imports of goods and subcomponents (to be added to Telex tables submissions)	M	M	Q	MOFEA

Table 2. Malawi: Summary of Reporting Requirements (concluded)

On and off-budget project reports	Q	Q	Q	MOFEA
Stocks of public sector and public-guaranteed debt [5, 8]	Q	Q	Q	MOFEA
Quarterly external debt service (actual and projections)	Q	Q	…	MOFEA
Debt service payments on domestic debt (outturn and projections)	M	Q	Q	MOFEA
Report on IMF program performance	Q	Q	…	MOFEA
Quarterly report on clearance of government domestic arrears	Q	Q	…	AG
Exports and imports of services, and subcomponents.	A	A	A	MOFEA
Annual financial reports of the 5 high-risk parastatals[9]	A	A	…	MOFEA
Consolidated financial statements and audit opinion	A	A	A	AG
Consolidated budget execution reports	M	M	A	AG
GDP[/GNP], by activity and expenditure, at constant and current prices	A	A	A	MOFEA

[1] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Semi-annually (SA); Irregular (I).

[2] Both market-based and officially-determined, including discount rates, money market rates, interbank money market rate, rates on treasury bills, notes, and bonds.

[3] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

[4] Includes a memorandum section which includes Net International Reserves based as defined in this TMU.

[5] 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.

[6] In accordance with the definition of arrears in the TMU Paragraph 17.

[7] Foreign and domestic banks, and domestic nonbank financing.

[8] Includes borrowing of 8 major parastatals: Agriculture Development and Marketing Corporation (ADMARC), Electric Supply Company of Malawi (ESCOM), Electricity Generation Company of Malawi (EGENCO), Malawi Housing Corporation, National Oil Company of Malawi (NOCMA), Northern Regional Water Board, Lilongwe Water Board, and Blantyre Water Board (BWB).

[9] ADMARC, BWB, ESCOM, EGENCO, and NOCMA.

INTERNATIONAL MONETARY FUND

MALAWI

November 14, 2022

REQUEST FOR DISBURSEMENT UNDER THE RAPID CREDIT FACILITY AND REQUEST FOR A STAFF MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT—DEBT SUSTAINABILITY ANALYSIS

Approved By
Costas Christou and Bjorn Rother (both IMF) Marcello Estevao and Asad Alam (both IDA)

Prepared by the International Monetary Fund and the International Development Association.[1]

Malawi: Joint Bank-Fund Debt Sustainability Analysis[2]	
Risk of external debt distress	*In Debt Distress*
Overall risk of debt distress	*In Debt Distress*
Granularity in the risk rating	*Unsustainable*
Application of judgment	*No*

Malawi's external and overall public debt is assessed as "in distress"—a downgrade from the previous Debt Sustainability Analysis (DSA) (December 2021) in light of ongoing debt restructuring negotiations. This DSA presents an analysis of Malawi's debt situation prior to the implementation of the authorities' debt restructuring strategy. Under the baseline scenario, the PV of PPG external debt-to-GDP ratio remains below the threshold throughout the horizon. A breach, however, is observed in the PV of debt-to-exports, debt service-to-exports, and debt service-to-revenue ratios over the medium term—the heaviest burden weighing in the near term with the external debt-to-exports ratio at 55.6 percent in 2022. The PV of the debt-to-exports ratio remains above the threshold of 140 percent especially if the residual financing gap were to be financed externally. The solvency indicator, the PV of public debt-to-GDP ratio, remains above the threshold throughout the medium term and beyond.

[1]The current DSA follows the revised Debt Sustainability Framework (DSF) for LICs and Guidance Note (2017) in effect as of July 1, 2018.

[2] Malawi's CI based on the current vintage (2022 CPIA) remains 'weak' with a CI score of 2.34.

PUBLIC DEBT COVERAGE

1. **The DSA covers central government debt, central government guaranteed debt, and central bank debt contracted on behalf of the government** (Text Table 1).[3] Public debt used for this 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 nonguaranteed state-owned enterprise (SOE) debt.[4]

Text Table 1. Malawi: Coverage of Public Sector Debt, 2021

	Subsectors of the public sector	Check box
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	

Public debt coverage and the magnitude of the contingent liability tailored stress test

		Default		Used for the analysis	Reasons for deviations from the default settings
1	The country's coverage of public debt	The central government, central bank, government-guaranteed debt			
2	Other elements of the general government not captured in 1.	0	percent of GDP	3	Limited coverage, 1 percent for contingent liabilities due to swaps
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2	percent of GDP	2	
4	PPP	35	percent of PPP stock	0.00	
5	Financial market (the default value of 5 percent of GDP is the minimum value	5	percent of GDP	5	
	Total (2+3+4+5) (in percent of GDP)			10.0	

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

2. **This DSA is being conducted in the context of the authorities' request for disbursement under the Rapid Credit Facility (RCF) and Staff Monitored Program with Executive Board Involvement (PMB)**. The last Low-Income Country (LIC) DSA using LIC-Debt Sustainability Framework (DSF) was considered by the Executive Board in November 2021 as part of the 2021 Article IV Consultation.[5] Malawi is subject to the IDA Sustainable Development Finance Policy (SDFP) which includes as Zero Nonconcessional Debt Ceiling.[6]

[3]The definition of external and domestic debt uses a residency criterion.

[4]The contingent liabilities shock from the SOE debt is kept at the default value of 2 percent to reflect risks associated with nonguaranteed SOE debt, currently excluded from the analysis due to data availability constraints. There are no current PPPs reported that subject the authorities to contingent liabilities.

[5]This DSA is prepared jointly by the staff of the IMF and World Bank, in collaboration with the authorities of Malawi. The last joint DSA can be found in IMF Country Report No. 21/269, November 2021.

[6] The International Development Association (IDA)'s Sustainable Development Finance Policy approved in 2020 builds on lessons learned from the Nonconcessional Borrowing Policy (NCBP) to further strengthen the focus on debt sustainability and debt transparency. Malawi has implemented Performance and Policy Actions (PPAs) related to Debt Transparency, Debt Management, and Fiscal Sustainability. These included PPAs on a zero nonconcessional borrowing ceiling in FY21 and FY22. Malawi satisfactorily implemented its FY21 and FY22 PPAs and is now three PPAs for FY23. Under the SDFP, a zero ceiling on nonconcessional borrowing applies to countries under LIC DSF at high risk of debt distress or that are in debt distress.

3. A sequence of external shocks has exacerbated Malawi's fragility—including worsening food insecurity. Malawi's economy recovered in 2021, but real GDP growth in 2022 is projected to decline to 0.8 percent—due to a series of exogenous shocks that have exacerbated macroeconomic imbalances. During the first quarter of the year, Malawi faced two tropical cyclones, rising commodity prices, and forex shortages—all contributing to an imminent BOP crisis. The economy remains fragile in the face of vulnerabilities to natural disasters and spillovers from the war in Ukraine. The ongoing energy crisis—chronic fuel shortages and extended electricity blackouts—has further dampened economic activity. Foreign exchange scarcity remains despite a 25 percent currency devaluation at end-May, contributing to inflation pressures and a de facto rationing of foreign exchange by commercial banks for the country's import needs. Substantial fiscal and external imbalances will further strain the economy in the near future. As a result of the multiple shocks, about 20 percent of the population are projected to be acutely food insecure at the "Crisis" level (IPC Phase 3 or higher) during the 2022/23 lean season (October 2022-March 2023). The population living at the crisis level more than doubled since last year.[7]

4. Continued fiscal and current account deficits resulted in a sharp rise in PPG debt. The government has relied on costly domestic bond issuances, increasing PPG debt as a share of GDP by more than 3-fold in 15 years (Text Figure 1) to support persistent fiscal deficits. Fiscal policy was only modestly adjusted in the face of decreased budget support and on-budget project grants after the Cashgate [8] scandal in 2013. Budget support and on-budget project grants that averaged 5.8 percent of GDP during 2005-13 were significantly reduced to about 1.8 percent of GDP since 2013. Since mid-2018, regional banks began to enter the domestic bond market, increasing Malawi's nonconcessional external borrowing. This supported the widening of current account deficits. The RBM and the Government of Malawi together had nonconcessional external commercial debt outstanding of 9.2 percent of GDP in 2021.

5. The trade deficit widened further in 2021. After a large decline in 2020, goods exports recovered in 2021, though not to the level of 2019. Meanwhile, imports continued to increase in 2021 amidst rising global prices. The volume of fertilizer and fuel imports are higher compared to pre-pandemic levels. Additionally, commodity-price hikes in 2021 pushed up the import value further and resulted in a further deterioration in the trade deficit.

6. Fiscal management and budget execution continue to be a challenge. FY2021/22 (April/March) marked a large deficit of 9.7 percent of GDP. Revenues held up, while expenditure exceeded previous years' average due to COVID-19 related fiscal support primarily to the private sector, fuel and fertilizers price hikes, higher interest expenses and wage increases. The latter represents the highest level of spending for employee compensation in over a decade.

[7] World Food Programme, Floods assessment Fact Sheet (10 June 2022) and Famine Early Warning System Network, Malawi Food Security Outlook Update (August 2022).

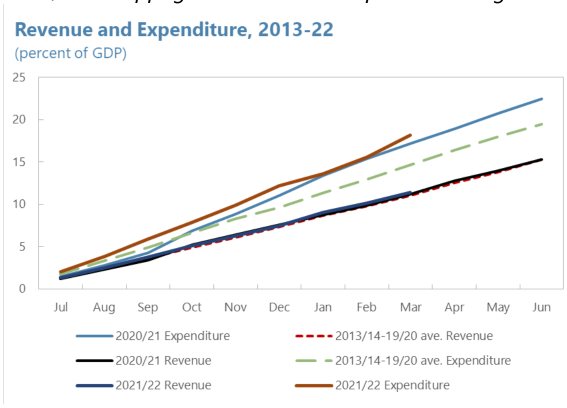
[8] "Cashgate" is a major corruption case that led to arrests, trials and convictions of a number of civil servants.

Overly optimistic budget revenue projections and weak commitment control also contributed to the fiscal deterioration. Delays in the fiscal consolidation thus made stabilizing debt more difficult.

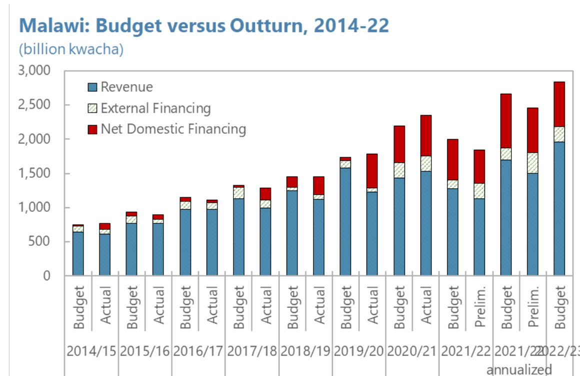
7. Public and external debt increased to unsustainable levels as a result. Total public debt increased from 45.3 percent of GDP in 2019 to 64.0 percent in 2021 to finance a large fiscal deficit in FY2021/22. External debt also reached 32.8 percent of GDP in 2021 compared to 27.8 percent in 2019.

Text Figure 1. Malawi: Fiscal Challenges Confronting a Fragile Economy, 2006–22

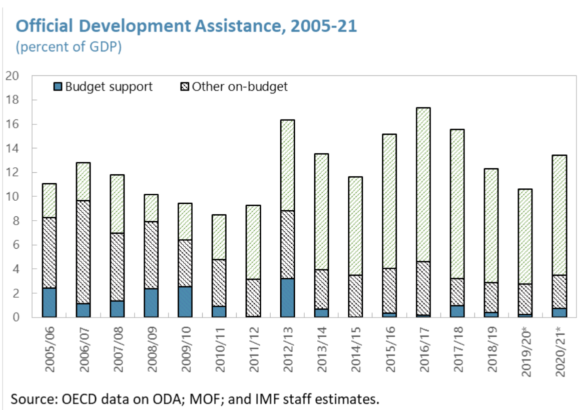
Revenues are holding up, while expenditure is exceeding previous years' average due to COVID-19 emergency response measures, fuel and fertilizers price hikes, and slippages relative to the planned budget.



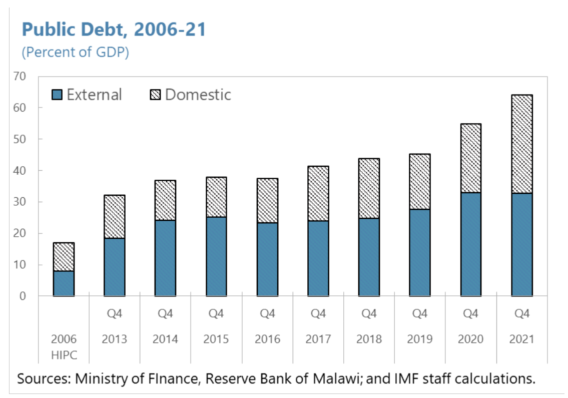
Overly optimistic budget revenue projections and weak commitment control have led to increased domestic financing.



Budget support declined significantly after the Cashgate scandal in 2013 but fiscal policy was only modestly adjusted.



As a result, at end-2021, public debt rose to 64 percent of GDP and external debt rose to 32.8 percent of GDP (a quarter of which is at nonconcessional terms).



Source: Malawian authorities; IMF staff estimates.

8. Public external debt (51.2 percent of total debt) is held mainly by official creditors (72 percent of total public external debt) (Text Table 2). Of this, official multilateral creditors hold 60.3 percent of Malawi's outstanding public external debt in 2021, including the International Development Association (IDA) (30.6 percent), the African Development Bank (AfDB) (11.1 percent), the IMF (10.2 percent), and other multilaterals (8.4 percent). Official bilateral debt is 11.7 percent.

Debt outstanding with nonofficial commercial banks is 28.0 percent of total external debt, of which AFREXIM bank (16.1 percent) is the largest private creditor to Malawi. Among debt outstanding held by nonofficial commercial banks, 5.8 percent is from foreign exchange swaps with nonresidents, with an amount equivalent to US$221.7 million.

9. Near term external debt service falls more heavily on commercial creditors. Terms of borrowing from commercial creditors are highly nonconcessional, with no grace period, and a typical maturity of 4-6 years. As a result, near-term debt service is highly concentrated among commercial creditors. Debt service to AFREXIM is $284 million in 2022 and $201 million in 2023, while that to TDB is $184 million in 2022 and $5.8 million in 2023. Debt service to AFREXIM and TDB is equivalent to 65 percent of external debt service in 2022.

10. Domestic debt comprises of government securities holdings by residents and foreign exchange swaps with residents. Residents hold MWK2.5 trillion T-Notes, of which 56 percent are held by commercial banks and the nonbanking sector, and MWK341.1 billion T-Bills. Combined, these government securities are equivalent to US$3,466 million presented in Text Table 2. Foreign exchange swaps with resident banks undertaken by the RBM amount to $202.2 million.

11. A credible process for restructuring debt to AFREXIM Bank is underway and Malawi is negotiating in good faith with TBD, to which it has arrears. Malawi has arrears vis-à-vis Trade Development Bank (TBD) while it is current on its obligations towards AFREXIM Bank.[9] With respect to TBD's claims, staff assesses that the requirements of the IMF's Lending Into Arrears (LIA) Policy are met, given that (i) prompt Fund support is considered essential for the successful implementation of Malawi's adjustment program, and (ii) Malawi is pursuing appropriate policies and it is making a good faith effort to reach a collaborative agreement with its private creditors. With respect to AFREXIM Bank's contribution to restore debt sustainability, assurances are derived from IMF staff's judgment that a credible process for debt restructuring is underway and such restructuring will likely deliver an outcome that restores debt sustainability to moderate risk in the medium term. With respect to both these creditors, Malawi has hired debt advisors, engaged in early discussions with its creditors on a restructuring strategy that is consistent with restoration of debt sustainability, has shared relevant information on its financial situation and its debt situation, and has given creditors an early opportunity to give input into the restructuring.

12. The authorities' debt restructuring strategy, if implemented, would bring Malawi's risk of debt distress to moderate in the medium term (Box 1). Compared to the November 2021 DSA, where near-term debt service to external nonofficial creditors was projected to be US$468 million in 2022 and US$207 million in 2023, the debt operations envisaged in the debt restructuring strategy would reduce debt service for nonconcessional loans substantially in 2022. From 2023, the possible commencement of a grace period would provide substantial relief.

[9] Malawi has also not incurred any arrears on bilateral official claims.

Text Table 2. Malawi. Decomposition of Public Debt and Debt Service by Creditor, 2021–2023[1]

	Debt Stock (end of period)			Debt Service			
	2021			2022	2023	2022	2023
	(In Million US$)	*(Percent total debt)*	*(Percent GDP)*	*(In US$)*		*(Percent GDP)*	
Total	7,521	100.0	64.0	2253	2012	19.2	17.4
External	3,853	51.2	32.8	719	377	6.1	3.3
Multilateral creditors[2]	2,324	30.9	19.8	93	92	0.8	0.8
IMF	394	5.2	3.4				
World Bank	1,178	15.7	10.0				
AfDB	427	5.7	3.6				
Other Multilaterals	325	4.3	2.8				
o/w: IFAD	94	1.2	0.8				
OFID	75	1.0	0.6				
Bilateral Creditors	450	6.0	3.8	47	45	0.4	0.4
Paris Club	7	0.1	0.1	3	3	0.0	0.0
o/w: Spain	5	0.1	0.0				
Belgium	1	0.0	0.0				
Non-Paris Club	443	5.9	3.8	44	42	0.4	0.4
o/w: EXIM China	239	3.2	2.0				
EXIM India	125	1.7	1.1				
Bonds	0	0.0	0.0	0	0	0.0	0.0
Commercial creditors	857	11.4	7.3	468	207	4.0	1.8
o/w: AFREXIM	619	8.2	5.3				
TDB	238	3.2	2.0				
FX Swaps with non-residents	222	2.9	1.9	111	33	0.9	0.3
o/w: Bank One	110	1.5	0.9				
ICBC London	67	0.9	0.6				
Domestic	3,668	48.8	31.2	1534	1636	13.0	14.2
Held by residents, total							
Held by non-residents, total							
T-Bills	3,466	46.1	29.5				
Bonds							
Loans							
FX Swaps with resident	202						
Memo items:							
Collateralized debt[3]	619	8.2	5.3				
o/w: Related							
o/w: Unrelated	619	8.2	5.3				
Contingent liabilities	192	2.6	1.6				
o/w: Public guarantees	192	2.6	1.6				
o/w: Other explicit contingent liabilities[4]							
Nominal GDP	12,004						

1/As reported by Country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same
2/Multilateral creditors" are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears)
3/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a
4/Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Box 1. Malawi: Debt Restructuring Strategy, October 2022

The authorities have developed a debt restructuring strategy which will serve as the cornerstone for restoring debt sustainability. They hired legal and financial advisors in May 2022 to support a credible process for restructuring based on adequate creditor engagement to ensure the approach taken delivers the necessary contributions in a sustainable manner. The Malawian authorities approached all creditors early in the process.

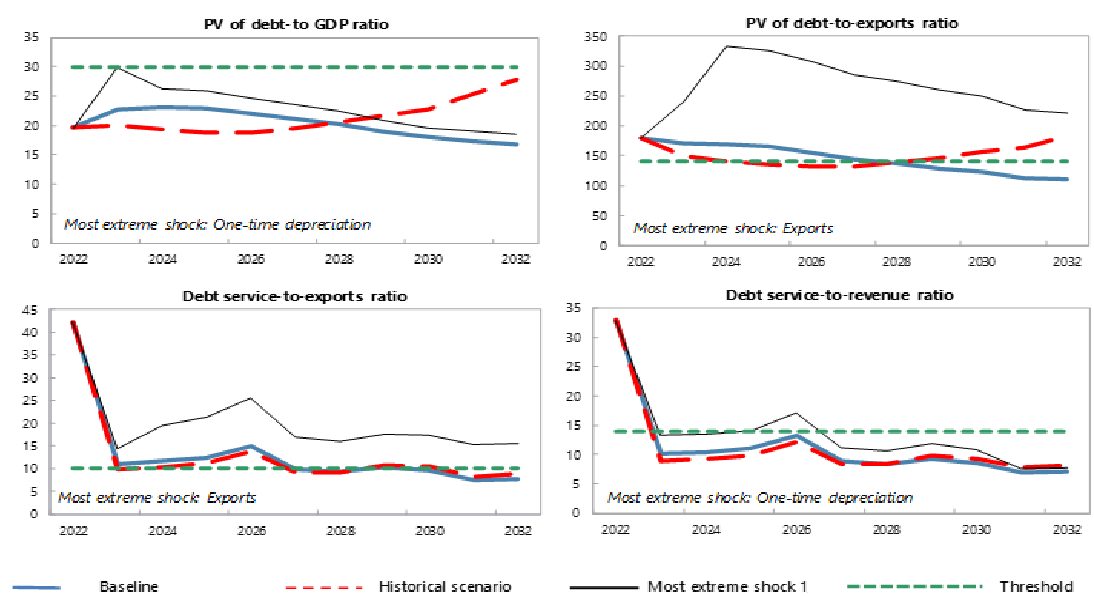
The debt restructuring strategy is designed to achieve debt sustainability and to close the financing gaps. The strategy relies on the following pillars to overcome current external debt challenges, including solvency and liquidity concerns:

- Bringing external public debt back to a moderate risk of debt distress in the medium term through a combination of policy adjustment and the necessary debt treatment. The debt strategy targets all external DSA solvency and liquidity ratios to move below their respective thresholds under the baseline over the medium term. This means the baseline of the present value of debt-to-GDP ratio to reach below 30 percent, the present value of debt-to-exports ratio below 140 percent, the external debt service-to-exports ratio below 10 percent and the external debt-to-revenue ratio below 14 percent in the medium term (see the panel chart below).

- Mobilization of nondebt-creating flows to ensure that external and fiscal financing gaps are closed over the program period, including through the debt treatment and the mobilization of external grant support from development partners.

- The corresponding net present value (NPV) debt reduction sought is US$579 million.

Indicators of Public and Publicly Guaranteed External Debt Under Post-Debt Restructuring Scenario, 2022–32



UNDERLYING ASSUMPTIONS

13. Financing assumptions rest on the implementation of a strict reform program by the authorities while debt restructuring negotiations are underway. The implementation of the reform program has already started in early 2022 with the passage of FY2022/23 budget with a sizeable fiscal consolidation in March, an increase in the monetary policy rate in April (and again in October), and the 25 percent devaluation in May. Decisive actions to secure financing and debt sustainability assurances are envisaged in the authorities' debt restructuring strategy (Box 1), which includes the replacement of nonconcessional external financing (assumed in the 2021 Article IV staff report) by nondebt-creating flows (grants[10] and debt relief). It is assumed that the authorities are current on existing obligations--except for TDB to which negotiations in good faith are ongoing.

14. The key macroeconomic assumptions have been updated from the DSA that accompanied the 2021 Article IV Staff Report (the November 2021 DSA hereafter). While the baseline scenario of the November 2021 DSA assumes the absence of policy reforms to restore debt sustainability, the current DSA assumes bold policy actions consistent with the reform program undertaken by the authorities to emerge from the BOP crisis. Financing gaps, however, remain as securing nondebt-creating flows to restore debt to a medium risk of debt distress is still underway. Changes to the underlying assumptions from the November 2021 DSA are as follows (Text Table 3):

- ***Economic growth*** has been revised downward. The real GDP growth projection for 2022 has been revised from 3.5 percent to 0.8 percent; reflecting the effect of Tropical cyclones Ana and Gombe, the impact of the war in Ukraine, import contraction due to FX shortages experienced since the first half of 2022, and the energy crisis in the second half of the year. Growth is projected to improve to 2.4 percent in 2023, reaching 4.5 percent in **the medium term**, incorporating gains from the reforms and investments underway. Meanwhile, the real GDP growth path in **the long term** has been revised downwards from 5.5 percent to 4.6 percent to capture recurrent weather shocks given Malawi's vulnerability to climate change.

  Key **structural reforms** and related investments include improvements to fiscal governance; implementation of the PFM Act 2022; policy reforms and investments to advance agricultural commercialization and productivity; as well as investments in transport, digital and energy infrastructure. These are expected to strengthen the resilience of the economy to climate change.

  Fiscal adjustment is achieved by increased revenue through taxes (see below), restraining recurrent spending as a share of GDP, including on the wage bill and the Affordable Input Programme (AIP). Development spending to support growth continues to be mainly financed by grants and highly concessional debt, and is expected to moderate in the medium to long term. Expenditures to cushion the impacts on the poor from the ongoing crisis and strengthen

[10] Consistent with the LIC DSF, grants were only included if they were committed and highly likely.

food security will be maintained or increased through grant financing. Over the long term, a stronger fiscal position is expected to contribute to increased confidence in the authorities' policies, improved macroeconomic stability and in turn increased private investment.

- ***CPI inflation*** is projected at 26.0 percent at end-2022 and about 6.5 percent in the long term, provided that the monetary and fiscal policy stance are well anchored in line with expected reforms. The projection captures rising fuel, food, and fertilizer prices in 2022. It also takes into consideration the depreciation of the currency and passthrough to inflation as the RBM builds up foreign reserves by purchasing foreign exchange in the market and winds down currency swap operations. It is assumed that reserve money growth will be kept in line with projected nominal GDP growth and the policy rate is assumed to be adjusted to achieve this goal. In this context, real interest rates are assumed to return to positive figures with the monetary tightening which targets inflation to approach the 6 percent target (Text Table 3). Moreover, it is also assumed that the RBM will conduct open market operations to sterilize the monetary impact of RBM's foreign exchange purchases; it is also assumed that the RBM may need to issue the central bank bills if the RBM does not have enough holdings of government securities to cover the magnitude of sterilization needed. It is also assumed that the government will contain fiscal deficits as envisaged under the program. The projected level and persistence of inflation in the medium term incorporates vulnerabilities to climate change and natural disasters.

- The ***fiscal primary deficit*** has been revised downward to reflect the envisaged fiscal consolidation. The projected fiscal primary deficit in FY2022/23 was revised down to 3.3 percent of GDP from the 4.8 percent projected during the 2021 Article IV Consultation. As the authorities implement policy reforms, the current fiscal primary deficit is projected to turn into a surplus of 0.7 percent of GDP by FY2025/26. Projections during the Article IV Consultation show that Malawi was able to reach the debt-stabilizing primary surplus at the end of the medium-term, but the current DSA shows that Malawi can reach it by 2025 thanks to the authorities' ambitious fiscal adjustment to restore debt sustainability. This fiscal consolidation reflects a comprehensive strategy that places equal weights on expenditure containment and revenue improvement. The revised FY2022/23 budget will reduce the domestic primary balance by 3½ percentage points of GDP relative to FY2021/22 by restraining the growth of the wage bill, and reductions in goods and services expenditures, the AIP, and domestically-financed development spending. The DSA assumes a balanced fiscal primary balance over the period 2025-42. The fiscal adjustment path takes into account the additional measures taken by the government to address high commodity prices.[11]

[11] In the 2022/23 lean season response, the government estimates total costs at MWK76 billion (approximately US$73 million). This sum will be covered in part under the current budget and with development partner support. The authorities have not announced any plans for further fuel price support.

Text Table 3. Malawi: Underlying DSA Assumptions, 2018–27

	Real GDP growth		Primary balance*		Total public debt*		Current account deficit		FDI	
	(Percent)		(Percent of GDP)		(Percent of GDP)		(Percent of GDP)		(Percent of GDP)	
Year	Previous	Current	Previous	Current	Previous	Current	Previous	Current	Previous	Current
2018	4.4	4.4	-2.7	-2.7	43.9	43.9	12.0	12.0	1.1	1.1
2019	5.4	5.4	-1.9	-1.9	45.3	45.3	12.6	12.6	1.0	1.0
2020	0.9	0.9	-2.7	-2.7	54.8	54.8	13.6	13.6	0.8	0.8
2021	2.2	2.2	-3.7	-3.7	58.3	64.0	15.0	14.6	0.8	0.8
2022	3.5	0.8	-6.5	-5.4	62.7	76.6	14.3	14.8	1.3	0.8
2023	4.5	2.4	-4.8	-3.3	66.9	74.6	12.6	13.6	1.3	1.0
2024	4.0	3.2	-4.2	-1.7	72.0	74.5	10.8	14.3	1.3	1.2
2025	4.0	3.8	-4.0	-0.2	78.0	73.8	10.7	13.1	1.4	1.3
2026	4.1	4.3	-4.2	0.7	83.6	72.6	10.4	11.2	1.4	1.4
2027	5.8	4.5	...	0.8	...	71.0	...	9.6	...	1.5
Avg 2027-2042	5.5	4.6	...	1.4	...	55.7	...	7.0	...	1.9

Sources: Malawian authorities and IMF staff calculations and projections.
* Fiscal data refers to fiscal year; e.g. 2021=FY2020/21

- Measures enhancing ***domestic revenue*** collection by about 3 percentage points of GDP are assumed during 2022-27. These would fall short of the 5 percent revenue enhancement target set forth in the government's Domestic Revenue Mobilization Strategy. Judgement was used to determine that such a path would not be realistic and a more careful, albeit still ambitious revenue trajectory entered the DSA. Additional income tax brackets and advance income tax were already introduced in 2022. To further boost revenue (which is at just 13.4 percent of GDP in FY2021/22), the authorities are committed to: introduce the presumptive tax for small businesses, rationalize the list of items subject to preferential General Sales Tax (GST) treatment, review tax incentive regimes to revamp the Taxation Act and Customs and Excise Act, strengthen the withholding tax regime, introduce measures to address Base Erosion and Profit Shifting (BEPS), reform excise tax rates; and continue efforts to improve tax administration such as the online rollout of the Integrated Tax Administration System (ITAS), also called Msokho. Additional measures are contemplated to improve nontax revenues. These include reviewing fees and charges to move them towards full cost recovery and ensuring that Ministries, Departments, and Agencies (MDAs) account for their revenue collections in IFMIS and remit nontax revenue collections to Malawi Government consolidated (MG1) account, the main source of funding of all its operations.

- ***Primary expenditure*** will decrease by about 3 percentage points of GDP during 2022-27 given adjustments in the wage bill, the AIP, and general goods and services. Spending within allocation and revenue performance would contain expenditure and discretionary spending to fall within the legislated budget. An increase in social protection spending of 0.2 percent of GDP, as a better targeted measure to support low-income households, will offset some of the expenditure reductions. An IDA operation is also scaling up support on social protection (Box 2). The combined cumulative adjustment is about 7.2 percentage points of GDP in the medium term or about 1½ percentage points of GDP per year.

- The ***current account deficit*** has been revised to 14.8 percent of GDP in 2022 and is projected to decline to 9.6 percent by end-2027. Staff projects a gradual recovery in service receipts (especially in hotel and transportation services), reaching pre-pandemic levels in 2024. Exports are expected to increase by 2024 considering the resumption of tobacco exports to the United States, the recent lifting of the export ban on maize, and other agricultural export diversification efforts. The impact of the exchange rate alignments (e.g., formalization of informal exports) is also assumed. Exports of goods and services are thus projected to increase from 11.0 percent of GDP in 2022 to 14.7 percent of GDP by end-2027, driven in part by the change in real effective exchange rate. The strategy is erring on the side of caution by excluding mining projects that could potentially commence during the medium term and generate exports.

- ***Gross official reserves*** were projected to increase from US$394.0 million (1.4 months of imports) in 2021 to US$401.8 million (1.5 months of next year's imports) in 2022 in the November 2021 DSA. In this DSA, it is revised to US$72 million (0.3 months of imports) in 2021 and US$172 million (0.6 months of next year's imports) in 2022, respectively. The gross official reserves were revised downwards compared to the 2021 Article IV Consultation because of the exclusion of encumbered deposits in line with the definition of reserve assets in the Monetary and Financial Statistics Manual. The **reserve accumulation path** assumes gross official reserves will recover to 3.7 months of imports by 2027. The external financing gap is assumed to be filled with nondebt creating flows, either debt relief or grants.

- **These adjustments in the external sector will be supported by a REER adjustment of about 39 percent** (the gap identified in External Sector Assessment), with a frontloaded adjustment in 2022 of 34 percent, and other efforts to improve exports. The REER adjustment will be achieved by allowing greater flexibility in the nominal exchange rate, supported by a tight monetary policy stance, fiscal consolidation, and a reduction of RBM external borrowing. RBM will purchase foreign exchange to build reserves, which it would subsequently sterilize to stem money growth and hence, depreciation.

15. The assumption for the financing mix and borrowing terms are in line with the Malawi's Medium-Term Debt Management Strategy (MTDS) which aims to gradually reduce short-term debt. The financing mix assumptions are as follows:

- ***External borrowing***. The baseline assumes no nonconcessional external borrowing. Concessional borrowing is assumed to remain elevated in the near term (about 2½ percent of GDP) but will decline to about 1½ percent of GDP by the end of the medium term. The envisaged concessional borrowing path assumes that sizeable grants would be mobilized through contributions to the Multi-Donor Trust Fund (MDTF) and IDA operations including prospective Development Policy Operations (Box 2 and Text Table 4). New financing in 2022 is assumed from the IMF conditional on the approval of the RCF.

- ***Domestic borrowing***. The baseline assumes the remaining financing gap will be picked up by domestic bank and nonbank institutions. Outstanding domestic debt is projected to increase from 37.7 percent of GDP in 2022 to 42.2 percent of GDP in 2027, and will decrease henceforth. The composition of government securities issuances is assumed to be as follows: 15 percent in Treasury bills and the rest in Treasury notes, ranging in tenor from 2 years to 6 years. The interest rates of the different tenors of government securities are assumed to move along with the policy rate. They are projected to range from 19 percent for Treasury bills to 22.5 percent for 6-year Treasury Notes in 2022.

  Given the size of projected fiscal deficits, net domestic borrowing averages about 4 percent of GDP each year during the medium term. The interest rate for the 3-year bond and the 10-year bond are assumed at 17½ percent and 22½ percent respectively. New bond issuance will move gradually towards longer maturities. The share of bonds with a maturity greater than 7 years is expected to increase from 5 percent of new issuances to 15 percent by 2042.

Box 2. Malawi: IDA Operations, 2022 and Beyond

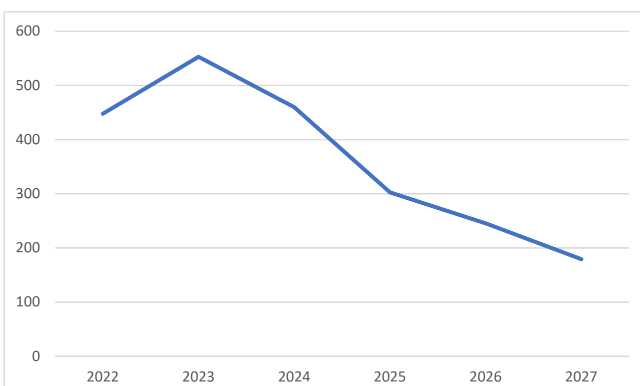
IDA is the major financier of on-budget development assistance in Malawi, aligned with the ambitious goals of Malawi Vision 2063. Total net flows during 2022-27 are anticipated to be more than $2 billion (Box Figure 1). IDA20, covering FY23-25, (which will be on grant terms) will include fast-disbursing operations that protect the poorest and support an inclusive and sustainable recovery.

Protecting the vulnerable and essential services. First, to strengthen Malawi's social protection during an acute 2022/23 lean-season the *Social Support for Resilient Livelihoods Project (SSRLP)* is already expanding a climate-smart public works program nationally to build resilience and livelihoods while facilitating the downscaling of the costly fertilizer subsidy program. IDA will also scale up the operation's shock-response instrument through an additional financing of $160 million. Second, IDA is preparing a $100 million *Emergency Operation to Protect Essential Health Services* which will bolster frontline services and essential medicines in the face of a rapidly escalating national cholera outbreak.

Promoting inclusive growth. IDA's Country Partnership Framework FY21-25 has a strong focus on commercial agriculture and energy access. Tapping into the new Food Systems Resilience Multi Phased Approach, IDA will provide a $250 million to scale up Malawi's successful *Agricultural Commercialization and Resilience Enhancement (AGCOM) program* providing financial and technical support directly to productive farmer groups with off-taker agreements. On energy, IDA's is financing the emergency rehabilitation of the Kapichira Hydropower Station while the World Bank Group is the key financier in the planned Mpatamanga Public Private Partnership which will enable Malawi to sell power into the Southern Africa Power Pool and restore critical baseload to catalyze more independent power producers to invest in solar. Complementing IDA investments, the prospective World Bank DPOs would aim to support Malawi to address longstanding weaknesses in public financial management, strengthen its fiscal position, promote agricultural growth, and improve resilience against shocks. The first DPO ($80 million) in a series of two prospective operations is expected in 2023.

IDA Net Inflows to Malawi, 2022–27

(Millions of U.S. dollars)



16. The projected external financing gap for the next 12 months is US$841 million (about 7 percent of GDP). The envisaged burden sharing/financing mix is spread across different sources. It includes debt treatment, concessional loans and grants. Debt relief is projected to close 47 percent of the financing gap (Text Table 4).

Text Table 4. Malawi: Financing Gap, 2022Q4–2023Q4[1]

(Millions of U.S. Dollars)

	Next 12 months	
	mil US$	% of total
Financing Gap	841	100
Prospective Debt relief	396	47
Prospective RCF	88	10
Prospective Grants	318	38
IDA	238	
MDTF and Other Support	80	
Residual Gap	39	5

[1]Grants figures are preliminary and further discussions are ongoing. Tentative donors for the Multi-Donor Trust Fund are EU, US, UK, AfDB, Ireland, and Germany.

Sources: Malawian authorities; and IMF staff estimates.

REALISM OF THE BASELINE ASSUMPTIONS

17. The realism tools suggest that the baseline scenario is credible compared to Malawi's historical experience and cross-country experiences (Figures 3 and 4).

- The left-hand side panels of Figure 3 show the ***evolution*** of projections of external and public debt to GDP ratios for the current DSA, the previous DSA (the November 2021 DSA), and the DSA from 5 years ago. The current DSA reflects the reform program of the authorities before the implementation of the debt restructuring strategy that brings debt to a sustainable path. Both external debt (as percent of GDP) and public debt (as percent of GDP) will peak and descend on a downward trajectory in the medium term. The difference between the current DSA and the previous DSA is large for the reasons discussed above (¶6).

- ***Debt-creating flows*** charts (middle panel) show that increased contribution of the nominal interest rate over the 5-year projected change, reflecting the compositional changes in external debt (¶4). In the past five years, the primary deficit was the largest contributor to public debt accumulation. During the program, the contribution of the primary deficit has been largely reduced due to the fiscal adjustments incorporated in the baseline. Meanwhile, the contribution of real exchange rate depreciation has risen because of the impact of the exchange rate devaluation on the local currency value of foreign currency denominated debt.

- The ***unexpected*** increases in PPG external debt and public debt (right-hand side panels of Figure 3) are about 13.1 and 36.5 percent of GDP, respectively, which are both above the median of the countries producing LIC DSF. The driver of the unexpected external debt accumulation is the unexpected increase in the current account deficit. Unexpected increase in the primary deficit and real interest rate drives unexpected public debt accumulation.

18. Ambitious improvement in the primary balance in the next three years is in the top quartile of historical data on LIC adjustment programs (Figure 4). The second DSF realism tool assesses the realism of the fiscal projection. The top-left panel of Figure 4 highlights the anticipated adjustment in the primary balance of 4.9 percentage points of GDP in the next three years. The top-right panel of Figure 4 shows that growth projection for 2022 is in line with what is suggested by the fiscal multiplier realism tool. The projection in 2023 is optimistic and assumes the authorities' reform policies yield good results. The bottom two panels reflect the authorities' plan to ramp up public investment to generate growth. The bottom right panel shows the downward revision in Malawi's medium term real economic growth projection, taking into consideration Malawi's vulnerability to recurrent natural disasters amid climate change.

COUNTRY CLASSIFICATION AND MODEL SIGNAL

19. Malawi's debt-carrying capacity based on the Composite Indicator (CI) is assessed as weak (Text Table 5).[7] The CI is determined by the World Bank's CPIA and other variables informed by 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 based on the current vintage (2021 CPIA) remains 'weak' with a CI score of 2.34. In addition, Malawi is classified as having "weak quality of debt monitoring"

Text Table 5. Malawi: Composite Index

Debt Carrying Capacity	Weak

Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintage
Weak	Weak 2.34	Weak 2.56	Weak 2.57

Calculation of the CI Index

Components	Coefficients (A)	10-year average values (B)	CI Score components (A*B) = (C)	Contribution of components
CPIA	0.385	3.196	1.23	53%
Real growth rate (in percent)	2.719	4.107	0.11	5%
Import coverage of reserves (in percent)	4.052	16.332	0.66	28%
Import coverage of reserves^2 (in percent)	-3.990	2.667	-0.11	-5%
Remittances (in percent)	2.022	1.564	0.03	1%
World economic growth (in percent)	13.520	3.050	0.41	18%
CI Score			2.34	100%
CI rating			Weak	

[7] The CI captures the impact of the different factors through a weighted average of the World Bank's 2020 Country Policy and Institutional Assessment (CPIA) score, the country's real GDP growth, remittances, international reserves, and world growth. A country's debt-carrying capacity would be assessed as weak if its CI value is below 2.69, medium if it lies between 2.69 and 3.05, and strong if it is above 3.05.

in line with the country's debt-recording capacity. The four external debt burden thresholds and the total public debt benchmark are determined by this classification of the debt carrying capacity (Text Figure 6).

Text Table 6. Malawi: Debt Carrying Capacity and Thresholds

EXTERNAL debt burden thresholds	Weak	Medium	Strong
PV of debt in % of			
Exports	140	180	240
GDP	30	40	55
Debt service in % of			
Exports	10	15	21
Revenue	14	18	23

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

SCENARIO STRESS TESTS

20. Standard scenarios stress test and a contingent liability stress test are conducted (Text Table 1, and Tables 3 and 4). A stress test combined contingent liabilities of a one-time debt shock (equivalent to 10 percent of GDP) in 2021, to capture the potential impact of limited public debt coverage (2 percent of GDP, instead of the default level of zero), contingent liabilities due to foreign exchange swaps, and contingent liabilities from SOEs[12] (equivalent to 2 percent of GDP) and the need to for bank recapitalization.[13]

21. A second tailored scenario presented is a commodity price shock (Tables 3 and 4). Given the high share of Malawi's tobacco exports in total exports (goods and services) of more than 50 percent over the previous three-year period, the DSA also conducts a stress test where commodity exports are shocked by a commodity price gap in the second year of projection, which converges to the baseline in 6 years.[14] A decline in exports to a level equivalent to one standard

[12] The SOE external liability is identified based on a Fund staff survey conducted in 2016.

[13] The need for bank recapitalization is equivalent to the default level of 5 percent of GDP to the average cost to the government of a financial crisis in a low-income country since 1980.

[14] The price gap is defined as the difference between the baseline commodity price in the second year of projection and the lower end of the 68 percent confidence interval from the IMF's commodity price forecast distribution for fuel and nonfuel commodities which may be found at IMF Primary Commodity Prices. The size and duration of these responses were informed by the analysis of episodes of commodity price busts in a sample of 34 commodity-intensive LICs during 1990-2015. The elasticities are within the range of estimates found in the literature (e.g., Spatafora and Samake, 2012. "Commodity Price Shocks and Fiscal Outcomes," IMF Working Paper No. 12/112; and Cespedes and Velasco, 2013. "Was This Time Different? Fiscal Policy in Commodity Republics," NBER Working Paper No. 19748).

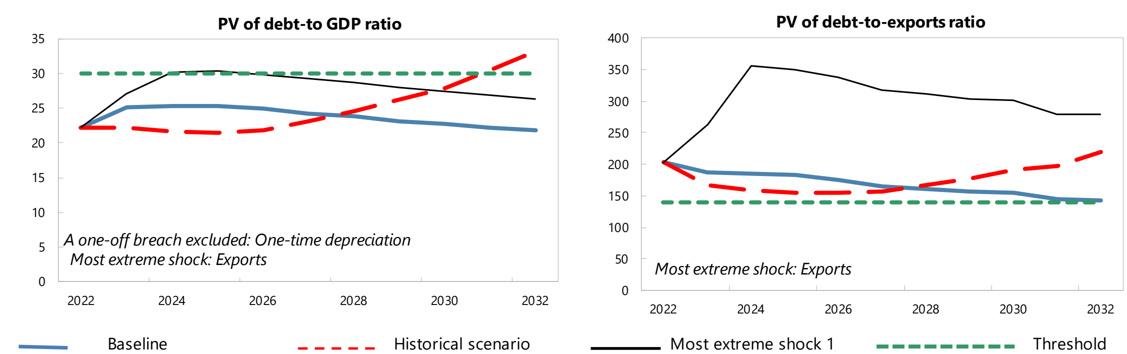
deviation below their historical average in the second and third years of the projection period would cause the debt-service-to-exports ratio and PV of debt-to-GDP to remain elevated exceeding the baseline projections over the medium term.

EXTERNAL DSA

22. Malawi's overall and external public debt are assessed to be in debt distress, as this DSA presents to a pre-restructuring scenario. Malawi's sustained threshold breaches on a number of debt stock and debt service indicators will continue in the medium term, highlighting the severity of external debt distress. The baseline scenario incorporates the authorities' reforms; but without the debt restructuring strategy described in Box 1, public debt would increase further from 64 percent of GDP in 2021 to 76.6 percent of GDP in 2022, and external debt would reach 38.9 percent of GDP in 2022. The stock indicators, the PV of PPG external debt to GDP ratio and the PV of external debt to export ratio, stay below or reach the threshold during the medium term. However, the PV of PPG external debt to export ratio would remain substantially above the threshold if the residual financing gap were to be financed externally (Box 3). Moreover, the flow indicators, the external debt service to revenue ratio and the external debt service to export ratio, notably indicate that without debt restructuring, Malawi would face an enormous debt service burden in the near term—the external debt service to exports ratio is 56 percent in 2022 and 27 percent in 2023, and the debt service-to-revenue ratio is 43 percent in 2022 and 25 percent in 2023.

Box 3. Malawi: Illustrative Scenario Without Debt Restructuring

In the absence of a debt restructuring, the authorities have to meet large debt services need. Repayment of contracted external debt under the original terms would imply declining external debt stocks but with a large financing gap. The pre-restructuring scenario assumes domestic financing of that residual. If that residual were to be financed externally (including through arrears), it would lead to a sustained breach of the debt-to-export ratio indicator over the medium term.



23. The stress scenarios highlight Malawi's debt is vulnerable to any shocks in exports and the exchange rate. The historical scenario, which assumes that real GDP growth, the primary balance-to-GDP ratio, the GDP deflator, the noninterest current account, and net FDI flows permanently remain at their historical averages, indicates that the baseline adopts policies that brings debt ratios on a descending path. Various stress test scenarios presented in Figure 1 show that Malawi's debt is vulnerable to shocks in exports (see the PV debt to export ratio and the debt service to export ratio), those in the exchange rate (see the debt service to revenue ratio and the PV debt to GDP ratio).

PUBLIC DSA

24. Malawi's overall public debt is assessed to be in distress—the PV of public debt-to-GDP ratio remains above the threshold over time (Figure 2). Total public debt in the medium term is projected to take a downward path but remains above the threshold in the medium and long term in the baseline scenario. While the historical scenarios also do not decline to reach threshold in the medium term, fiscal reforms enable public debt ratios go down earlier compared to the baseline scenario. The PV public debt-to-GDP ratio peaks at 66 percent in 2022, the PV of public debt-to-revenue and grants ratio reaches 405 percent in 2022 and the debt service-to-revenue and grants ratio reaches 118 percent in 2022. These numbers point to the severity of the debt burden on the economy. There are many factors contributing to the situation: Malawi's inability to sustain growth, partly due to frequent weather-related shocks; high cost of sovereign borrowing; weak macroeconomic management/governance; and the high level of existing debt with a large fraction being on nonconcessional term.

RISK RATING AND VULNERABILITIES

25. Malawi's external and public debt is in debt distress and granularity in risk rating assesses that public debt under current policies is unsustainable. The assessment reflects the significant debt vulnerabilities emanating from the large and sustained breaches on the PV public debt to GDP, PV external debt to export, external debt service to export, and external debt service to revenue ratios during the entire medium term.

26. Risks to the ratings assessment remain significant on several fronts. Reducing Malawi's macroeconomic vulnerabilities requires a sizeable debt operation, which is risky, including due to potential delays in obtaining financing assurances especially from bilateral official creditors and comprehensive collateralization of the borrowing from AFREXIM bank. Additional risks stem from possible delays in cash management and commitment controls that are envisaged under the program could derail fiscal consolidation effort and add to the deep-rooted governance vulnerabilities. The RBM's program to scale up foreign exchange purchases and reducing swap arrangements and or costly short-term trade credits could face delays, jeopardizing the reserve accumulation path. Climate shocks represent an additional risk. Lack of monetary tightening could prolong the period of price instability and excessive exchange rate volatility. Loss of market confidence could result in drawdown on foreign exchange deposits, capital flight, resulting in a worsening of foreign exchange liquidity. Mitigating factors include: significant fiscal tightening, the

RBM's strong commitment for further efforts for greater flexibility in the foreign exchange market, and the authorities' implementing recommendations from the special audit, and the 2021 safeguards assessment along with undertaking a proposed governance diagnostic exercise. Staff also see that further restraining nominal wage growth while fully utilizing an increase in revenue (inflation tax) could be a fiscal contingency measure.

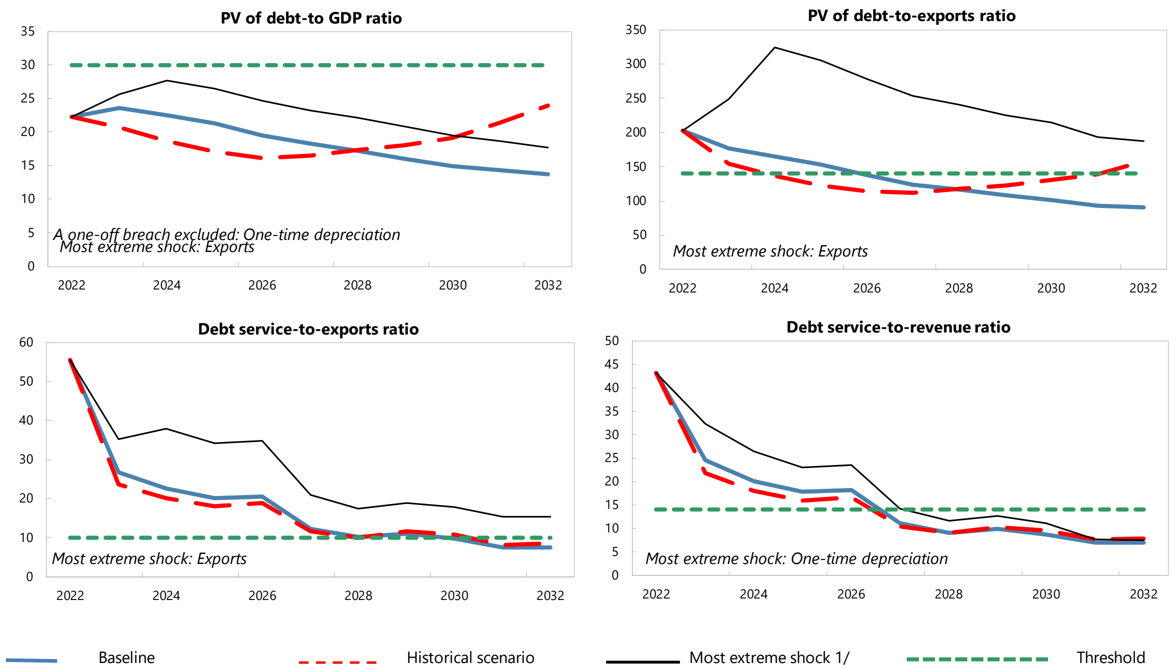
27. The authorities' commitment to macroeconomic adjustment, in conjunction with debt restructuring, is the only channel for Malawi to return to moderate risk of debt distress in the medium term. A strong commitment to fiscal discipline to contain fiscal deficits and public debt would require reforming the AIP and realism in budget forecasts and public financial management (PFM) reforms. This needs to be supported by strengthening public sector governance and institutions to help safeguard scarce resources and strengthen policy effectiveness, as envisaged in MEFPs. The RBM's financing of the government and external nonconcessional borrowing should not be undertaken. In this regard, given that Malawi's external position is assessed to be substantially weaker than the level implied by economic fundamentals and desirable policies, allowing for greater flexibility in the exchange rate along with a well-functioning and transparent foreign exchange interbank market development and a foreign exchange reserve management strategy are crucial. To help guide policy directions, the authorities need to improve further fiscal, monetary, and external sector data compilation and reporting.

28. The authorities are committed to significant structural reforms and policies to support inclusive growth and increase diversification outside of agriculture. Enhancement in productivity, value addition, and job creation should lead to stronger growth, larger fiscal buffers and resilience to external shocks. Addressing a narrow production base through structural reforms is critical, especially given the absence of fiscal space and tight monetary conditions. Well targeted and more cost-efficient subsidy programs for the agriculture sector, along with well-tailored reforesting and climate adaptation plans, should reduce fiscal risks, safeguard food security, and help weather external and climate shocks. This also requires expanding reliable access to electricity, including sustainable energy investment projects. All these call for addressing informality, boosting the business environment and raising competitiveness through measures such as tax reforms and stronger governance in key sectors. The World is supporting Malawi in addressing longstanding weaknesses in public financial management, strengthening its fiscal position, promoting agricultural commercialization, and improving resilience against shocks.

AUTHORITIES' VIEWS

29. The authorities are in broad agreement with the WB's and IMF's staff assessments. The authorities are determined to take bold policy action and have recently reiterated their request for an ECF arrangement. The proposed PMB would aim to: (i) restore macroeconomic stability, including debt sustainability; (ii) address weaknesses in governance; and (iii) build the foundation for sustainable and inclusive growth. Restoring macroeconomic stability will require political commitment to strong fiscal and external adjustment accompanied by a debt treatment. The Fund program would catalyze support from the international community, which would be essential given Malawi's immediate financing needs which are best met through grants and nondebt creating flows. Addressing weaknesses in governance will focus on enhancing transparency and accountability of public financial management and foreign exchange management of the Reserve Bank of Malawi. This reform agenda will reflect inputs from the Safeguards Assessment Report completed in December 2021.

Figure 1. Malawi: Indicators of Public and Publicly Guaranteed External Debt Under Baseline (Pre-debt restructuring) Scenarios, 2022–32



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	Yes	
Natural disaster	n.a.	n.a.
Commodity price	No	No
Market financing	n.a.	n.a.

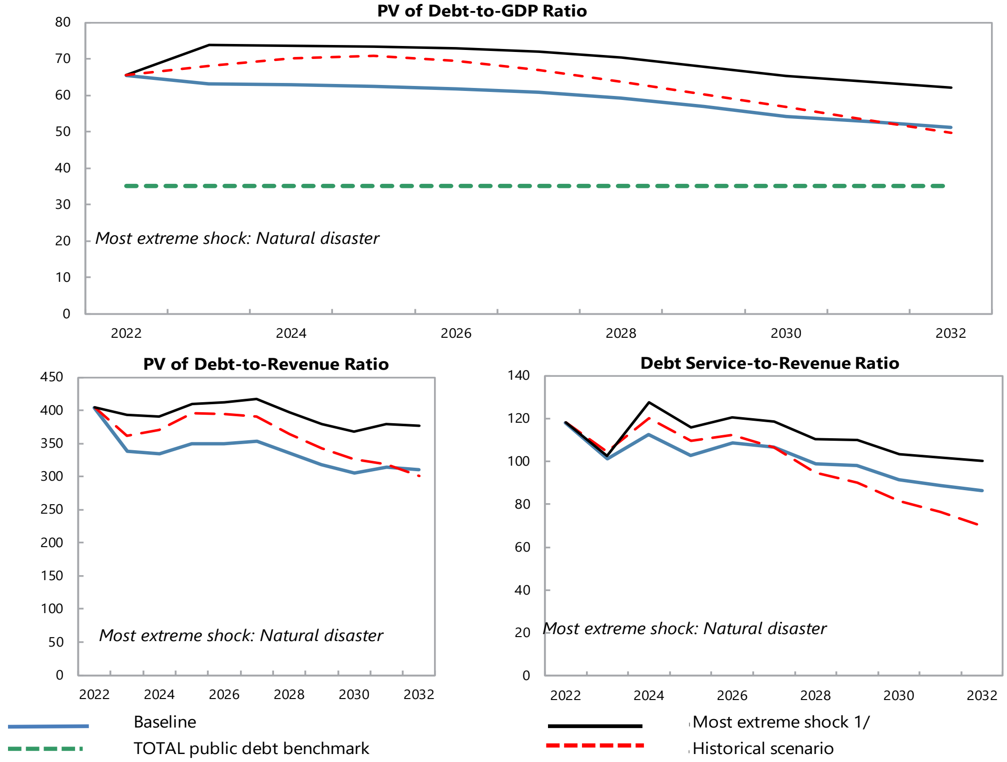
Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing assumptions on additional financing needs resulting from the 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	0.8%	0.8%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	34	34
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 2032. 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.
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, FY2022–32



Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	10%	10%
Domestic medium and long-term	76%	76%
Domestic short-term	13%	13%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	0.8%	0.8%
Avg. maturity (incl. grace period)	34	34
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	5.1%	3.0%
Avg. maturity (incl. grace period)	4	10
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	1.7%	1.7%

* 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.

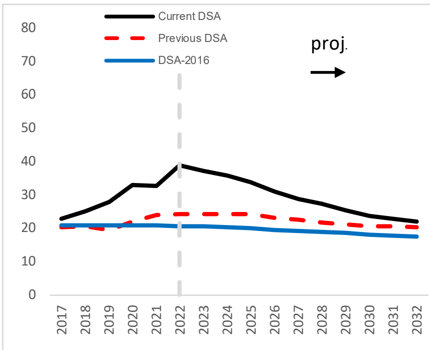
Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2032. 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.

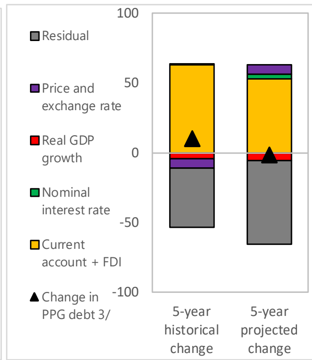
Figure 3. Malawi: Indicators of Public Debt Under Alternative Scenarios, FY2021–32

External debt

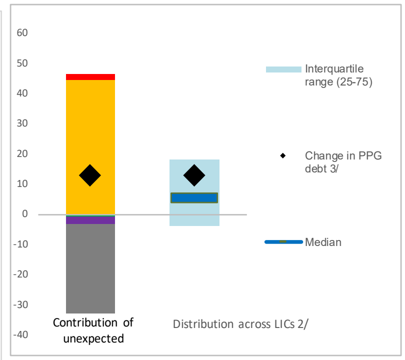
Gross Nominal PPG External Debt
(in percent of GDP; DSA vintages)



Debt-creating flows
(percent of GDP)

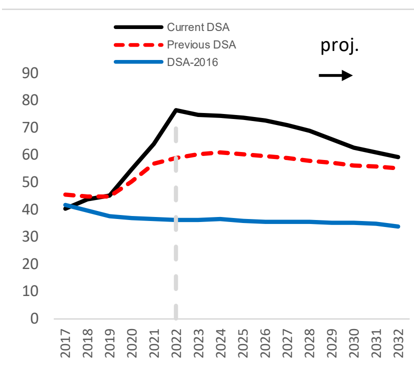


Unexpected Changes in Debt 1/
(past 5 years, percent of GDP)

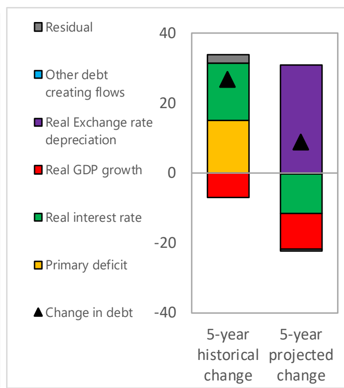


Public debt

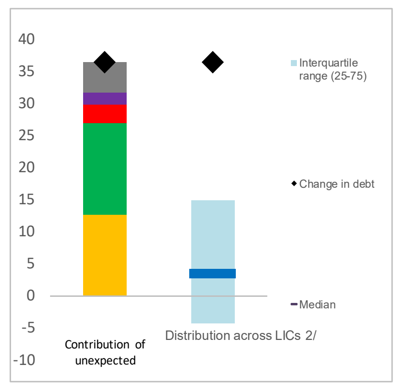
Gross Nominal Public Debt
(in percent of GDP; DSA vintages)



Debt-creating flows
(percent of GDP)



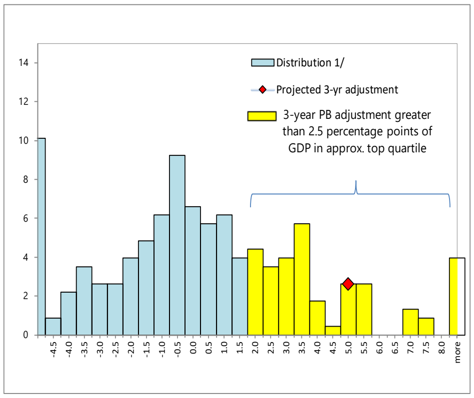
Unexpected Changes in Debt 1/
(past 5 years, percent of GDP)



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.

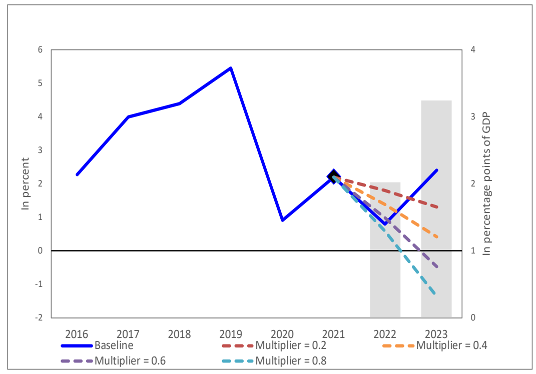
Figure 4. Malawi: Realism Tools

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



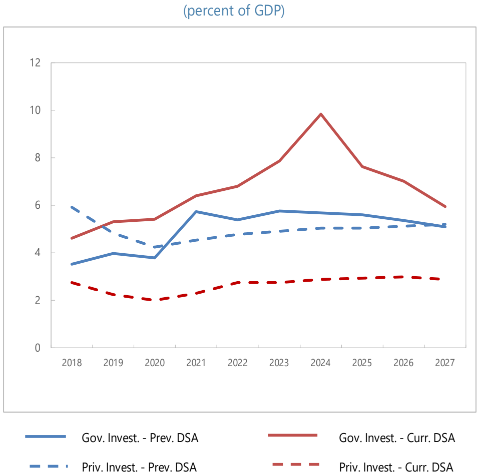
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

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
(percent of GDP)



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

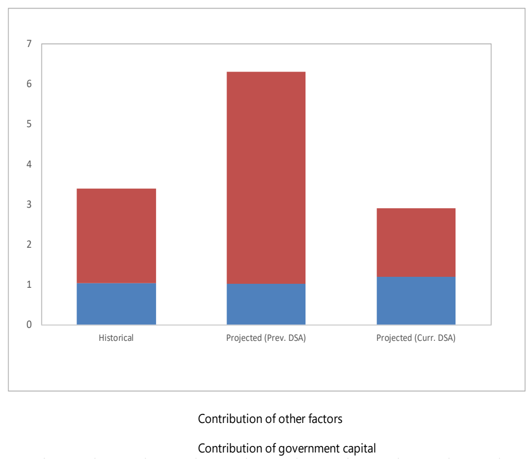
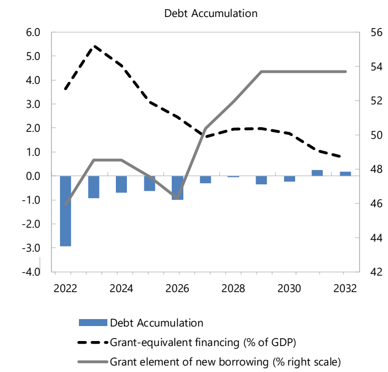


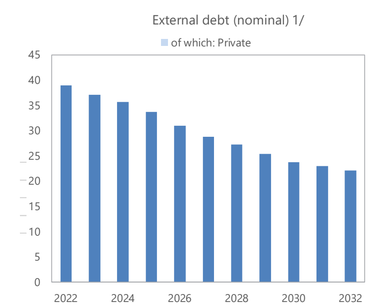
Table 1. Malawi: External Debt Sustainability Framework, Baseline Scenario, FY 2019–42*

(Percent of GDP, Unless Otherwise Indicated)

	Actual			Projections								Average 8/	
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2032	2042	Historical	Projections
External debt (nominal) 1/	27.8	32.9	32.8	38.9	37.1	35.6	33.6	30.9	28.8	22.1	15.0	24.8	29.7
of which: public and publicly guaranteed (PPG)	27.8	32.9	32.8	38.9	37.1	35.6	33.6	30.9	28.8	22.1	15.0	24.8	29.7
Change in external debt	2.9	5.1	-0.1	6.1	-1.8	-1.5	-2.0	-2.7	-2.1	-0.8	-0.7		
Identified net debt-creating flows	9.0	10.9	12.9	13.1	9.1	11.3	10.0	7.7	6.8	4.3	3.0	9.1	7.7
Non-interest current account deficit	12.6	13.6	14.3	13.2	10.5	13.1	12.2	10.2	9.3	7.0	5.6	11.2	9.9
Deficit in balance of goods and services	16.7	17.6	16.6	17.9	16.5	16.8	15.5	13.7	12.1	9.9	8.9	14.3	13.3
Exports	10.8	8.2	10.5	11.0	13.4	13.7	13.9	14.2	14.7	15.2	11.5		
Imports	27.6	25.8	27.1	28.9	29.9	30.5	29.4	27.8	26.8	25.1	20.5		
Net current transfers (negative = inflow)	-5.8	-5.6	-5.3	-6.2	-7.7	-5.6	-5.2	-5.4	-4.7	-4.7	-5.0	-4.9	-5.3
of which: official	-0.4	-0.4	0.0	-0.6	-2.4	-0.7	-0.5	-0.7	0.0	0.0	0.0		
Other current account flows (negative = net inflow)	1.7	1.5	2.9	1.5	1.8	1.8	1.9	1.9	1.9	1.8	1.7	1.8	1.8
Net FDI (negative = inflow)	-1.0	-0.8	-0.8	-0.8	-1.0	-1.2	-1.3	-1.4	-1.5	-1.9	-2.1	-1.5	-1.5
Endogenous debt dynamics 2/	-2.7	-1.9	-0.6	0.7	-0.4	-0.6	-0.9	-1.1	-1.1	-0.8	-0.6		
Contribution from nominal interest rate	0.0	0.0	0.3	1.0	0.6	0.5	0.4	0.3	0.2	0.2	0.1		
Contribution from real GDP growth	-1.2	-0.2	-0.7	-0.3	-1.0	-1.2	-1.3	-1.4	-1.3	-1.0	-0.7		
Contribution from price and exchange rate changes	-1.4	-1.7	-0.2	...	...	...	...	...	...	...	...		
Residual 3/	-6.1	-5.8	-13.0	-7.0	-10.9	-12.7	-12.0	-10.4	-8.9	-5.1	-3.7	-6.7	-8.7
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	...	...	24.8	22.2	23.6	22.5	21.3	19.5	18.2	13.7	9.1		
PV of PPG external debt-to-exports ratio	...	...	235.5	202.3	176.6	164.9	153.3	137.7	124.0	90.2	79.1		
PPG debt service-to-exports ratio	0.0	0.0	6.4	55.6	26.7	22.7	20.2	20.6	12.2	7.6	6.1		
PPG debt service-to-revenue ratio	0.0	0.0	4.9	43.2	24.6	20.2	17.8	18.3	11.1	6.9	7.1		
Gross external financing need (Billion of U.S. dollars)	1.3	1.5	1.8	2.2	1.4	1.6	1.5	1.4	1.2	1.0	1.2		
Key macroeconomic assumptions													
Real GDP growth (in percent)	5.4	0.9	2.2	0.8	2.4	3.2	3.8	4.3	4.5	4.6	4.6	3.5	3.8
GDP deflator in US dollar terms (change in percent)	5.9	6.4	-0.9	-2.6	-12.0	-1.4	-0.9	-0.3	0.9	1.2	1.3	-2.0	-1.0
Effective interest rate (percent) 4/	0.0	0.0	1.0	3.0	1.5	1.4	1.2	1.0	0.8	0.8	0.8	0.1	1.2
Growth of exports of G&S (US dollar terms, in percent)	7.6	-19.2	30.6	2.6	9.8	3.9	4.5	6.1	9.4	4.0	3.8	0.3	6.2
Growth of imports of G&S (US dollar terms, in percent)	12.8	0.3	6.7	4.6	-6.8	3.7	-0.8	-1.5	1.4	4.1	3.5	4.0	2.0
Grant element of new public sector borrowing (in percent)	...	...	...	45.9	48.5	48.5	47.6	46.3	50.4	...	...	...	...
Government revenues (excluding grants, in percent of GDP)	13.1	12.8	13.7	14.1	14.5	15.4	15.8	16.0	16.2	16.5	10.0	13.1	15.9
Aid flows (in Billion of US dollars) 5/	0.3	0.4	0.4	0.5	0.6	0.5	0.4	0.3	0.2	0.2	0.2		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	3.6	5.4	4.6	3.1	2.5	1.6	0.7	0.4	...	2.6
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	66.3	80.6	78.6	73.8	72.3	73.4	53.7	53.7	...	72.3
Nominal GDP (Billion of US dollars)	11	12	12	12	11	11	11	12	12	16	29		
Nominal dollar GDP growth	11.6	7.4	1.3	-1.9	-9.9	1.8	2.8	3.9	5.4	5.9	5.9	1.5	2.8
Memorandum items:													
PV of external debt 7/	...	...	24.8	22.2	23.6	22.5	21.3	19.5	18.2	13.7	9.1		
In percent of exports	...	...	235.5	202.3	176.6	164.9	153.3	137.7	124.0	90.2	79.1		
Total external debt service-to-exports ratio	0.0	0.0	14.4	55.6	26.7	22.7	20.2	20.6	12.2	7.6	6.1		
PV of PPG external debt (in Billion of US dollars)			3.0	2.6	2.5	2.4	2.4	2.3	2.2	2.2	2.6		
(PVt-PVt-1)/GDPt-1 (in percent)				-2.9	-0.9	-0.7	-0.6	-1.0	-0.3	0.2	0.1		
Non-interest current account deficit that stabilizes debt ratio	9.7	8.5	14.4	7.0	12.3	14.5	14.2	12.9	11.5	7.9	6.3		

Definition of external/domestic debt	Residency-based
Is there a material difference between the two criteria?	Yes





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) + Εα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ε=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

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.

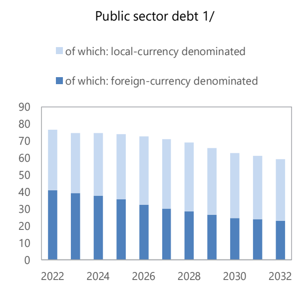
* Residual calculation does take into account another large nondebt creating inflow factor, net official transfers for "capital" spending (capital account balance). Once it is taken into account, residual goes down to 6.9 percent of GDP over 6 years.

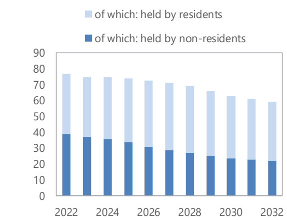
Table 2. Malawi: Public Sector Debt Sustainability Framework, Baseline Scenario, FY2019–42

(Percent of GDP, Unless Otherwise Indicated)

	Actual			Projections								Average 6/	
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2032	2042	Historical	Projections
Public sector debt 1/	**45.3**	**54.8**	**64.0**	**76.6**	**74.6**	**74.5**	**73.8**	**72.6**	**71.0**	**59.3**	**44.6**	**41.8**	**69.2**
of which: external debt	**27.8**	**32.9**	**32.8**	**38.9**	**37.1**	**35.6**	**33.6**	**30.9**	**28.8**	**22.1**	**15.0**	**24.8**	**29.7**
Change in public sector debt	1.4	9.5	9.2	12.6	-2.0	-0.1	-0.7	-1.2	-1.6	-1.7	-1.2		
Identified debt-creating flows	**1.4**	**8.8**	**7.2**	**-1.8**	**-8.4**	**-5.0**	**-3.9**	**-2.8**	**-2.7**	**-2.6**	**-2.1**	**2.8**	**-3.7**
Primary deficit	**1.5**	**5.0**	**4.8**	**2.7**	**-0.5**	**-0.2**	**-0.9**	**-1.5**	**-1.7**	**-0.8**	**-0.6**	**2.1**	**-1.0**
Revenue and grants	14.8	14.5	15.6	16.2	18.7	18.8	17.8	17.7	17.2	16.5	10.0	**15.6**	**17.6**
of which: grants	1.7	1.8	1.9	2.1	4.2	3.4	2.1	1.6	1.0	0.0	0.0		
Primary (noninterest) expenditure	16.3	19.5	20.4	18.9	18.2	18.6	17.0	16.2	15.5	15.7	9.4	**17.6**	**16.5**
Automatic debt dynamics	**-0.1**	**3.9**	**2.4**	**-4.5**	**-7.9**	**-4.9**	**-3.0**	**-1.3**	**-1.0**	**-1.8**	**-1.5**		
Contribution from interest rate/growth differential	-0.1	3.9	2.4	-4.5	-7.9	-4.9	-3.0	-1.3	-1.0	-1.8	-1.5		
of which: contribution from average real interest rate	2.2	4.3	3.6	-4.0	-6.1	-2.5	-0.3	1.8	2.2	0.9	0.6		
of which: contribution from real GDP growth	-2.3	-0.4	-1.2	-0.5	-1.8	-2.3	-2.7	-3.0	-3.1	-2.7	-2.1		
Contribution from real exchange rate depreciation	0.0	0.0	0.0	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	**0.0**	**0.0**	**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	0.0	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	**0.0**	**0.6**	**2.0**	**14.4**	**6.4**	**5.0**	**3.2**	**1.6**	**1.1**	**0.9**	**0.8**	**1.6**	**3.3**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	**...**	**...**	**56.5**	**65.5**	**63.2**	**63.0**	**62.5**	**61.8**	**60.9**	**51.2**	**38.9**		
PV of public debt-to-revenue and grants ratio	**...**	**...**	**361.2**	**404.5**	**337.8**	**334.8**	**350.1**	**350.0**	**353.4**	**310.5**	**390.6**		
Debt service-to-revenue and grants ratio 3/	**18.4**	**18.5**	**21.6**	**118.0**	**101.4**	**112.7**	**102.8**	**108.6**	**106.6**	**86.5**	**99.7**		
Gross financing need 4/	4.2	7.7	8.1	21.9	18.5	21.0	17.4	17.7	16.7	13.5	9.3		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	5.4	0.9	2.2	0.8	2.4	3.2	3.8	4.3	4.5	4.6	4.6	**3.5**	**3.8**
Average nominal interest rate on external debt (in percent)	0.0	0.0	0.6	3.1	1.9	1.6	1.3	1.1	0.9	0.8	0.8	**0.1**	**1.3**
Average real interest rate on domestic debt (in percent)	5.2	9.5	6.8	0.4	0.3	5.8	8.5	10.5	9.8	5.4	4.8	**4.7**	**6.4**
Real exchange rate depreciation (in percent, + indicates depreciation)	1.0	4.0	5.9	...	...	...	...	...	...	...	...	**20.4**	**...**
Inflation rate (GDP deflator, in percent)	7.7	6.3	6.5	17.3	20.6	15.3	11.3	7.6	6.3	5.8	5.8	**14.7**	**9.8**
Growth of real primary spending (deflated by GDP deflator, in percent)	3.1	21.2	6.7	-6.4	-1.6	5.5	-5.5	-0.6	0.4	4.1	-3.2	**6.9**	**1.5**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	0.1	-4.5	-4.4	-9.9	1.5	-0.1	-0.2	-0.3	-0.1	0.9	0.67	**-2.9**	**-0.6**
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	**Residency-based**
Is there a material difference between the two criteria?	**Yes**





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 Residency-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 PPG External Debt, FY2022–32
(Percent)

	Projections 1/										
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
PV of debt-to GDP ratio											
Baseline	22	24	23	21	20	18	17	16	15	14	14
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	22	21	19	17	16	16	17	18	19	21	24
B. Bound Tests											
B1. Real GDP growth	22	24	24	22	21	19	18	17	16	15	14
B2. Primary balance	22	24	23	22	20	19	18	17	16	15	15
B3. Exports	22	26	28	26	25	23	22	21	20	19	18
B4. Other flows 3/	22	26	26	25	23	22	21	20	18	17	17
B5. Depreciation	22	**31**	25	24	21	20	18	17	15	15	14
B6. Combination of B1-B5	22	26	25	24	22	21	20	19	17	17	16
C. Tailored Tests											
C1. Combined contingent liabilities	22	24	23	22	20	19	18	17	16	15	15
C2. Natural disaster	22	25	24	22	21	20	19	17	16	16	15
C3. Commodity price	22	24	23	21	20	18	17	16	15	14	14
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	**202**	**177**	**165**	**153**	138	124	117	108	102	93	90
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	**202**	**155**	136	123	114	112	117	122	131	139	**158**
B. Bound Tests											
B1. Real GDP growth	**202**	**177**	**165**	**153**	138	124	117	108	102	93	90
B2. Primary balance	**202**	**178**	**168**	**157**	**142**	129	122	113	108	98	96
B3. Exports	**202**	**249**	**325**	**306**	**279**	**254**	**241**	**225**	**214**	**194**	**188**
B4. Other flows 3/	**202**	**194**	**192**	**180**	**164**	**149**	**141**	132	125	113	110
B5. Depreciation	**202**	**177**	**142**	130	115	102	95	87	81	74	73
B6. Combination of B1-B5	**202**	**238**	**187**	**238**	**216**	**196**	**185**	**173**	**163**	**148**	**144**
C. Tailored Tests											
C1. Combined contingent liabilities	**202**	**181**	**170**	**159**	**144**	130	123	115	109	100	98
C2. Natural disaster	**202**	**187**	**175**	**164**	**149**	135	128	119	114	105	103
C3. Commodity price	**202**	**177**	**165**	**153**	138	124	117	108	102	93	90
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	**56**	**27**	**23**	**20**	**21**	**12**	**10**	**11**	10	8	8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	**56**	**24**	**20**	**18**	**19**	**12**	**10**	**12**	**11**	8	9
B. Bound Tests											
B1. Real GDP growth	**56**	**27**	**23**	**20**	**21**	**12**	**10**	**11**	10	8	8
B2. Primary balance	**56**	**27**	**23**	**20**	**21**	**12**	**10**	**11**	**10**	8	8
B3. Exports	**56**	**35**	**38**	**34**	**35**	**21**	**17**	**19**	**18**	**15**	**15**
B4. Other flows 3/	**56**	**27**	**23**	**21**	**21**	**13**	**11**	**11**	**11**	9	9
B5. Depreciation	**56**	**27**	**23**	**20**	**20**	**12**	10	**11**	10	6	6
B6. Combination of B1-B5	**56**	**32**	**31**	**28**	**28**	**17**	**14**	**15**	**15**	**12**	**12**
C. Tailored Tests											
C1. Combined contingent liabilities	**56**	**27**	**23**	**20**	**21**	**12**	**10**	**11**	10	8	8
C2. Natural disaster	**56**	**28**	**24**	**21**	**21**	**13**	**11**	**12**	**10**	8	8
C3. Commodity price	**56**	**27**	**23**	**20**	**21**	**12**	**10**	**11**	10	8	8
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	**43**	**25**	**20**	**18**	**18**	11	9	10	9	7	7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	**43**	**22**	**18**	**16**	**17**	10	9	10	10	8	8
B. Bound Tests											
B1. Real GDP growth	**43**	**25**	**21**	**19**	**19**	12	10	10	9	7	7
B2. Primary balance	**43**	**25**	**20**	**18**	**18**	11	9	10	9	7	7
B3. Exports	**43**	**25**	**21**	**19**	**19**	12	10	11	10	9	9
B4. Other flows 3/	**43**	**25**	**20**	**18**	**19**	11	9	10	10	8	8
B5. Depreciation	**43**	**32**	**26**	**23**	**24**	**14**	12	13	11	8	8
B6. Combination of B1-B5	**43**	**24**	**20**	**18**	**18**	11	9	10	10	8	8
C. Tailored Tests											
C1. Combined contingent liabilities	**43**	**25**	**20**	**18**	**18**	11	9	10	9	7	7
C2. Natural disaster	**43**	**25**	**20**	**18**	**18**	11	9	10	9	7	7
C3. Commodity price	**43**	**25**	**20**	**18**	**18**	11	9	10	9	7	7
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, FY2022–32

(Percent)

	Projections 1/										
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
	PV of Debt-to-GDP Ratio										
Baseline	**66**	**63**	**63**	**62**	**62**	**61**	**59**	**57**	**54**	**53**	**51**
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	**66**	**68**	**70**	**71**	**69**	**67**	**64**	**60**	**57**	**53**	**50**
A2. Alternative Scenario :[Customize, enter title]	**68**	**70**	**74**	**78**	**80**	**81**	**82**	**82**	**82**	**81**	**80**
B. Bound Tests											
B1. Real GDP growth	**66**	**65**	**67**	**68**	**68**	**68**	**67**	**65**	**63**	**62**	**61**
B2. Primary balance	**66**	**67**	**71**	**70**	**70**	**69**	**67**	**64**	**62**	**60**	**58**
B3. Exports	**66**	**65**	**68**	**67**	**66**	**65**	**64**	**61**	**58**	**57**	**55**
B4. Other flows 3/	**66**	**66**	**67**	**66**	**66**	**65**	**63**	**60**	**58**	**56**	**54**
B5. Depreciation	**66**	**63**	**62**	**61**	**59**	**58**	**56**	**53**	**50**	**48**	**46**
B6. Combination of B1-B5	**66**	**65**	**65**	**64**	**63**	**62**	**60**	**57**	**54**	**53**	**51**
C. Tailored Tests											
C1. Combined contingent liabilities	**66**	**73**	**72**	**72**	**71**	**70**	**68**	**66**	**63**	**61**	**59**
C2. Natural disaster	**66**	**74**	**74**	**73**	**73**	**72**	**70**	**68**	**65**	**64**	**62**
C3. Commodity price	**66**	**64**	**62**	**61**	**60**	**59**	**57**	**56**	**54**	**53**	**52**
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.
TOTAL public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
	PV of Debt-to-Revenue Ratio										
Baseline	405	338	335	350	350	353	335	318	306	314	310
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	405	361	371	396	395	391	364	343	327	319	301
A2. Alternative Scenario :[Customize, enter title]	118	94	109	94	99	94	92	95	90	82	80
B. Bound Tests											
B1. Real GDP growth	405	346	355	378	383	393	377	362	354	370	371
B2. Primary balance	405	359	376	393	394	398	378	359	347	357	353
B3. Exports	405	347	360	376	376	379	360	342	329	338	332
B4. Other flows 3/	405	351	356	372	372	375	356	338	325	333	329
B5. Depreciation	405	343	333	343	339	339	318	298	284	287	279
B6. Combination of B1-B5	405	349	345	357	356	358	338	319	307	317	312
C. Tailored Tests											
C1. Combined contingent liabilities	405	388	384	402	402	406	386	367	354	364	360
C2. Natural disaster	405	393	391	410	412	417	398	379	367	380	377
C3. Commodity price	405	340	333	344	341	342	327	314	306	317	317
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	118	101	113	103	109	107	99	98	91	89	87
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	118	105	120	110	112	106	95	90	82	76	70
A2. Alternative Scenario :[Customize, enter title]	118	94	109	94	99	94	92	95	90	82	80
B. Bound Tests											
B1. Real GDP growth	118	103	118	109	116	115	107	107	101	99	98
B2. Primary balance	118	101	118	113	117	115	107	106	99	97	95
B3. Exports	118	101	113	103	109	107	99	98	92	90	88
B4. Other flows 3/	118	101	113	103	109	107	99	98	92	90	88
B5. Depreciation	118	98	109	99	104	101	94	93	86	83	81
B6. Combination of B1-B5	118	99	111	105	109	107	99	98	92	91	88
C. Tailored Tests											
C1. Combined contingent liabilities	118	101	126	114	118	116	108	107	101	99	97
C2. Natural disaster	118	103	128	116	121	119	110	110	104	102	100
C3. Commodity price	118	101	110	99	102	99	92	92	87	85	84
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 benchmark.
2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.
3/ Includes official and private transfers and FDI.

INTERNATIONAL MONETARY FUND

MALAWI

November 14, 2022

REQUEST FOR DISBURSEMENT UNDER THE RAPID CREDIT FACILITY AND REQUEST FOR A STAFF MONITORED PROGRAM WITH EXECUTIVE BOARD INVOLVEMENT—INFORMATIONAL ANNEX

Prepared By

The African Department
(In Consultation with Other Departments, the World Bank, and the African Development Bank)

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FUND RELATIONS

(As of October 31, 2022)

Membership Status

Joined: July 19, 1965; Article VIII

General Resources Account:

	SDR Million	%Quota
Quota	138.80	100.00
Fund holdings of currency (exchange rate)	136.36	98.24
Reserve tranche position	2.44	1.76

SDR Department:

	SDR Million	%Allocation
Net cumulative allocation	199.40	100.00
Holdings	9.75	4.89

Outstanding Purchases and Loans:

	SDR Million	%Quota
RCF Loans	138.75	99.96
ECF Arrangements	129.74	93.47

Latest Financial Commitments:

Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF	04/30/2018	09/24/2020[1]	105.84	53.85
ECF	07/23/2012	06/29/2017	138.80	138.80
ECF	02/19/2010	07/22/2012	52.05	13.88

Outright Loans:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
RCF	10/02/2020	10/06/2020	72.31	72.31
RCF	05/01/2020	05/05/2020	66.44	66.44

[1] The 2018 ECF was cancelled by the authorities on September 24, 2020 as presented in the request in the October 2020 Request for Rapid Credit Financing.

Overdue Obligations and Projected Payments to Fund[1]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	2022	2023	2024	2025	2026
Principal	8.67	22.37	23.11	33.46	47.84
Charges/Interest	0.91	4.71	4.71	4.71	4.71
Total	9.58	27.08	27.82	38.17	52.55

Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	December 2000
Assistance committed	
by all creditors (US$ Million)[1]	1,057.00
Of which: IMF assistance (US$ million)	45.27
(SDR equivalent in millions)	33.37
Completion point date	Aug 2006
Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	33.37
Interim assistance	11.57
Completion point balance	21.80
Additional disbursement of interest income[2]	3.82
Total disbursements	37.19

[1] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

[2] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

Implementation of Multilateral Debt Relief Initiative (MDRI):

MDRI-eligible debt (SDR Million)[1]	37.87
Financed by: MDRI Trust	14.53
Remaining HIPC resources	23.34

Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGF**	**Total**
December 2006	N/A	7.91	7.91
September 2006	10.84	19.12	29.96

[1] The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

Implementation of Catastrophe Containment and Relief (CCR)[1]:

Date of Catastrophe	Board Decision Date	Amount Committed (SDR million)	Amount Disbursed (SDR million)
N/A	04/13/2020	7.20	7.20
N/A	10/02/2020	7.20	7.20
N/A	04/01/2021	7.81	7.81
N/A	10/06/2021	6.72	6.72
N/A	12/15/2021	3.91	3.91

[1] As of February 4, 2015, the Post-Catastrophe Debt Relief Trust has been transformed to the Catastrophe Containment and Relief (CCR) Trust.

Safeguards Assessments:

The 2021 safeguards assessment of the RBM is substantially completed. It found significant deterioration of safeguards at the RBM since the 2018 assessment. Governance arrangements and the internal control environment are considered weak. Governance reform should establish the Board as the RBM's main decision-making body responsible for oversight and policy formulation, and to introduce collegiality in executive management. Amendments of the central bank legal framework are needed to safeguard the central bank's autonomy and enhance collegiality in executive management. The RBM will also need to strengthen management of foreign reserves.

Exchange Arrangements:

In May 2012, the government liberalized the foreign exchange regime, devalued the kwacha by about 33 percent, and adopted a de jure floating exchange rate regime. Since May 2012, the RBM has not set a target rate and allowed substantial volatility in the exchange rate. However, the U.S. dollar exchange rates have shown remarkable stability since October 2016. Accordingly, the de facto exchange rate arrangement is classified as "stabilized". Inflows of foreign exchange and swap arrangements have allowed for increase in international reserves until 2020. The exchange regime is free of restrictions and multiple currency practices. The RBM reintroduced in August 2021 a surrender requirement to address foreign exchange shortages which is treated as a temporary measure to address extraordinary circumstances and should be lifted as conditions improve. In May 2022, kwacha was devalued by 25 percent to correct for a large real exchange rate overvaluation for the first time since 2012.

Article IV Consultation:

The Executive Board concluded the last Article IV consultation with Malawi on December 13, 2021.

Financial Sector Assessment Program (FSAP), Reports on Observance of Standards and Codes (ROSCs), and Offshore Financial Center (OFC) Assessments:

A joint team of the World Bank and the International Monetary Fund visited Malawi under the FSAP program during two missions in July and December 2007. The Financial System Stability Assessment (FSSA) was issued in June 2008 (SM/08/198). An FSAP development module was conducted in mid-2017.

Corporate Governance and Accounting and Auditing ROSC missions visited Malawi in February and June 2007.

An update on the FAD mission on the fiscal transparency module was issued in March 2007. A ROSC on the data module, based on a September 2003 mission, was published in October 2004.

Capacity Development: (since 2020, as of October 20, 2022)

Date of Delivery	Department	Ministry/ Agency	Purpose/Topic	Modality
10/22	STA	MOF	Strengthen the quality of GFS/PSDS	Virtual Mission
09/22	FAD	MRA	Strengthen the management of MRA's tax arrear's function and improve debt management capacity	Mission
08/22	MCM	RBM	Enhance the RBM's understanding of systematic risk in domestic systematically important banks	Mission
08/22	FAD	MRA	Review the deployment of new Information Tax Administration System (ITAS)	Virtual Mission
07/22	FAD	MRA	Review the Revenue Mobilization Thematic Fund (RMTF) project	Mission

Date of Delivery	Department	Ministry/ Agency	Purpose/Topic	Modality
07/22	FAD	MRA	Review MRA's proposed organizational design for the Domestic Tax Division	Virtual Mission
06/22	FAD	MRA	Assess the effectiveness of the tax audit program	Virtual Mission
05/22	AFE	MOF	Strengthen project appraisal and selection techniques	Mission
05/22	FAD	MRA	Tax Administration Diagnostic Assessment Tool training workshop	Virtual Mission
05/22	AFE	MOF	Strengthen the credibility and reliability of the Public Sector Investment Plan document	Mission
04/22	AFE	MRA	Strengthen MRA's investigations capacity and customs administration	Workshop
04/22	AFE	NSO	Designing new IIP and PPI bulletin	Virtual Mission
04/22	MCM	RBM	Basel III framework with a focus on credit, operational and liquidity risk	Virtual Mission
04/22	STA	MOF	Improve the quality of fiscal data for the consolidated general government	Virtual Mission
04/22	STA	NSO	Improve the quality and timeliness of external sector statistics	Virtual Mission
03/22	AFE	RBM	Review the key components of FPAS	Virtual Mission
02/22	FAD	MRA	Strengthen revenue administration	Virtual Mission
11/21	AFE	MOF	Strengthen SOE analysis	Virtual Mission
11/21	FAD	MOF	Supporting implementation of a new ITAS	Virtual Mission
11/21	AFE	MOF	Improving quality of general government fiscal data	Virtual Mission
11/21	AFE	NSO	Compilation of GDP expenditure and production	Virtual Mission
09/21	AFE	NSO	Finalize new weights and update the CPI basket	Virtual Mission
09/21	STA	MOF	Using tax data for GDP compilation	Virtual Mission
09/21	FAD	MOF	Developing a VAT compliance improvement plan	Virtual Mission
09/21	FAD	MOF	Integrating performance budgeting and IT systems	Virtual Mission
09/21	FAD	MOF	Excise management	Virtual Mission
08/21	AFE	MOF	Strengthening project appraisal and selection	Virtual Mission
07/21	AFE	NSO	Continued compilation of GDP expenditure	Virtual Mission
07/21	FAD	MOF	Audit of high risk sectors for VAT	Virtual Mission
06/21	AFE	NSO	CPI Update	Virtual Mission
05/21	MCM	RBM	Principles for financial market infrastructures training	Workshop
05/21	MCM	RBM	Review of oversight framework	Workshop
04/21	STA	RBM	Monetary and financial statistics	Virtual Mission
04/21	FAD	MOF	Strengthen excise management	Virtual Mission
03/21	STA	RBM	External sector statistics	Virtual Mission

Date of Delivery	Department	Ministry/ Agency	Purpose/Topic	Modality
12/20	AFE	NSO	National accounts: Review and assist to compile GDP by production	Virtual Mission
09/20	FAD	MOF	Develop a revenue action plan to mitigate the impact of COVID-19	Virtual Mission
08/20	FAD	MOF	Fiscal risks during COVID-19	Virtual Mission
07/20	AFE	NSO	COVID-19 Prices: Compiling PPI and IIP weights	Virtual Mission
07/20	AFE	NSO	COVID-19 National Accounts: Compilation of the supply table	Virtual Mission
06/20	FAD	MOF	Fiscal reporting: Completing the cash basis IPSAS implementation	Virtual Mission
06/20	FAD	MOF	Implementing Msonkho online	Virtual Mission
02/20	FAD	MOF	Public sector balance sheet	Mission
02/20	FAD	MOF	Developing a revenue mobilization strategy	Mission
01/20	MCM	RBM	Projection of the Central Bank balance sheet	Mission

JOINT MANAGERIAL ACTION PLAN

(As of October 20, 2022)

Title	Products	Expected Delivery Date
A. Mutual Information on Relevant Work Programs		
World Bank work program in the next 12 months	FY23 Analytical and Advisory Activities: 1. Malawi: Overcoming Challenges to Transform Human Capital 2. Country Climate and Development Report 3. Malawi Poverty Assessment 4. Malawi Economic Monitor 5. Malawi: Overcoming Challenges to Transform Human Capital 6. Integrated Water Resources Management 7. Malawi Transport InfraSAP2.0 8. Malawi Country Economic Memorandum 9. Malawi: Energy Sector Financial Strengthening 10. Malawi: Out of School Children 11. Malawi: Human Resourcing in Health 12. Malawi: A Deep-Dive Study for Promoting Resilient Urban **Development and Driving Sustainable Regional Growth** 1. FY23 Lending 2. Malawi Growth and Resilience Development Policy Financing – Series 1 3. Regional Statistics Capacity Building Project 4. Agriculture Commercialization Project 2.0 5. Emergency Protecting Basic Services Project 6. Additional Financing Social Support for Resilient Livelihoods Project 7. Urban Water Series of Operations	 November, 2022 October, 2022 November, 2022 Twice a year November, 2023 June, 2023 December, 2023 June, 2023 June, 2023 June 28, 2022 July 29, 2023 December, 2023 [FY23 tbc] [FY23 tbc] May, 2023 December 20, 2022 December 20, 2022 September, 2023
B. Requests for Work Program Inputs		
IMF request to World Bank	1. Updates on WB support to Malawi	Continuous
World Bank request to IMF	1. Regular updates and exchange of views on medium-term macroeconomic and fiscal projections including sharing detailed excel tables on Real, Monetary, Fiscal and External Sectors	Continuous
C. Agreement on Joint Products and Missions		
Joint products in next 12 months	1. Debt Sustainability Analysis (update)	December, 2021

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK

(As of November 2022)

The African Development Bank (AfDB) operations in Malawi date back to 1969. The AfDB Group Malawi Country Office was opened in 2007. As of September 30, 2021, the AfDB had provided significant and diversified support to Malawi, with cumulative commitments worth UA 1,010.2 billion (about US$1.4 billion) to finance 116 operations, including thirteen studies and two lines of credit.

The AfDB' s Malawi Country Strategy Paper (CSP) covering the period 2018-2022 is fully aligned with the third Malawi Growth and Development Strategy (MGDS III, 2017-22), Malawi Vision 2063, and the AfDB's corporate priorities in the Long-Term Strategy (LTS, 2013–22) and High 5 priorities.

The current CSP 2018-2022, aims to support the foundations of private sector led growth by investing in infrastructure and promoting diversification and transformation agenda. In this regard, the CSP covers two pillars. Pillar I: *Investing in infrastructure development through energy and transport; and* Pillar II: *Investing in economic transformation by strengthening agriculture value addition and developing water infrastructure*.

The strategic objective of pillar 1 is to improve competitiveness and efficiency of private and public sector, by extending infrastructure, limiting bottlenecks, and reducing investment constraints that increase business transaction costs. The outcomes to this pillar include improved connectivity to local and regional markets, reduced transport costs, and increased private sector investment in energy and transport. Similarly, the strategic objective of pillar 2 is to boost economic diversification and build resilience by reducing cost of market entry, underpinning the creation of firms and jobs that contribute to the broadening the tax base and enhancing macro-stability. The outcomes for pillar 2 include increased productivity and production, increased market development and diversification, empowered local communities and improved health and wellness.

Crosscutting themes are mainstreamed into the CSP and are an integral part of lending and non-lending operations. Environment and climate change, skills, and training especially amongst the youth, and economic and financial governance are the central cross-cutting areas in operations selected for support.

The CSP (2018-2022) was financed from ADF 14 and ADF-15 resources, with an indicative financing envelop of USD 391.3 million. The Bank approved twelve projects exceeding the ten initially planned. The approved projects are in line with the CSP priorities and covered diverse sectors: transport, agriculture, water, and sanitation as well as cross-cutting areas of economic governance and skills development. About 62% (UA 97.6 million) of the approved resources were secured from the African Development Fund; while the remaining balance came from Nigerian Trust Fund, Global Environmental Facility and Special Relief Fund. The recently approved projects include Africa Disaster Risk Financing Programme (USD 4.7 million) in June 2022 and Malawi Emergency Food Production (USD 20 million. In 2021, the Bank approved the Technical Assistance for the Catchment Based Climate Resilient Water Security Project (USD 865 thousand) in June and Support for Digitization, Financial Inclusion and Competitiveness in December.

Through a strong partnership with the EU, the AfDB has managed to secure 18 million Euros (grant) on 25th February 2019 to co-finance the Multinational Nacala Road Corridor Development Project Phase V. In support of the Nkhata Bay Town Water Supply and Sanitation Project, the AfDB is administering OPEC Fund for International Development (OFID) USD 12 million loan.

Three were approved during 2021-2022 period and are under implementation: (i) Digitalization, Financial Inclusion and Competitiveness Project for USD 13.7 million – 8 December 2021, (ii) Africa Disaster Risk Financing (ADRiFi) worth USD 4.9 million – 2 June 2022, and (iii) Rehabilitating and Upgrading of M5 Road (North-South Road Corridor Project – Benga-Nkhotakota-Dwangwa Road (USD 49.7 million) planned to be approved in late 2022. Funds in the amount of USD 20 million earmarked for Agriculture Commercialization, Value Addition & Youth Agribusiness Project were repurposed and used for Agriculture Emergency Food Production Project.

These interventions aim at strengthening economic transformation by enhancing agriculture value chains, increasing mechanization, increasing access to finance, improving market linkages, and supporting crop diversification. These will underpin new income opportunities for emerging commercial farmers while strengthening linkages to small-scale farmers with increased focus on women and youth. Small industry development will be supported through agro-processing and light industrialization that will contribute to expand the economy and create jobs. The interventions in the water sector are expected to increase capacity of water reservoirs, small dams harvesting schemes, and improve access to potable water to free up time in rural areas especially for women: to allow them focus on other social economic activities. The interventions will support water resource management in key water basins such as Songwe River and Lake Malawi that impact on other sectors, such as energy, agriculture, tourism, and fisheries.

Looking forward, the AfDB plans to scale up its lending to the energy sector with a view to address power shortages. Under ADF-16, the Bank is considering two projects for financing from the Non-Sovereign Operation private sector window, Voltalia Kanengo Dzuwa Solar Project (USD 15.8 million) with a Partial Risk Guarantee facility for Voltalia Solar PV Project of USD 2.3 million and NBS Bank Limited (USD 7.9 million The AfDB continues to engage with the World Bank and other partners for co-financing arrangements of its pipeline operations. In view of this, the AfDB is taking the lead in promoting private investment in the energy sector, through PPPs and the use of innovative financing instruments, such as Partial Risk Guarantees.

The AfDB undertook a project completion review of the CSP2018-2022 in June 2022, to take stock of achievement of results and aligned with Malawi's new National Development Plan and the Bank's Long-Term Strategy in particular, the "High Fives" priorities, which include "Light up and Power Africa", "Feed Africa", "Industrialize Africa", "Integrate Africa" and "Improve the Quality of Life for the People of Africa". The outcome of the review will guide the formulation of its new CSP for the period 2023-2027. The new CSP will build on the experiences from the CSP 2018-2022 and focus on initiatives to close infrastructure gaps and spur diversification of the economy through industrialization and building resilience to persistent disasters. Government has requested that the Bank Priority Areas remain the same as in 2018-2022 CSP. Under ADF 16, the Bank in 2023 will finance Rumphi and Blantyre Water Supply and Sanitations Systems Project (USD 33.4 million) and Shire Valley Transformation Project phase two (USD 26 million).

STATISTICAL ISSUES

As of October 20, 2022

I. Assessment of Data Adequacy for Surveillance
General: Data provision has shortcomings that are serious and significantly hamper surveillance. Most affected areas are: national accounts, fiscal, monetary and external sector statistics.
National Accounts: GDP was rebased from 2010 to 2017. Malawi's nominal GDP for 2017 has been revised upwards by 38.4 percent from MK4,635.4 billion (US$6.35 billion) in the 2010 base year to MK6,417.3 billion (US$8.8 billion) in the 2017 base year. STA is providing a series of technical assistances (TA) to the National Statistics Office (NSO) on reconciling GDP by expenditure and GDP by production with rebased figures. GDP by production and by expenditure had a discrepancy of around 14 percent, which could be a shortcoming that significantly hampers surveillance. Following an assessment of available data sources in July 2022, GDP by production was still four percent larger than GDP by expenditure. The revised GDP estimates are expected to be published by end-2022.
Price Statistics: The NSO will update consumer price index (CPI) weights using expenditure data from the 5th Integrated Household Survey (IHS5), which was conducted from April 2019 to April 2020. Current CPI weights are based on the results of the 4th Integrated Household Survey (IHS4 which was conducted during 2016-2017. AFRITAC East (AFE) has provided technical assistance (TA) to the NSO to update the CPI in 2021, in particular with developing weights from expenditure data generated by the 5th IHS and according to COICOP. The producer price index (PPI) is based on outdated weights derived from the results of the Annual Economic Survey conducted in 2012. In addition to updating the weights, index coverage should be expanded to include other activities to better reflect the current structure of the economy. The NSO is in the process of developing export-import price indexes.
Government Finance Statistics: The accuracy and reliability of the data are affected by source data weaknesses. A key shortcoming in this area is the inadequate system of recording source data. In addition, there are serious quality problems, including data inconsistencies, that complicate program monitoring: • Due primarily to differences in coverage, published data for the budgetary central government include a sizeable statistical discrepancy between above and below the line data. The coverage of government for above the line data is considerably narrower than the information on financing reported by RBM. • While tax revenue data are received in a timely fashion, it is not always possible to reconcile them with deposits in the Malawi Government (MG) Account.

Government Finance Statistics:

- This is a result of the way taxes are reported, and timing differences between receipt of taxes and cleared funds being available for the government. The finances and operations of the Malawi Revenue Authority are also unusually opaque.

- Nontax revenue, including capital revenues collected by line ministries, is not properly accounted for in the fiscal reports prepared by the Ministry of Finance.

- The Ministry of Finance does not include zero-coupon promissory notes, recently issued to clear arrears, in its fiscal reporting.

- Interest payments are currently reported on a currency basis rather than based on the residency of the holder of the security.

The authorities have received significant technical assistance from the Fund and other donors to strengthen expenditure monitoring and reporting, accounting, and statistical reporting, but results have lagged. The government has pledged to strengthen public financial management and fiscal reporting. The new IFMIS was rolled out to all MDAs on 1 July 2021, and authorities are working to produce comprehensive fiscal reports using the new system. The authorities are currently working with East AFRITAC to modify the chart of accounts and output-based structures so that they could more easily be realigned to the national strategy and be more readily understood.

- Annual government finance data for the Budgetary Central Government in a GFSM 2014 presentation are reported for publication in the Government Finance Statistics Yearbook (GFSY). However, these data are not disseminated domestically. STA TA missions have encouraged the authorities to compile and report high frequency data for Budget Central Government in GFSM 2014 framework and assisted them in compiling data for extrabudgetary units (EBUs) with the objective of expanding coverage to central government.

Monetary and Financial Statistics: STA has been working with the Reserve Bank of Malawi (RBM) over the past five years on establishing reporting based on Standardized Report Forms (SRFs) of monetary data. The RBM now submits to the Fund staff SRF-based monetary and financial statistics which is yet to published in the International Financial Statistics. RBM compiles and disseminates all core financial soundness indicators (FSIs) as well as nine additional FSIs. Malawi reports data on several series indicators of the Financial Access Survey (FAS), including mobile and internet banking, mobile money, gender-disaggregated data, and the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (SDGs).

Financial Sector Surveillance: In response to a request from the Reserve Bank of Malawi (RBM), a technical assistance (TA) mission assisted RBM in improving its monetary operations framework and to facilitate the development of the broader financial markets in April 2019. MCM provided a mission to the RBM on domestic asset management strategy which took place in January 2020.
External sector statistics (ESS): The NSO is responsible for compiling trade statistics and balance of payments (BOP) data. The Trade in Goods data are compiled monthly, and the timeliness has improved to up to two months from the reference period but some inconsistencies remain. Annual BOP and international investment position (IIP) statistics are compiled up to 2021 with most of the standard components reported. Quarterly BOP and IIP data are not available. The lack of timeliness and accuracy of the ESS significantly hampers the staff's work on projection and macroframework of the external sector development.
The ESS mission conducted by STA in March–April 2022 focused on improvements of the coverage, compilation, and timeliness of goods trade data, along with assessment of the BOP and IIP data compilation to follow up on previous TA missions (the latest in 2021). The mission noted quality issues in the trade data. The mission set out recommendations regarding source data collections, staff capacity, and intra-agency cooperation. The daily exchange rate data, monthly international reserves data as well as the FXI data are regularly reported from the Reserve Bank of Malawi (RBM). The reported international reserves data follow closely the data template on International Reserves and Foreign Currency Liquidity (IRFCL). The RBM has started reporting an independent line for the estimated size of pledged deposits. The value of pledged deposits is, however, subject to change upon the completion of the special audit of foreign exchange reserves. The RBM also started to submit a daily FX cashflow table on a regular basis. Regarding the external debt data, the government of Malawi (GOM) now provides granular breakdowns on top of the end-year stock data. In the current conjuncture of Malawi's extremely vulnerable position to the external sector, reliable and timely ESS reporting is essential for diagnoses of any developments in the external sector. To move forward with improvements, the NSO, RBM, and the GOM should continue to improve coordination and take appropriate steps to implement TA recommendations to ensure a regular flow of data from this system for trade, BOP and IIP compilation; and the government should allocate sufficient resources for conducting regular surveys.

II. Data Standards and Quality	
Malawi participates in the Enhanced General Data Dissemination System (e-GDDS) and publishes essential macroeconomic and financial data on its National Summary Data Page since November 2016 (http://cb.malawi.opendataforafrica.org/uwkhibc/national-summary-data-page-nsdp). Timeliness of data disseminated under the e-GDDS would need to be improved.	Data ROSC was published on February 17, 2005.

Statement by Mr. Nakunyada, Executive Director for Malawi, Mr. Ubisse, Alternate Executive Director, and Ms. Nainda, Senior Advisor to the Executive Director

1. On behalf of the Malawian authorities, we thank management and staff for facilitating the authorities' request for emergency financing under the new Food Shock Window (FSW) and a Staff Monitored Program (SMP) with Board involvement (PMB. Our authorities view rapid financing under the FSW as critical to alleviate food shortages, while the PMB would help sustain the reform momentum and pave the way for deeper reforms under a new Upper Credit Tranche (UCT) program.

2. The economy of Malawi remains challenged by elevated vulnerability to frequent and large tropical cyclones and intermittent droughts that have undermined agricultural production and food self-sufficiency. More recently, rising international food, fuel, and fertilizer prices in the wake of the Russia-Ukraine war, have precipitated a cost-of-living crisis with disproportionate effects on vulnerable households. Consequently, emergency financing needs have emerged as the food import bill has increased substantially in the context of limited fiscal space. Against this backdrop, the authorities seek emergency financial support under the food shock window of the RCF amounting to 50 percent of quota. Rapid financing under the newly established FSW would be vital to fill the immediate financing gap created by the spillovers from the war, while a PMB is essential to restore macroeconomic stability and set the foundations for graduation to a fully-fledged UCT-program.

Impact of Multiple Shocks

3. Economic activity has been negatively affected by the overlapping external and domestic shocks in recent years, with growth remaining below pre-pandemic levels. The consistent cycle of vulnerabilities including from lingering pandemic effects, the spillovers from the war in Ukraine, multiple and successive tropical storms, below-average crop production, and increasing prices for food and agricultural inputs such as fertilizers and seeds, have culminated in rising food insecurity. Specifically, the Malawi Vulnerability Assessment Committee (MVAC) report for the 2022/23 consumption season, released in August, has shown that about 2.3 million people face food insecurity and require urgent assistance. At the same time, a total of 3.8 million people (about 20 percent of the population) will be facing critical food security challenges in the coming 5 to 6 months.

4. Furthermore, Malawi faces worsening fuel shortages compounded by the prevailing high oil prices alongside extended electricity blackouts. As a result, growth is projected to decelerate from 2.2 percent in 2021 to 0.8 percent in 2022 while the outlook remains subject to significant downside risks. Inflation accelerated from 7.6

percent at end-2020 to 25.9 percent year-on-year in September 2022, with food inflation reaching 33.7 percent. As the staff report rightly noted, the country faces persistent foreign exchange shortages, with the stock of international reserves at critically low levels with readily available gross reserves of about 1.6 months of import cover at end-2021. Overall, it is assessed that Malawi faces an urgent BOP need estimated at US$841 million over the next 12 months, reflecting the repercussions of the food-price shock. As a result, prospective financing under the RCF would only cover 10 percent of the external financing needed for the next 12 month, which highlights the need for additional donor support.

Response to Rising Food Insecurity

5. The strengthening of social protection has become critically important considering that poverty incidence and food insecurity in Malawi ranks amongst the highest in the world. In this context, the authorities are preserving existing social protection programs to cushion vulnerable households. Going forward, they plan to establish a floor on social spending as an indicative target (IT) under the PMB, comprising government contribution to health and basic and secondary education spending, as well as several social safety net programs such as the social cash transfer program (SCTP) and Affordable Input Program (AIP). These measures seek to support the vulnerable groups including the elderly, children, and the disabled by providing them with social cash transfers and additional resources to cushion farmers from increased prices of fertilizers. Furthermore, the authorities plan to procure additional maize and other food stuffs under the Disaster Affairs Department for lean season response (December 2022 - March 2023) and distribute quality seeds to the vulnerable population to enhance maize production, the country's staple grain.

6. The authorities are determined to ensure that implementation of social protection programs achieve the desired outcomes**.** In this respect, they have committed to undertake periodic audits in the context of annual fiscal reporting to the National Assembly under the PMB. Further, they will take additional measures to prevent cost overruns from escalating fertilizer prices in the AIP, the Government subsidy program, through augmentations of farmer contributions as well as limiting the Government Subsidy. The authorities also stand ready to take any additional measures that may be needed over and above those pronounced in the MEFP and, in consultation with staff.

Policy Measures Under the PMB

Debt Management and Fiscal Policy

7. The authorities are committed to foster fiscal disciple to restore debt sustainability and lay the groundwork for sustainable and inclusive growth. To this end, they have adopted a debt restructuring strategy aimed to help restore debt sustainability and close attendant financing gaps. In particular, the strategy relies on bringing external

public debt levels back to moderate risk of debt distress in the medium-term through a combination of policy adjustment and debt treatment. To this end, the debt strategy targets all external Debt Sustainability Analysis (DSA) solvency and liquidity ratios to cross their respective thresholds under the baseline in the next five years. To support a credible process for restructuring public debt, the authorities engaged a debt advisor to ensure their approach delivers the necessary contributions in a sustainable manner. Further, the authorities have approached all creditors early in the process and they are committed to achieve a debt treatment that places the country's debt back on a sustainable path consistent with program objectives.

8. To achieve fiscal discipline and support efforts to bring debt towards a more sustainable path, the authorities fiscal consolidation efforts for the remainder of FY2022/23 will be geared towards (i) strengthening implementation of the domestic revenue mobilization strategy (DRMS) in a timely manner (ii) rationalizing and prioritizing spending, (iii) introducing and implementing sound commitment controls through IFMIS and (iv) implementing well targeted measures to support low-income households. To this end, the authorities have already rolled out the first phase of reforms to the fertilizer and seed subsidy program under the (AIP) through the introduction of a Consolidated Social Protection Program using the Unified Beneficiary Register to reduce duplication of access and improve beneficiary targeting. Other planned measures include strengthening the oversight of state-owned enterprises (SOEs) as well as monitoring SOE management accounts on a quarterly basis. In addition, to ensuring compliance with the new PFM Act, the authorities will prepare an annual consolidated report of all SOEs.

9. Sustained revenue mobilization efforts will continue to be supported by the DRMS launched in December 2021. The authorities' main target is to increase revenue by 5 percent of GDP during the 5-year implementation of the strategy, including through PAYE brackets aimed at introducing additional income tax brackets starting in April 2022, which partly reversed the loss in revenue from previous changes in rates and brackets. They also rolled out full implementation of the advance income tax in May 2022 which raised additional revenue. Other measures in the pipeline include tax stamps on beverages, taxes for business, and tax incentives to help unlock the much-needed foreign investment. To strengthen tax administration, the authorities are on track with the launching of the Integrated Tax Administration System (ITAS), also called *Msonkho* online which is expected go-live in December 2022, with all modules expected to be integrated by March 2023.

10. The authorities are committed to stepping up efforts to address governance weaknesses and reduce corruption vulnerabilities, including through enhancing transparency and accountability of public financial management (PFM), strengthening autonomy and governance of the Reserve Bank of Malawi (RBM) and strengthening of its foreign exchange reserves management. In this context, they

passed the new PFM Act in March 2022 to align the legal framework with ongoing PFM reforms. The authorities are also in the process of drafting the regulations and Treasury instructions to support the implementation of the new Act which they intend to finalize by March 2023 and June 2023, respectively.

Monetary and Financial Sector Policies

11. The RBM's core focus is to restore price stability by anchoring inflation expectations, including through tightening monetary policy as needed. They intend to maintain a reserve money targeting framework to curtail monetary growth, while limiting foreign exchange interventions. At the same time, the central bank will implement the agreed path towards accumulating foreign exchange reserves to rebuild the country's reserve assets, including by reducing direct foreign exchange sales to the market in support of imports. Concurrently, the RBM will gradually wind down the existing swap open position as guided by the foreign exchange accumulation path.

12. Considering the effects of the increase in the exposure of the banking sector to the public sector and recent interest rate hikes, the Reserve Bank remains attentive to these risks and continue to strengthen financial sector oversight. To promote financial stability, they are closely monitoring the banking system's sovereign exposure through securities and swap operations as well as reassessment of loan and collateral quality needs of commercial banks.

Conclusion

13. The authorities recognize the importance of safeguarding transparency and accountability in the use of Fund resources as well as the signaling effects of a good track record under the SMP-PMB. Importantly, the Fund's support under the PMB will provide a strong anchor for the effective coordination and implementation of policies that support macroeconomic stability, while working towards a possible successor ECF arrangement to restore macroeconomic imbalances and support the authorities' long-term development plan under *Vision 2063*. They look forward to Executive Directors' support for their request for emergency financing to sustain their efforts to deal with the acute food insecurity along with an SMP-PMB to act as a bridge towards deeper reforms under a UCT-arrangement, which catalyzes additional donor support, and anchor the authorities broader reform agenda.