International Monetary Fund

Malawi and the IMF

Press Release:
IMF Executive Board Completes Fifth and Sixth Reviews under Malawi's ECF Arrangement, and Approves US$ 18.1 Million Disbursement
March 23, 2015

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Malawi: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

March 4, 2015

The following item is a Letter of Intent of the government of Malawi, which describes the policies that Malawi intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Malawi, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

Letter of Intent

March 4, 2015

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

Dear Madam Lagarde:

On January 17, 2014, the Executive Board of the International Monetary Fund (IMF) completed the third and fourth reviews under the three year Extended Credit Facility (ECF) arrangement for Malawi. At the same time, the Board extended the arrangement to November 2015. This letter and the attached Memorandum of Economic and Financial Policies (MEFP) report on recent economic developments and performance under the ECF arrangement since that time, and on the policies we plan to implement in the remainder of fiscal year 2014/15 and over the medium term.

The new government of Malawi, led by Professor Arthur Mutharika, assumed power last year in a very challenging economic environment. The large scale theft of public funds uncovered in late 2013—dubbed the "cashgate" scandal—exposed substantial weaknesses in our public finance management (PFM) systems and severely impacted our macroeconomic situation. The immediate effect was a suspension of all donor budget support, then valued at about 5 percent of GDP. As a result the fiscal situation became dire, and difficulties were compounded by an increased recourse to domestic financing. Domestic payment arrears emerged, inflationary pressures persisted and the exchange rate depreciated sharply.

Since that time, we have made significant efforts to stabilize our macroeconomic situation, regain control over our PFM systems, and safeguard the stability of our financial sector. We are confident that these ongoing efforts will restore private sector confidence in our policy stance, place inflation on a downward trajectory, and foster growth-promoting private investment.

We remain committed to the objectives of the original ECF-supported program, namely attaining strong inclusive growth, single digit inflation, and an increase of reserves to at least three months of import cover. Important to these ends will be preservation of our flexible exchange rate regime and automatic fuel pricing mechanism, both of which have served us well since 2012. We will continue to implement a tight monetary policy stance capable of forcing inflation onto a clear downward trajectory and will maintain positive real interest rates throughout the program period. Our fiscal program for FY2014/15 is calibrated to support such a strong disinflation effort and to restore private sector confidence in our ability to control fiscal expenditure and safeguard debt sustainability. We are combining this firm macroeconomic policy stance with the implementation of a far-reaching strategy to address weaknesses in our PFM system.

We are requesting waivers for the nonobservance of one periodic performance criterion (PC) related to the fifth review (end-December test date) and two periodic PCs for the sixth review (end-June 2014 test date) that were not met. The PCs on net domestic assets of the central bank and net domestic borrowing were missed mainly because of the difficulties arising from ongoing external financing shortfalls and uncertainties surrounding our recent tripartite elections.

The continuous ceilings on external payments arrears and on non-concessional debt were not met following the contracting and subsequent nonpayment of external obligations on a supplier's credit for military equipment. With regard to the contracted non-concessional credit, we have taken remedial actions by renegotiating the supplier's credit agreement, reducing substantially the value of transactions value of transactions with the supplier from US$145.3 million to US$33 million and have also taken further remedial measures to improve debt management capacity. With regard to the external payments arrears, we have normalized the outstanding arrears as explained in our February 19 letter, in response to your February 12 letter. On the basis of our remedial actions, we are requesting a waiver for the nonobservance of the performance criteria on the contracting of non-concessional external debt with a maturity of more than one year and on the accumulation of external payments arrears that resulted in non-complying disbursements.

The continuous ceiling on new non-concessional external debt maturing in more than one year was also not met due to the contracting of two non-concessional loans: (i) a supplementary loan for the rehabilitation of an inter-city road, which became effective in April 2014; and (ii) a loan we contracted in February 2015 for the construction of a cancer treatment center in Lilongwe. Efforts to obtain better terms for the infrastructure loan were unsuccessful and the government decided to go ahead with the loan on the grounds that it was relatively small (US$4 million), but also because it was critical to addressing Malawi's infrastructure gap and necessary to avoid accumulation of arrears to the contractor. The construction of a cancer treatment center is a critical addition to Malawi's health care infrastructure, as the incidence of cancer is rising quickly and the cost of referring patients to foreign hospitals is extremely high. The loan, (US$13 million), was negotiated with the OPEC Fund for International Development. It carries a 29 percent grant element and was only agreed after exhausting efforts to secure more concessional financing from other development partners.

Going forward, we are committed to take measures to improve our ability to monitor the concessionality of new external loans and to strengthen debt management in general. To these ends, we are resuscitating the Debt Management Committee. With members drawn from senior civil servants, this committee will be responsible for ascertaining the concessionality of every borrowing proposal, with a view to safeguarding debt sustainability and ensuring that all loans remain compliant with the Public Financial Management Act. We will discuss with Fund staff all new loan proposals before they are brought to the attention of the Cabinet or Parliament and ensure transparency of the grant element of loan proposals. We also will continue implementing the Debt management reform programme that was agreed with the IMF and World Bank, which is aimed at strengthening our debt management capacity. On this basis, we request a waiver for the nonobservance of the continuous ceiling on new non-concessional external debt with a maturity of more than one year.

We have undertaken the following prior actions before consideration of the fifth and sixth ECF arrangement reviews by the IMF's Executive Board: (i) implementation of expenditure cuts necessary to limit net domestic financing under the program ceiling for the fiscal year 2014/15; (ii) issuance of a letter to the central bank to transfer revenues to the main government account; (iii) inclusion of our main government accounts (MG1 and the six operational accounts) in our information management system; (iv) submission to Parliament of legislative amendments to limit RBM's credit to government to 10 percent of the previous year's revenue; and (v) submission to Parliament of amendment to the Banking Act and the Financial Services Act in line with those recommended by March 2013 Fund TA mission.

On the basis of our overall performance, the corrective actions that are being taken, as well as the strength of policies set forth in the attached MEFP, we request that the Executive Board of the IMF complete the fifth and sixth reviews under the ECF arrangement and release the sixth and seventh tranches totaling SDR 13.02 million. We also request an extension of the arrangement by 6 months to May 22, 2016 to allow for the completion of the eighth review, as well as the rephasing of the remaining disbursements under the arrangement.

We believe that the policies set forth in the attached Memorandum of Economic and Financial Policies are adequate to achieve the objectives of the program, but we will take any further measures that may become appropriate for this purpose. We will consult with the Fund on the adoption of these measures, and in advance of any revisions to the policies contained in the MEFP, in accordance with the IMF's policies on such consultation. Moreover, we will provide the IMF with such information as they request in connection with progress in implementing our policies and obtaining the objectives of the program.

The Government of Malawi authorizes the IMF to make this letter and the attached MEFP and Technical Memorandum of Understanding available to the public, including through the IMF internet website.

Yours sincerely,

/s/	/s/
Mr. Goodall Gondwe, Minister of Finance	Mr. Charles Chuka, Governor of the Reserve Bank of Malawi

Attachments:

- Memorandum on Economic and Financial Policies;
- Technical Memorandum of Understanding.

Attachment I. Memorandum on Economic and Financial Policies for the Fifth and Sixth Reviews under the ECF Arrangement

March 2015

BACKGROUND

1. This memorandum supplements the Memorandum of Economic and Financial Policies (MEFP) attached to the Letter of Intent dated December 26, 2013. It describes recent developments and performance under the ECF-supported arrangement since completion of the third and fourth reviews in January 2014. It also elaborates on the policies and structural reforms we intend to carry out in the year ahead to regain macroeconomic stability, improve our public financial management systems, and safeguard financial sector stability.

2. Tripartite elections at all levels of Government were held in May 2014. Despite some logistical issues, these elections were considered by independent observers to have been free and fair. Following the elections, a new Government, led by Professor Arthur Peter Mutharika, assumed power and committed to correcting macroeconomic imbalances and setting the country on a path to sustainable and inclusive noninflationary growth. In the sections below, we describe our policy agenda for significantly enhancing and accelerating our macroeconomic and structural reform process. Some of the modalities we intend to adopt represent a departure from those of the previous Government, a change largely motivated by altered circumstances and, in some cases, a more realistic evaluation of implementation capacity. The differences mainly reflect a recasting of priorities, but the underlying aim of rapidly regaining macroeconomic balance, rebuilding government fiscal systems, improving financial sector stability, and achieving our growth potential remains unchanged. We also remain committed to the fundamental reforms adopted in 2012 that established a flexible exchange rate and automatic fuel pricing mechanism, as we view these as necessary and appropriate to Malawi's present economic circumstances.

RECENT ECONOMIC DEVELOPMENTS AND NEAR TERM OUTLOOK

Impact of the "Cashgate" Scandal

3. The discovery of the theft of government funds in late 2013—dubbed the "Cashgate" scandal—revealed deficiencies in our fiscal systems on a scale previously unsuspected. Following the discovery, measures to improve our public financial management (PFM) system were adopted in October 2013 in the form of a Government Action Plan, which was developed in consultation with, and generously supported by, development partners. In March 2014, an independent assessment was made on 39 actions that were due for monitoring and verification. The assessment indicated that 22 of 66 actions were met, progress had been made on 10 others, 1 was not met and 6 could not be assessed. However, an internal assessment of these actions was done in October 2014 and showed that 48 actions were met, there was progress on 12 actions and 6 actions were yet to be met. Notwithstanding this progress, we realize that

achieving credible and reliable PFM systems will require a more strategic and results based-approach.

4. One of the main undertakings of the government's Action Plan was the commissioning of an external forensic audit with financial assistance from DFID. An interim report was issued in February and the final report was delivered to Government in October 2014. In addition to providing details of the illicit transactions uncovered—details that are now being used by our law enforcement agencies to carry out prosecutions and to effect recovery of stolen funds—the reports also provided insight into the deficiencies of our PFM system that had allowed the thefts to take place. This analysis, supplemented by technical assistance from the IMF and the donor community, has been helpful to us in designing a comprehensive action plan, with a well thought out design and sequencing of reforms, which we intend to vigorously implement over the remaining period of our IMF-supported program (see below). Currently, Government has engaged Price Waterhouse Coopers International to carry out comprehensive forensic audit on the Epicor System for the period 2009 to March 2013 with assistance from GIZ. Furthermore, Government has engaged private auditors to conduct comprehensive forensic audits on all independent sites (sub IFMIS systems) which include: State Residences, Malawi Defense Forces and the Malawi Police.

5. The "cashgate" scandal interrupted what would otherwise have been a period of economic recovery. After some initial trepidation following the floating of the exchange rate in May 2012, and the subsequent depreciation that followed, markets in Malawi had begun to see the substantial benefits of the new exchange rate regime. They had also come to recognize that the automatic fuel pricing mechanism had been responsible for eliminating the fuel shortages of the previous year. Following a good tobacco season in March-August 2013, substantial reserves were accumulated and this, combined with monetary tightening, had arrested the decline of the exchange rate. Inflation was on a downward trend, growth prospects appeared good and, with rising private sector confidence, we anticipated further macroeconomic stabilization and strong growth over the coming year.

6. The outbreak of "cashgate" significantly changed this outlook, and the suspension of budget support that followed continues to impact our macroeconomic position. With our budget for FY2013/14 heavily reliant on these cash disbursements, their sudden withdrawal necessitated fiscal adjustment on a scale that overwhelmed our weakened PFM systems. As a result, domestic borrowing limits were exceeded, and large domestic payments arrears accumulated. With the Reserve Bank financing a substantial portion of the government's borrowing requirement, and with incomplete sterilization of foreign exchange reserve purchases, liquidity control became problematic. This led to un-programmed increases in reserve money and net domestic assets (NDA) of the Reserve Bank of Malawi (RBM) that compromised our disinflation program. Moreover, the loss of the foreign exchange associated with budget support and dedicated grants, in the absence of complete fiscal adjustment, also slowed reserve accumulation from what could otherwise have been achieved.

RECENT ECONOMIC DEVELOPMENTS

7. As of the final quarter of 2014, the macroeconomic situation remains mixed. Growth has shown considerable resilience, but inflation and recent exchange rate movements are worrisome. With the protracted period of uncertainty, private sector confidence has been eroded, and inflationary expectations remain high.

- Growth has held up so far in 2014, with preliminary indications that real GDP growth will increase from 5.2 percent in 2013 to about 6 percent in 2014, led by strong outcomes from the agriculture, wholesale/retail trade, and information and communication sectors. The ready availability of foreign exchange and fuel appear to be continuing to support the recovery in economic activity. All major sectors of the economy are projected to register positive growth except the mining sector which will be adversely affected by the suspension of uranium production at Kayerekera mine since June 2014.

- International trade remains strong. Exports are set to grow by 7 percent during 2014, driven by a recovery in tobacco production as well as continued export growth in traditional (tea, sugar, cotton) and nontraditional commodities (such as edible nuts). Growth in these sectors is expected to compensate for the closure of the Kayelekera Mine, which by 2013 was exporting the equivalent of one-third of total tobacco exports. Imports are expected to grow slowly at about 3.7 percent during 2014, sustained in part by the imports required by a large power plant investment Kapichira II. Overall, both the merchandise and services deficits are expected to improve during 2014.

- The fiscal situation has been challenging. The "cashgate" scandal not only necessitated a sharp curtailment of programmed expenditure, but it also undermined trust in public financial management systems and raised concerns that the budget was not fully financed. In the event, with annual shortfalls in external disbursements amounting to almost 6.6 percent of GDP, our PFM systems proved too weak to enforce the discipline needed to follow the adjustment path agreed under the program. By the end of the 2013/14 fiscal year, domestic financing rose to about 6 percent of GDP and payment arrears (1.7 percent of GDP) had accumulated an amount substantially above our target level. Compounding the issue, we have also uncovered additional arrears that had been accumulated by the previous Government over the past several years.

- The disinflation process stagnated in 2014 and inflation at end-2014 remained elevated, at 23 percent (year-on-year). This reflects, in part, high liquidity levels from largely unsterilized foreign exchange purchases during the tobacco season, and from some financing of the FY2013/14 fiscal deficit by the Reserve Bank of Malawi (RBM). In July 2014, in anticipation of a more favorable outlook for inflation, the RBM lowered its policy rate by 250 basis points to 22.5 percent. In retrospect, we now believe this move was somewhat premature, as the annual inflation rate accelerated over the subsequent two months rendering the policy rate negative in real terms. Since this was sending a conflicting signal to the market, we subsequently raised the rate back to 25 percent on October 30th. We believe this level is sufficiently positive in real terms to send appropriate signals to the private sector regarding our commitment to the disinflation process. This measure was followed by a directive restructuring the liquid reserve ratio (LRR) by requiring that the current LRR (15.5 percent) be imposed on foreign currency deposits in local currency rather than in foreign currency. This became effective on November 10, 2014, and is contributing to the absorption of liquidity from the banking system.

- Interest rates on bank loans have remained elevated, and this has reduced the growth of private sector credit sharply. Anecdotal evidence suggests this is increasingly restricting new business investment which, combined with reduced real incomes from the inflation, will affect growth going forward. Evidence from the third-party diagnostics of individual banks suggests there has also been some impact on the health of the banking sector as non-performing loans have risen steadily since end-2012 and now stand at 15.8 percent of gross loans.

- The exchange rate came under considerable pressure and depreciated by 15 percent in 2014. This is in part a seasonal phenomenon, as the rate usually weakens after the end of the tobacco buying season in August. However, it has been particularly acute so far this year, owing to the unattractive level of real kwacha interest rates prevalent up to November, and shortfalls in external financing. International reserve levels have reached a relatively healthy level of 2.9 months of import cover in December, but remain below our target level of three months. As it did last year, the RBM purchased substantial reserves during the 2014 tobacco buying period, helping to smooth exchange rate volatility during the first half year of 2014.

- Malawi's external public debt to GDP ratio is growing and is expected to reach 32 percent of GDP in net present value terms at end-2014. Nonetheless, this is not expected to worsen the debt dynamics significantly, as external debt remains mostly concessional. Our external debt service burden remains low, with a debt service ratio in 2014 of only 4.7 percent of exports of goods and services. In contrast, our domestic debt burden is becoming more worrisome due to increased recourse to domestic financing over the last two years, and from our recent decision to securitize past domestic arrears. As a result, total public debt as a share of GDP is set to reach 75.8 percent of GDP at end-2014.

PERFORMANCE UNDER THE PROGRAM

8. As a result of these developments, a majority of the periodic quantitative targets for end-December 2013 (fifth review test date) and end-June 2014 (sixth review test date) under the program were missed. The exception was the performance criterion on net international reserves (NIR), which was met comfortably for both test periods. In the first period, this was the result of the RBM refraining from exchange rate intervention after the end of a strong tobacco season in August 2013, as it preferred to maintain—at a cost of some exchange rate depreciation—a prudent level of reserves. The end-June 2014 target on NIR was met from the carry over effect of this, but also because of another strong tobacco season in mid 2014. However, incomplete sterilization of these purchases increased system liquidity and pushed NDA and reserve money of the RBM above program targets in both December 2013 and June 2014. The performance

criterion (PC) on net domestic borrowing by government was met for the December 2013 test date but, as spending pressures became acute in the second half of the fiscal year, control over expenditure suffered and additional borrowing was undertaken that breached the end-June 2014 program ceiling. The indicative target on social spending was also missed, in part because of lower spending on the Farm Input Subsidy Program (FISP).

9. The continuous ceiling on the accumulation of nonconcessional external debt was missed, due to: (i) the contracting in October 2013 of a medium-term nonconcessional suppliers' credit; (ii) the contracting in April 2014 of a supplementary loan for the rehabilitation of the Liwonde-Naminga road and (iii) the contracting in February 2015 of a loan for the construction of a cancer treatment center in Lilongwe. The continuous ceiling on external payments arrears was also missed as of October 2013 due to arrears incurred on the supplier's credit loan. The above mentioned supplier's credit with the Paramount group in 2013 was to acquire military equipment. Proceeds from the sale of the presidential jet in 2013 were used to make partial restitution of overdue payments on this credit agreement. On coming into office, however, the new Government determined that this contract was an anomaly and took steps to exit the agreement. To this end, we have renegotiated the contract so that it only includes equipment that has either been already delivered or currently in the production line, resulting in a reduction in the total value of the arrangement from $145.3 million to $33 million. We wish to reassure the Fund that the present government is committed to the PFM Act and that transactions and contracts of this nature will not be repeated in.

10. The supplementary loan for the Liwonde-Naminga road is relatively small (US$4 million) and was contracted with a relatively high grant element of 29 percent. We indicated to the Fund our intention to obtain financing for this project in order to close the financing gap in the project as agreed in the remedial measure of our current program. However, efforts to obtain better terms or financing from additional concessional lenders were unsuccessful. A decision to continue with the project was then made on the basis of its small size, that the government had already engaged a contractor, the strategic importance of this road, and the fact that it will not affect debt dynamics significantly or persistently. Moreover, delaying payments to the contractors would have incurred higher costs in terms of idle time, contract extension and penalties. The Government realized that this loan was nonconcessional but considering that works on the road had stalled, it would have been costly to terminate the contract with the contractor in view of the fact that the amount required to complete the road was small. Litigation and interest costs would have made the project even more costly than US$4 million. Furthermore, considering the strategic nature of the road, Government was determined to complete the works on the road because the works started a long time before the current program. Government made this borrowing on the basis on necessity and we undertake to stick to the agreed non-concessional borrowing for any future projects.

11. The ceiling on new nonconcessional external debt maturing in more than one year was also missed with the contracting of a loan in February 2015 for the construction of a cancer treatment center in Lilongwe. In Malawi Data from the cancer registry is showing that new cancer cases are rising quickly and the proportion of patients living with cancer and requiring continuous treatment is rising even faster. Chemotherapy, when available, is very expensive and is about $1400 per treatment. This is beyond the reach of the average Malawian. Radiotherapy is

a more affordable and appropriate palliative modality for cancer patients. It is envisioned that the National Cancer Centre will be an outpatient radiotherapy and chemotherapy referral centre, catering for both fee paying and non paying patients. The proposed project will provide a cost efficient national and regional cancer centre drawing patients from around Malawi and neighboring countries. The National Cancer Centre is also expected to become a centre for learning, incorporating resources such as a joint hospital/cancer centre library and learning centre, along with facilities to enable the development of partnerships with nursing and medical schools. The loan, which amounts to US$13 million), was negotiated with the OPEC Fund for International Development and carries a 29 percent grant element. It was only agreed after exhausting efforts to secure more concessional financing from other development partners.

12. Under the Health SWAP 1, the Government made a plea to Development Partners to have the cancer project be included as part of the critical infrastructure needed for improved health. However Development Partners wanted the integration of cancer issues within the existing health delivery mechanism than a standalone facility. Realizing the high costs of cancer treatment in terms of referrals outside the country, in 2010 Government decided to finance the cancer centre using local resources and most of these funds were used on studies and obtaining approval from International Atomic Energy Agency (IAEA). After failing to secure funding from any of the traditional development partners whose funding is concessional, it was only OFID that agreed to finance this life saving facility (US$13 million). Just like all other OFID loans the Grant Element is 29 percent and the Government considers this very close to the grant element of 35 percent that is recommended by the Fund.

13. Progress on structural reform under the program has been uneven. We have verified the stock of government domestic arrears for 2013/14 financial year and those accumulated in previous years. The total stock of arrears stands at K157 billion (8 percent of GDP). However, as these numbers were very large and because some of the claimants are mentioned in the forensic audit report, we have asked the Auditor General to repeat the entire audit. Regarding arrears accumulated during FY13/14, further work is needed to verify that some of the infrastructure works presented in the claims were actually carried out. Government has authorized the RBM to stop the automatic conversion of overdrafts into government securities. This significantly reduced the stock of treasury bills held by the central bank, but had little effect on curbing the accumulation of government debt held in the form of advances. The RBM has regularly published a quarterly financial stability report, we have adopted a prompt corrective action framework for bank resolution, amendments to the RBM Act were submitted to Parliament (prior action), and third party diagnostics were completed for every bank in the system.

14. The forensic audit of the "Cashgate" period was completed and the full report was made publically available, and prosecutions of malefactors and recovery of stolen funds has begun and has met with some initial success. We are using the 53 case files arising from the forensic report to prosecute those individuals involved in theft of state funds and money laundering. To date there have been five convictions and MK 183 million has been recovered so far. With the assistance of an external asset recovery expert financed by the U.K we will endeavor to increase the efficacy of recoveries as prosecutions proceed. Investigative agencies, namely the Anti Corruption Bureau, Financial Intelligence Unit, the Financial Fraud Unit of the Malawi Police Force and the Malawi Revenue Authority are closely collaborating in getting evidence to pursue

prosecutions under the Penal Code, the Corrupt Practices Act, the PFM Act and the Anti-Money Laundering framework. In recognition of gaps in the legal framework we will request technical assistance from the Fund in amending some of these acts.

15. Given "out of scope" transactions highlighted by the forensic audit report (transactions outside the auditors' remit to investigate cashgate transactions) , we have now harmonized procurement across the public sector and will conduct an audit of these transactions in each ministry. Auditors from the private sector will be employed to complement our existing audit function which will be centralized within the Ministry of Finance. To reinforce compliance with obligations under the PFM Act, controlling officers in each ministry and senior civil servants will be required to attend a series of workshops on the responsibilities and sanctions under the PFM Act. Moreover, all controlling officers will be issued with appointment letters with revised terms of reference. In addition to benchmark progress we will issue a report by an audit firm confirming the status of implementation of the forensic audit recommendations (end-December benchmark).

16. On a number of other structural commitments work has progressed, but closure has proved difficult. We have uploaded into IFMIS most of the manual transactions undertaken when our systems were suspended in October-November 2013. However, the completion of this exercise was delayed due to the pending validation of these transactions. The reconciliation has shown that few votes have still not been finalized in capturing their expenditures into the system. We have thus set a deadline of end-February 2015 as a final date of completing this assignment. Similarly, progress has been made towards doing daily reconciliation of government accounts with the RBM beginning January, 2014, but due to technical problems of Epicor based IFMIS it has been difficult to finalize adjusting the unreconciled items into the system. However, a 15 member team was assigned to manually do the reconciliation from 10th November, 2014 and we are hopeful that the assignment will be finalized by the end of February, 2015. As regards the follow up on the backlog, the Central Internal Audit Unit will finalize its work by end-February, 2015. We have not provided Departments and Agencies with quarterly spending ceilings, as we felt our resource envelope was too constrained, but we have continued to issue monthly ceilings. Moving to quarterly ceilings which will increase spending efficiency remains our intention and we will implement this soon as feasible. We also encountered administrative delays in submitting amendments to the Banking Act and Financial Services Act to Parliament.

17. Performance on the macroeconomic level since mid 2014 has been significantly better. In order to anchor monetary and fiscal policies, we agreed on informal targets with IMF staff for end-September and end-January 2015 on gross international reserves, net domestic assets of the RBM and government net domestic borrowing. While we missed the end-September 2014 target on net domestic borrowing, all others were met. Furthermore, we have carried out a number of structural measures, described below, as prior actions for completion of the fifth and sixth reviews.

OUTLOOK AND KEY ECONOMIC OBJECTIVES

Key Goals

18. We remain committed to the objectives of the original program including increasing reserve cover to at least three months of imports and reducing inflation to single digits. Our overriding short-term goals are to stabilize our macroeconomic situation, regain firm control over our fiscal systems, and safeguard the stability of the financial sector. These are necessary conditions that must be met if we are to successfully address Malawi's pressing development needs in the years ahead. Responsible fiscal and monetary policy combined with vigorous PFM reform are needed to restore confidence in the budget, reduce inflation, reverse the contraction of real incomes, and foster the private sector confidence needed to encourage growth-promoting investment.

19. To this end, we recently raised our policy rate from 22½ percent to 25 percent, a move that significantly tightened our monetary policy stance. We are supporting this measure with appropriate liquidity operations to ensure that the rate increase translates into an upward shift in other key interest rates and establishes sharply positive real interest rates throughout the economy, with particular attention to the rates on treasury bills. Concurrently, we have embarked on a series of accelerated PFM reforms designed to quickly regain control of our fiscal operations so that our stabilization program is not forced off track by unauthorized spending or by a further accumulation of arrears.

MACROECONOMIC OUTLOOK AND RISKS

20. We view a restrictive policy position as necessary in the short term to stabilize our economy, but we recognize that this will exert a cost in near-term growth. Support from lower international prices for food and fuel and a stronger currency will assist in bringing inflation to single digits over the next 12 to 15 months. This will dampen growth somewhat in 2015. However, concurrently with this, we anticipate a steady increase in private sector confidence, as agents come to acknowledge that fiscal control is being regained, and that the stance of policy is leading us towards a sustainable macroeconomic position. Moreover, maintenance of positive real interest rates will begin to improve the attractiveness of the kwacha as a currency of investment. This should provide some relief to the exchange rate pressures recently experienced, as well as providing us with an additional policy tool, going forward, for limiting intra-year exchange rate volatility. As confidence, and subsequently investment and consumption levels gradually rises, we would expect activity to begin accelerating towards the end of the calendar year, setting the stage for sustainable, low inflation in 2016 and beyond.

21. We therefore view 2015 as a year to consolidate our position and lay the groundwork for a period of sustained noninflationary growth. Real growth in 2015 is expected to reach 5.5 percent (one percentage point lower than anticipated in our December 2013 MEFP) and to gradually increase to 6 percent in 2017. Inflation will decline to 12 percent by end-2015 and single digit levels towards end-2016. Fiscal restraint and a reliance on concessional foreign borrowing for the majority of our finance needs will allow some reduction in the stock of domestic debt relative to GDP to take place. Strong debt management in the near-to medium term will be implemented to ensure that debt is sustainable and the right balance of costs and

risks is achieved. This will be attained by resuscitating the Debt Management Committee whose membership will be at senior level, which will look at each borrowing, to ascertain its concessionality and to insure debt sustainability. The Government will also continue implementing the Debt Management Reform Programme, that was agreed with IMF and World Bank that is aimed at strengthening the debt management capacity of the Debt and Aid Management Division. We aim to achieve a level of international reserves of at least 3.3 months of import cover by 2016 for general prudential purposes and in order to be better equipped to smooth seasonal fluctuations in the currency. Under a setting of macroeconomic stability, recovering growth, and higher confidence in the domestic currency, we expect the current account deficit to decline by about 1.7 percentage point of GDP by the end of 2015.

POLICIES

Fiscal Policy

22. Our fiscal program for FY2014/15 is calibrated to support a strong disinflation effort and to re-establish private sector confidence in our ability to control fiscal expenditure and safeguard debt sustainability. In an effort to catalyze confidence quickly by enhancing transparency, we will begin the regular monthly publication of our detailed fiscal operations. In light of the significant fiscal risks and uncertainties we face in the year ahead, we have introduced a number of adjustments and contingencies to our approved budget to ensure orderly execution. A circular informing Cabinet of these adjustments was issued as another prior action for completion of the reviews. When fully executed, this adjusted budget will result in about a 2¾ percentage points of GDP improvement in the overall balance relative to last year.

- We have conservatively estimated total revenue at 33 percent of GDP, about ½ percentage points higher than last year. Tax revenue is projected at 0.5 percentage point of GDP below the outturn for last fiscal year to reflect uncertainties in the economic outlook. This is offset by an increase in foreign—mostly project—grants. Furthermore in a bid to enhance compliance and improve mobilization of domestic resources for Government, the Malawi Revenue Authority (MRA), is undertaking a Modernization Program under the theme "Innovation and Modernization". The reforms and initiatives under this program are aimed at improving tax compliance in domestic taxes, promoting the use of enhanced ICT services which include electronic fiscal devices (EFD), and cargo scanners; and widening the tax registration net, among other benefits.

- We have programmed significant adjustment on the expenditure side, where total outlays at 38.9 percent of GDP represent a decline from last year of 2 percentage points of GDP. The majority of this adjustment—5½ percentage points of GDP—falls on current expenditure. In addition to savings of 0.6 percentage points of GDP from not having to fund the elections this year, we have made a number of savings in other areas. In light of their potential second-round inflationary impact, we have contained the nominal increase in public sector wages, and the overall wage bill will decline by more than ½ percentage points of GDP. Domestic interest payments at 4.6 percent of GDP will remain high due to elevated rates associated with the disinflation effort but, with sharply reduced recourse to new domestic financing, this will still represent a decline of almost 1½ percentage points of GDP. Subsidies and other current transfers will continue to absorb a large share of current outlays to safeguard social spending, particularly the Farm Input Subsidy Program (FISP) and a new program for assisting our poorest citizens with housing construction, both of which we feel have sufficiently strong social and productive impact to justify their cost. Fortunately, falling world prices for fertilizers have allowed us to budget for both these programs within the share of GDP expended on the FISP alone last year. On the development side, we will increase capital spending by a 3.2 percentage points to 9.6 percent of GDP.

- On the financing side, domestic borrowing will be sharply reduced, from almost 6 percent of GDP in FY2013/14 to about 2 percent this fiscal year. As a result, and because one of the effects of high inflation is to include in the interest bill an implicit repayment of real principal, net domestic debt stock (excluding the stock of domestic arrears) will fall from 22.2 percent of GDP in 2013 to 19.4 percent in 2014, a substantial reduction. Foreign assistance will be mainly limited to project loans and funds disbursed under the Sector-Wide Assistance Programs.

23. With IMF assistance we have finalized a methodology to regularize the large stock of domestic arrears accumulated from past years. We view this as necessary to restoring private sector confidence in government policies, but remain constrained by the size of the outstanding stock relative to our available resources. All arrears will be verified and audited. Of the arrears that accumulated in FY13/14 we have made arrangements in our fiscal program for cash payments of MK 10 billion in FY14/15. Remaining arrears accumulated in FY13/14 and those incurred before will be regularized through securitization in three equal tranches during the current fiscal year and in FY15/16 and FY16/17 budgets. We will deploy auditors in each ministry, strengthen commitment controls, and hold controlling officers accountable under the PFM Act for willful breach of voted allocations in order to prevent the emergence of new unauthorized payment obligations.

Monetary and Financial Sector Policies

24. Following a year where price increases have remained at unacceptably high levels, we are determined to use monetary policy to place inflation on a clear declining trajectory. To this end, we will ensure that the central bank rate remains well above the rate of inflation, and will use liquidity operations in the interbank and Treasury bill markets to ensure the attainment and maintenance of sharply positive real interest rates in our financial system. We will also improve communication with the commercial banks and other market participants so that they are aware of our commitment to regaining price stability. We anticipate that a steadfast adherence to these policies will gradually increase the transparency and credibility of monetary policy. This credibility will be enhanced by additional amendments to the RBM Act that we submitted to Parliament as a prior action for completion of the reviews. These amendments will visibly limit the possibilities for fiscal dominance by establishing an upper bound on total government borrowing—regardless of instrument—from the RBM in any given year. Supported by this assurance, and by demonstrated fiscal discipline and ongoing improvements in our PFM systems, we anticipate that the private sector will regain confidence that our policy framework and execution is effective and sustainable, with the result that lower inflationary expectations will begin to firm up. As this

happens, and as attractive real returns on domestic assets are maintained, confidence in the kwacha is expected to increase, eventually mitigating the depreciation pressure on the domestic currency that is currently a major source of inflationary risk. Underpinning these policies will be a continued adherence to the flexible exchange rate regime, which we see as a fundamental precondition for the success of our economic adjustment policies.

25. We will combine tight monetary conditions with efforts to safeguard financial sector stability. We migrated to Basel II in early 2014, notably by raising Tier 1 and total capital requirement ratios to 10 percent and 15 percent from 6 percent and 10 percent, respectively. All banks, except two now have higher capital adequacy ratios than required under the new standard. With Fund TA, we have improved prudential norms in the areas of asset classification and provisioning. In addition, we have adopted a prompt corrective action (PCA) framework to strengthen and clarify existing triggers for early remedial action against distressed banks.

26. Third party diagnostic assessments were designed as a tool to identify problem banks as well as banking sector-wide issues. The diagnostic assessments of all banks have now been completed and reviewed. All major areas of concern have been communicated by the RBM to the boards of directors of the respective banks for their action. Reviews of measures taken by each bank to address these concerns will be conducted by the RBM through its regular on-site and off-site supervision activities. Further, in light of the findings of the assessments, the RBM will identify and design an appropriate strategy within the legal framework to address sector-wide issues.

27. Meanwhile, the restructuring process of the two weakest banks is underway and will be completed as soon as possible. A transaction advisor has completed the due diligence on one the banks and has submitted a report on possible restructuring options that encompass its sale or recapitalization. The next steps are to dispatch the Information Memorandum on the bank to all bidders and to select the preferred bidders.

28. The RBM is committed to taking further appropriate steps to address any risks in the financial sector. Efforts to strengthen the supervisory framework of the banking system are underway. This includes enhancement of both on-site and off-site supervision, as well as close monitoring and enforcement of compliance with all prudential norms. Furthermore, an external bank supervision advisor has been hired and commenced work in July 2014, focusing among other things, on enhancement of supervisory skills in the staff of RBM.

29. Loan concentration remains one of the major risk factors in our banking system. This risk has continued to rise from extension of large credit to a limited numbers of borrowers or to specific economic sectors and activities and could lead to challenges in liquidity and capital positions of banks, particularly in the wake of increasing levels of non-performing loans. The RBM will continue to closely monitor loan concentrations in the banking sector and will strictly limit waivers for specific exposures exceeding the loan concentration limit.

30. We also remain committed to strengthening the regulatory framework of the banking system. To this end, amendments to the Banking Act of 2010 and Financial Services Act of 2010 have been submitted to Parliament for enactment (prior action). These two amendments, which were informed by IMF technical assistance recommendations, will align the legal framework for

bank resolution more closely with best practices and provide more options for dealing with problem banks.

Anti-Money Laundering Initiatives

31. In light of the findings of the forensic report that the Cashgate scheme was not an opportunistic theft but rather a complex system of fraud and money laundering, we will address gaps in our regulatory framework. These measures will include amending the Anti-Money Laundering/Controlling the Financing of Terrorism (AML/CFT) Act, the Penal Code and the Corrupt Practices Act, and aligning them with the Financial Action Task Force standards and the United Nations Convention Against Corruption. The Reserve Bank of Malawi will re-evaluate its capacity to monitor and supervise possible breaches of compliance with AML requirements by banks and apply appropriate supervisory sanctions with regard to any breaches of compliance.

Public Financial Management Reform

32. The Government continues to implement the Public Finance and Economic Management Reform Programme (PFEM RP). However, in light of the weaknesses that have been highlighted in the area of Public Finance Management (PFM), Government with technical assistance from the IMF has revised the process of revising the strategy for strengthening PFM systems. It should be noted that the strategy being developed falls within the overall PFEM RP, and that it specifically recommends addressing issues regarding fiscal reporting, bank reconciliation, enforcement of commitment control, improvement of other internal controls and strengthening the overall PFM control environment. In formulating the programme, it has recognised that most PFM rules and regulations of the GoM already follow well establish standards, but their enforcement and compliance remained major challenges. For this reason, the PFM Reform Programme will ensure that the established rules and regulations are followed by adopting a “getting the basics right first” approach. Furthermore, the revised PFM Reform Programme seeks to ensure efficient and effective resource utilization within the public sector, hence maximisation of value for money in public expenditure. Therefore, the programme will seek to bring key officers in all GoM ministries, departments and agencies (MDAs) to know and understand the public finance rules and regulations, and ensure that these are practiced. The Ministry of Finance, Economic Planning and Development will establish the means of identifying where fiscal infractions occur, and of correcting such infractions as quickly and effectively as possible. In this regard, the Ministry of Finance will enhance its capacity to report and deal with laxities in financial management within all MDAs.

33. Government of Malawi implemented EPICOR (version 7.5.5) based IFMIS, to serve the Government in managing public resources efficiently, effectively and transparently.
Several operational and system deficiencies have been observed for a number of years and government has been commissioning a number of studies. These studies have revealed a number of weaknesses that have required urgent attention. We have conducted a comprehensive Business Processes Review and Reengineering (BPR) of the EPICOR based Integrated Financial Management Information System (IFMIS). The review revealed the weaknesses in the system with regards to: inadequacy of the security features, over customization of the system, limited staff manpower that affects segregation of duties, poorly defined and designed process interfaces, among others. Following the review, Government

defined the functional requirements and specifications that will in turn ensure installation of a credible system that addresses the identified shortfalls. This included specifying for a system with robust security and control features, allowance for interfaces with other Government system for seamless flow of information.

34. Government has decided to procure a new system of IFMIS instead of upgrading the current version 7.5.5 to version 10. Government has identified five best and well known IFMIS systems in the world and plans to assess them in order to identify the most suitable one for Government business in Malawi. The EPICOR version 10 will be amongst the systems to be assessed. We have established IFMIS Steering and Technical Committees with clear terms of reference (ToRs) to oversee the procurement and implementation of the new IFMIS.
These committees have already developed an implementation plan for the new system but also a plan for ensuring that the current system is secure and well functioning without disrupting Government business in accounting functions. While enhancements to the current system are already underway, Government has also finalised development of the bidding documents for the new system and procurement processes are expected to commence in January 2014. We believe with proper planning and technical expertise the new system will be up and running in July 2016. This will ensure that time lines are not being missed and milestones are being met as planned.

35. In order to strengthen the scrutiny and audit functions, we have moved the Central Internal Audit Unit to the Ministry of Finance, Economic Planning and Development from the Office of the President and Cabinet in order to revamp the internal audit functions. In recent times, the Government has recruited more internal auditors specialised in various fields other than accounting background alone to ensure that there is diversity in terms of areas of focus. We have engaged Cowater International of Canada to enhance capacity and skills in various types of audits especially in risk based internal audit. Cowater is also providing training in IT Audit.

36. We also plan to place an internal auditor in every MDA so as to detect fiscal infractions early enough for correction. The internal auditors will report to the Ministry of Finance. We are also in the process of engaging private internal auditors to help in transfer of skills to our internal auditors. In addition, we have engaged an experienced advisor in the Ministry of Finance, who will follow up on possible fiscal malpractices as reported by the internal auditors. The advisor will also assist the Ministry of Finance in strengthening the PFM framework.

37. In order to address the cash flow management, we have revitalised the cash management committee meetings and MDAs are being restricted to spend within their approved budgets, and requests for extra-budgetary funding is not being allowed. The Ministry of Finance plans to submit monthly expenditure reports to all MDAs. These will indicate monthly and cumulative expenditure figures as well as available balances on their allocations. This will allow MDAs to plan and limit their expenditures to the allocations. We have strengthened budget monitoring by re-orienting our Budget/desk officers to monitor budget performance better, and are required to submit monthly budget performance reports. This procedure involves the tracking of the accumulation of arrears by MDAs.

38. More importantly, we plan to enforce the legal mandates of the Minister and Secretary to the Treasury in applying sanctions as the requirements of the PFM legal and regulatory

frameworks, including applying sanctions to institutions and individuals that fail to comply with those requirements.

39. To this end, we have developed a PFM strategy to operationalize our agenda and put in place institutional structures to monitor and control our progress. This action plan includes the key recommendations of the FAD technical assistance mission on PFM of which the transfer of revenues to the government's main account will facilitate the reconciliation of government accounts (prior action) as well as elements from the forensic audit report.

The closure of redundant and dormant accounts, the preparation of reports on the stock of arrears, and the audit by an international firm of the status of implementation are key benchmarks.

Program Issues and Monitoring

40. For the fifth review (end-December 2013 test date) the periodic performance criterion (PC) on net domestic assets (NDA)and the indicative target (IT) on reserve money and social spending were not met, in part because of the shortfalls in external financing. For the sixth review, the periodic PC on NDA, net domestic financing (NDF),and the IT on reserve money and social spending were not met owing in part to continued difficulties in program implementation in the face of continued shortfalls in external financing and election uncertainties. For the fifth and sixth reviews, the continuous PC on the contracting of nonconcessional external debt with a maturity of more than one year was not met due to the contracting of the above-mentioned non-concessional loans. The RBM intensified its open market operations to ensure that the September 2014 informal targets on NDA and gross reserves agreed with the staff were met but that on NDF was missed. The RBM will continue to mop up liquidity through over issuance of Treasury bills and maintain a tight stance of monetary policy. Additional informal targets on gross reserves, NDA and NDF were set for end-January 2015 to anchor monetary and fiscal policies. Gross international reserves and NDA were met but NDF was missed due to shortfalls in donor dedicated grants for social sectors. On the basis of these corrective actions we have put in place, we request for a waiver for the nonobservance of the performance criterion for the fifth review on NDA. We also request for a waiver for the nonobservance of the performance criteria for the sixth reviews on NDA, net domestic financing (NDF). For the fifth and sixth reviews, we request waivers for the nonobservance of the performance criteria on nonconcessional external debt maturing in more than one year and on the accumulation of external payments arrears.

41. Program implementation will continue to be monitored with quantitative targets and structural benchmarks (TMU Tables 3 and 6). PCs have been established for June 2015 and December 2015. The seventh review is expected to be completed by mid-September 2015 based on the end-June 2015 test date and the sixth review is expected to be completed by mid-April 2016 based on the end-December 2015 test date.

Attachment II. Technical Memorandum of Understanding

March 2015

1. **This memorandum sets out the understandings between the Malawian authorities and the International Monetary Fund** regarding the definitions of quantitative performance criteria, benchmarks, and indicative targets for the program supported by the ECF arrangement, and the related reporting requirements.

COVERAGE

2. **The central government includes all units of government that exercise authority over the entire economic territory.** Unless otherwise indicated, the central government does not include local governments, the Reserve Bank of Malawi (RBM), or any other public entity with autonomous legal personality. The accounts of the monetary authorities include those of the Reserve Bank of Malawi (RBM). Monetary aggregates under the program are based on the twelve-bank monetary survey.

QUANTITATIVE PERFORMANCE CRITERIA: DEFINITIONS AND DATA SOURCES

A. Budget Support

3. **Definition of budget support:** Budget support includes all grants and foreign financing not directly linked to additional budgetary expenditure. Excluded from this definition is external project financing to fund particular activities, including food security funding from the European Union; loan financing from the IMF; and donor inflows from the U.S. dollar–denominated donor pool accounts for the health SWAp, education SWAp, agricultural SWAps, and National AIDS Commission (NAC) held in the Malawi banking system. Budget support is measured as a cumulative flow from the beginning of the fiscal year. It will be recorded in the original currency of disbursement and then converted into U.S. dollars using the program cross exchange rates listed in Table 6.

B. Floor on Net International Reserves of the RBM

4. **Definition of net international reserves (NIR) of the RBM:** The NIR of the RBM is defined as gross reserve assets minus gross reserve liabilities. For evaluation purposes, the values of all foreign assets and liabilities will be converted into U.S. dollars at each test date using the program cross exchange rates for the various currencies. The program exchange rate of the Malawi Kwacha to the U.S. dollar is set at MK 402 = US$1.

5. **Gross reserve assets of the RBM** are defined in 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).

6. **Gross reserve assets of the RBM** include the following: (i) monetary gold holdings of the RBM; (ii) holdings of SDRs; (iii) the reserve position in the IMF; (iv) foreign convertible currency holdings; (v) foreign currency denominated deposits held in foreign central banks, the Bank for International Settlements, and other banks; (vi) loans to foreign banks redeemable upon demand; (vii) foreign securities; and (viii) other unpledged convertible liquid claims on nonresidents. It excludes the following: (i) any foreign currency claims on residents; (ii) capital subscriptions in international institutions; (iii) foreign assets in nonconvertible currencies; (iv) transfers of foreign currency claims to RBM by other institutional units in Malawi just prior to reporting dates with accompanying reversals of such transfers soon after those dates; (v) assets obtained through currency swaps of less than three months duration; (vi) gross reserves that are in any way encumbered or pledged, including, but not limited to: (a) assets blocked when used as collateral for third party loans and third-party payments, or pledged to investors as a condition for investing in domestic securities; (b) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and (c) foreign reserves blocked for letters of credit.

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

Adjusters Applied to NIR Program Ceiling

8. The program floor on NIR will be adjusted as follows if budget support, inflows from donor accounts for the social sectors, and external debt service to the World Bank and the African Development Bank (ADB) deviate from their programmed levels:

- **Budget support:** The floor on the NIR of the RBM will be adjusted upward by the full amount by which the cumulative receipts from the budget support are greater than US$10 million above the program baseline (as defined in Table A). The floor on NIR of the RBM will be adjusted downward by the amount by which the cumulative receipts from budget support are less than the program baseline. This downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 9.

Table A. Program Baseline: Projected Budget Support, March–December, 2015
(In millions of USD, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Budget support	0.0	17.7	0.0	0.0

[1]Fiscal year runs from July 1 to June 30 of the following year

- **Donor pool accounts for the social sector,** including health and education SWAps, and National AIDS Commission (NAC): The floor on the NIR of the RBM will be adjusted downward by the amount by which the donor inflows from the U.S. dollar–denominated donor accounts for SWAps and NAC held in the RBM are smaller than the program baseline (as defined in Table B). This downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 9. These donor inflows are measured as the cumulative receipts by the budget from the beginning of the fiscal year. They will be recorded in the original currency of disbursement and then converted to U.S. dollars using the above defined program cross exchange rates.

Table B. Program Baseline: Projected Inflows from Donor Accounts for the Social Sector, March–December, 2015
(In millions of USD, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Donor inflows	47.7	51.4	6.8	37.9

[1]Fiscal year runs from July 1 to June 30 of the following year

- **Debt service payments:** The floor on NIR of the RBM will be adjusted upward (downward) by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank fall short of (exceed) the program baseline (as defined in Table C). Debt service payments will be measured as the cumulative payments from the beginning of the fiscal year. They will be recorded in the original currency of payment and then converted to U.S. dollars using the above defined program cross exchange rates. This downward adjustment of the NIR floor will be subject to the limitations outlined in paragraph 9.

Table C. Projected Debt Service Payments to World Bank and AfDB, March–December, 2015
(In millions of USD, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Debt service	8.2	12.1	3.9	7.8

[1]Fiscal year runs from July 1 to June 30 of the following year

9. **Cumulative adjustment to the NIR program target:** Notwithstanding the adjustments stipulated in paragraph 8, the total downward adjustment to the NIR program target from the combined impact of a (i) a shortfall of budget support relative to the program projections; (ii) a shortfall of inflows to the donor accounts for the social sector relative to the program projections; and (iii) any excess of debt service payments to the World Bank and the African Development Bank (ADB) relative to the program projections, will be subject to a cumulative limit of US$15 million.

C. Net Foreign Assets of the RBM

10. **Definition of Net Foreign Assets (NFA) of the RBM:** The NFA of the RBM are defined as its gross foreign assets (GFA) minus its gross foreign liabilities. Gross foreign liabilities are equal to gross reserve liabilities as defined in paragraph 7, plus any other foreign liabilities not listed in that paragraph.

11. **Gross foreign assets (GFA) of the RBM** are defined as gross reserves assets as defined in paragraph 6, plus (i) any foreign currency claims on residents; (ii) capital subscriptions in international institutions; (iii) foreign assets in nonconvertible currencies; (iv) transfers of foreign currency claims to RBM by other institutional units in Malawi just prior to reporting dates with accompanying reversals of such transfers soon after those dates; (v) assets obtained through currency swaps of less than three months duration; (vi) gross reserves that are in any way encumbered or pledged, including, but not limited to: (a) assets blocked when used as collateral for third party loans and third-party payments, or pledged to investors as a condition for investing in domestic securities; (b) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and (c) foreign reserves blocked for letters of credit.

D. Reserve Money of the RBM

12. **Definition of reserve money of the RBM (RM):** Reserve money is defined as the sum of currency issued by the RBM, including currency outside banks, the vault cash of commercial banks, and balances of commercial banks' accounts with the RBM. Commercial banks' accounts with the RBM include required reserves held for local currency and foreign currency deposits, other domestic currency liabilities, and other demand and time deposits held with the RBM.

E. Ceiling on Net Domestic Assets of the RBM

13. For program proposes, net domestic assets (NDA) of the RBM are defined in kwacha terms as reserve money less NFA of the RBM at the program exchange rate.

Adjusters Applied to NDA Program Ceiling

14. The program ceiling on NDA will be adjusted as follows if budget support, inflows from donor accounts for the social sector, and external debt service to the World Bank and the African Development Bank (ADB) deviate from their programmed levels:

- **Budget support:** For the purposes of this adjustor, cumulative receipts from budget support will be measured in the foreign currency of disbursement and converted to kwacha using the program exchange rates. The ceiling on NDA of the RBM will be adjusted downward by the amount that cumulative receipts from budget support exceed the sum of the program baseline (as defined in Table D) and the kwacha equivalent of US$10 million. The kwacha equivalent of US$10 million will be calculated as US$10 million multiplied by the program exchange rate. The ceiling on NDA of the RBM will be adjusted upward by the amount that cumulative receipts from budget support (in kwacha) fall short of the program baseline, with this upward adjustment to the NDA ceiling subject to the limitations described in paragraph 15. The kwacha equivalent of the upward adjustment will be calculated as the US dollar value of the adjustment multiplied by the program exchange rate.

Table D. Program Baseline: Projected Budget Support, March–December, 2015
(In billions of kwacha, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Budget support, at the program exchange rate	0.0	8.0	0.0	0.0
Budget support plus kwacha equivalent of US$10 mil, at the program exchange rate	0.0	12.2	0.0	0.0

[1]Fiscal year runs from July 1 to June 30 of the following year

- **Donor pool accounts for the social sector** (including health, education, and NAC): For the purposes of this adjustor, cumulative receipts from donor [pool] accounts for the social sector will be measured in the foreign currency of disbursement and converted to kwacha using the program exchange rates. The ceiling on NDA of the RBM will be adjusted upward by the amount by which the donor inflows to the budget (in kwacha) from the U.S. dollar–denominated donor accounts for the SWAps and NAC held in the RBM fall short of the donor inflow to those accounts in the program baseline (as defined in Table E). This upward adjustment to the NDA ceiling will be subject to the limitations described in paragraph 15. The kwacha equivalent of the upward adjustment will be calculated as the US dollar value of the adjustment multiplied by the program exchange rate.

Table E. Program Baseline: Projected Inflows from Donor Accounts, March–December, 2015
(In billions of kwacha, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Donor inflows, at the program exchange rate	20.0	21.6	2.9	15.9

[1]Fiscal year runs from July 1 to June 30 of the following year

- **Debt service payments:** For the purposes of this adjustor, cumulative debt service payments (from the beginning of the fiscal year) will be measured in the foreign currency of payment and converted to kwacha using the program exchange rates. The ceiling on NDA of the RBM will be adjusted downward (upward) by the full cumulative amount by which debt service payments to the World Bank and the ADB falls short of (exceeds) the program baseline (as defined in Table F). The upward adjustment to the NDA ceiling will be subject to the limitations described in paragraph 15.

Table F. Program Baseline: Projected Debt Service Payments, March–December, 2015
(In billions of kwacha, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Debt service, at the program exchange rate	3.3	4.9	1.7	3.1

[1]Fiscal year runs from July 1 to June 30 of the following year

- **Additional adjustment for changes in the liquidity reserve requirement:** The ceiling on NDA of the RBM will be adjusted downward for a decrease in the reserve requirement ratio on domestic deposits, and will be adjusted upward for an increase in the ratio. The adjustment will be spread equally over two quarters, starting in the quarter in which the reserve requirement ratio is reduced. The adjuster will be calculated as follows: (one minus the existing required fraction of reserve assets) multiplied by (the program baseline required reserve ratio minus the new required reserve ratio) multiplied by (the amount of average reservable deposit liabilities in commercial banks during the last month before the change in regulation). The program baseline required reserve ratio was 15.5 percent at end-June 2014.

15. **Cumulative adjustment to the NDA program target:** Notwithstanding the adjustments outlined above in paragraph 14, the total upward adjustment to NDA from the impact of (i) a shortfall of budget support relative to the program assumptions; (ii) a shortfall of inflows to

the donor accounts for the social sector relative to the program assumptions; and (iii) an excess of debt service payments to the World Bank and the African Development Bank relative to the program assumptions will be capped at the kwacha equivalent of US$15 million. The kwacha equivalent of US$15 million will be calculated as US$15 million multiplied by the program exchange rate. The adjustment to the NDA ceiling for changes in the liquidity reserve requirement is independent of the other adjustments and is not subject to limitation.

F. Ceiling on Central Government Net Domestic Borrowing (CGDB)

16. **Definition of central government net domestic borrowing (CGDB):** CGDB is defined as the sum of (i) net borrowing from the RBM (including ways and means advances, loans, holdings of local registered stocks, government bonds, and holdings of treasury bills and treasury notes minus deposits); plus (ii) net borrowing from commercial banks (including advances, holdings of local registered stocks, and holdings of treasury bills and treasury notes minus deposits); plus (iii) net borrowing from nonbanks (including, but not limited to, holdings of local registered stocks and holdings of treasury bills and treasury notes); plus (iv) holdings of promissory notes. Excluded from the CGDB ceiling are (i) promissory notes issued to cover exchange rate valuation losses of RBM; and (ii) government securities issued in 2014 and 2015 to clear government domestic arrears up to a maximum exclusion of MKW 157 billion. Treasury bills and locally registered stocks will be valued at cost rather than face value. The ceiling is measured as the change in the stock of CGDB cumulative from the beginning of the fiscal year, including promissory notes and securities transferred to the RBM from the treasury since the beginning of the fiscal year. Transfers from extra-budgetary funds will not be considered revenues for this performance criterion. Instead, they will be treated as domestic borrowing from the private sector (as their accounts are outside the definition of government). Asset sales or privatization revenues will be accounted for under financing as a separate category, separate from domestic or foreign financing in calculating CGDB.

Adjusters Applied to CGDB Program Ceiling

17. The program ceiling on CGDB will be adjusted as follows if budget support, inflows from donor accounts for the social sector, and external debt service to the World Bank and the African Development Bank deviate from their programmed levels.

18. The program ceiling on CGDB will be adjusted as follows if budget support, inflows from donor accounts for the social sector, and external debt service to the World Bank and the African Development Bank deviate from their programmed levels.

- **Budget support:** For the purposes of this adjustor, cumulative receipts from budget support will be measured in the foreign currency of disbursement and converted to kwacha using the program exchange rates. The program ceiling on CGDB will be adjusted upward by the full amount by which cumulative receipts from budget support are less than the program baseline (as defined in Table D). This upward adjustment to CGDB will be subject to the limitations described in paragraph 20. In the event of excess budget support, the ceiling on CGDB will be adjusted downward by the amount that cumulative receipts from budget support exceed the sum of the program baseline (as defined in Table D) and the kwacha equivalent of US$10 million. The kwacha equivalent of US$10 million will be calculated as US$10 million multiplied by the program exchange rate.

- **Donor pool accounts for the social sector,** including health and education SWAps, and NAC: For the purposes of this adjustor, cumulative receipts from donor pool accounts for the social sector will be measured in the foreign currency of disbursement and converted to kwacha using the program exchange rates. The ceiling on CGDB will be adjusted upward by the amount by which donor inflows to the budget from the U.S. dollar–denominated donor accounts for health, education, and other SWAps, and NAC held in RBM fall short of the program baseline (as defined in Table E). This upward adjustment to CGDB will subject to the limitations described in paragraph 19.

- **Debt service payments:** For the purposes of this adjustor, cumulative debt service payments (from the beginning of the fiscal year) will be measured in the foreign currency of payment and converted to kwacha using the program exchange rates. The ceiling (floor) on CGDB will be adjusted downward (upward) by the full cumulative amount by which debt service payments to the World Bank and the ADB fall short of (exceed) the program baseline (as defined in Table F). This upward adjustment to CGDB will subject to the limitations described in paragraph 20.

19. **Cumulative adjustment to the CGDB program target:** The total upward adjustment to CGDB from a shortfall of (i) budget support relative to the program baseline, (ii) donor inflows to the donor accounts for the social sector relative to the program baseline and (iii) an excess of actual debt service payments to the World Bank and the African Development Bank (ADB) relative to the program baseline will be capped at US$15 million. The kwacha equivalent of US$15 million will be calculated as US$15 million multiplied by the program exchange rate.

G. Ceiling on External Payment Arrears

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

H. Ceiling on Non-concessional External Debt

21. **Definition of non-concessional external debt:** The definition of debt, for program purposes, is set out in Executive Board Decisions No. 6230–(79/140) August 3, 1979, and as amended by Decisions No. 11096–(95/100), October 25, 1995; 12274–(00/85) August 24, 2000;

and 14416–(09/91), August 31, 2009. For program purposes, short-, medium- and long-term debt is non-concessional if it includes a grant element of less than 35 percent, as indicated in Decision No. 11248–(96/38), April 15, 1996. The grant element is calculated using a discount rate of 5 percent. The ceiling on non-concessional debt applies to the contracting and guaranteeing of debt with nonresidents by the central government, the RBM, public enterprises, and other official sector entities, unless an explicit selective exclusion is made per paragraph 24.
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.

22. **Definition of short-term debt:** Short-term debt is outstanding stock of debt with an original maturity of one year or less.

23. **Definition of medium- and long-term debt:** Medium- and long-term debt is outstanding stock of debt with a maturity of more than one year.

24. **Excluded from the limit on non-concessional external debt is the following:** (i) the use of IMF resources; (ii) any kwacha-denominated treasury bill and local registered stock holdings by nonresidents purchased from the secondary market; (iii) debts classified as international reserve liabilities of the RBM; (iv) new debt issued to restructure, refinance, or repay existing non concessional external debt as of December 31, 2014, up to the amount actually used for the above-mentioned purposes; (v) normal import financing; and (iv) arrangements to pay overtime obligations arising from judicial awards to external creditors—a financing arrangement for imports is considered to be "normal" when the credit is self-liquidating.

QUANTITATIVE INDICATIVE TARGETS AND STRUCTURAL BENCHMARKS

25. **Reserve money of the RBM:** Reserve money of the RBM is defined in paragraph 12 above. The program baseline for reserve money is defined in Table G. No adjusters are applicable to reserve money targets for program purposes.

Table G. Projected Stock of Reserve Money, March–December, 2015
(In billions of kwacha, cumulative within the fiscal year[1])

	Mar-15	Jun-15	Sep-15	Dec-15
Reserve money	223.4	243.8	248.2	260.5

[1]Fiscal year runs from July 1 to June 30 of the following year

26. **Social spending:** Using functional classification of expenditure, social spending is defined as the sum of central government spending on health, education, the farm input subsidy program, the cement and iron sheet program, and government social protection (comprising

government expenditures by the Ministry of Gender, Children, and Social Welfare, the Ministry of Disability and Elderly Affairs, the local development fund, and the Poverty and Disaster Management Cost Center under the Office of the Vice President. In order to maintain Malawi's commitment and progress toward poverty reduction and the MDGs, the social spending allocations in the government budget will not subject to downward adjusters under the program. Quarterly social spending under this definition is presented in Table 8.

27. **Domestic arrears:** Domestic arrears are defined as overdue payment obligations of the central government to residents, including on wages and salaries, pensions, transfers, domestic interest, goods and services, obligations arising from court cases, legally established compensation claims, and tax refunds. Payments on wages and salaries, pensions, transfers, court-established obligations, and compensations are in arrears when they remain unpaid for more than 30 days beyond their due date. Domestic interest payments are in arrears when the payment is not made on the due date. Payments for goods and services are deemed to be in arrears if they have not been made within 90 days of the date of invoice, or—if a grace period has been agreed—within the contractually agreed grace period.

28. **Structural benchmarks** are contained in Tables 5 and 6.

Table 1. Malawi: Quantitative Targets, 2013[1]

	Target type [2]	End-June 2013 (IT) Prog.[10]	Adj. Prog.[10]	Actual	Status	End-September 2013 (PC) Prog.[10]	Adj. Prog.[10]	Actual	Status	End-December 2013 (PC) Prog.[10]	Adj. Prog.[10]	Actual	Status
I. Monetary targets (millions of kwacha)													
1. Ceiling on net domestic assets of the RBM [3, 4, 5, 6]	PC	108,487	110,839	72,920	M	87,854	59,365	81,224	NM	107,710	110,715	120,781	NM
2. Ceiling on reserve money[3]	IT	106,902	106,902	126,570	NM	110,017	110,017	134,756	NM	135,223	135,223	156,899	NM
II. Fiscal targets (millions of kwacha)													
3. Ceiling on central government's net domestic borrowing [5,6,7]	PC	-18,605	-16,253	-2,492	NM	-5,218	-2,018	58,685	NM	72,042	75,047	73,683	M
4. Floor on social spending (cumulative from beginning of fiscal year)[8]	IT	185,511	185,511	181,764	NM	15,330	15,330	48,952	M	106,617	106,617	105,007	NM
III. External sector targets (US$ millions, unless otherwise indicated)													
5. Floor on net international reserves of the RBM[3, 5, 6]	PC	53	46	270	M	127	117	254	M	188	177	215	M
6. Ceiling on the accumulation of external payments arrears [7,9]	PC	0	0	0		0	0	0	M	0	0	2.2	NM
7. Ceiling on new nonconcessional external debt maturing in more than one year [7,9]	PC	0	0	142	NM	0	0	0	M	0	0	145.3	NM
8. Ceiling on new nonconcessional external debt maturing in one year or less [7,9]	PC	0	0	0		0	0	0	M	0	0	0	M
9. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [9,10]	PC				M				M				M
Memorandum items:													
Net foreign assets of the RBM (US$ millions)		-5		151		69		167		86		113	
Budget support (US$ millions)		245		244		50		9		27		19	
Budget support (millions of kwacha)		78,355		78,219		15,978		2,846		8,645		6,080	
Debt service payments to the World Bank and AfDB (US$ millions)		6		6		1		1		5		4	
Debt service payments to the World Bank and AfDB (millions of kwacha)		1,920		1,936		465		465		1,475		1280	
Health SWAp receipts (millions of kwacha)		11,290		15,040		3,194		4,815		6,971		3,711	
Education SWAp receipts (millions of kwacha)		23,245		1,764		4,800		3,548		9,191		13,532	
NAC receipts (millions of kwacha)		12,281		441		4,288		999		3,070		0	
Program exchange rate (kwacha per US$)		320		320		320		320		320		320	

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

[1] Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.

[2] "PC" means Performance Criterion, and "IT" means Indicative Target.

[3] Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).

[4] Target is subject to an adjuster for liquidity reserve requirement.

[5] Targets are subject to an adjuster for budget support and debt service payments.

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

[7] Defined as a cumulative flow from the biginning of the fiscal year.

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

[9] Evaluated on a continuous basis.

[10] IMF Country Report No. 14/37

Table 2. Malawi: Quantitative Targets, 2014[1]

	Target type [2]	End-Mar. 2014 (IT)				End-June 2014				End-Sep. 2014 (IT)			
		Prog.[10]	Adj. Prog.	Act.	status	Prog.[10]	Adj Prog.	Act.	status	Prog.[10]	Adj Prog.	Act.	status
I. Monetary targets (millions of kwacha)													
1. Ceiling on net domestic assets of the RBM [3, 4, 5, 6]	PC	113,035	115,595	117,434	NM	94,817	97,697	142,547	NM	97,701	97,701	136,885	NM
2. Ceiling on reserve money[3]	IT	134,392	134,392	169,100	NM	145,225	145,225	193,201	NM	151,232	151,232	192,097	NM
II. Fiscal targets (millions of kwacha)													
3. Ceiling on central government's net domestic borrowing [5,6,7]	PC	52,018	54,578	81,548	NM	6,622	9,502	93,147	NM	-20,023	-18,423	19,521	NM
4. Floor on social spending (cumulative from beginning of fiscal year)[8]	IT	170,424	170,424	167,106	NM	214,832	214,832	206,961	NM	...			
III. External sector targets (US$ millions, unless otherwise indicated)													
5. Floor on net international reserves of the RBM[3, 5, 6]	PC	169	161	262	M	260	251	259	M	269	265	475	M
6. Ceiling on the accumulation of external payments arrears [7,9]	PC	0	0	4.2	NM	0	0	9.2	NM	0	0	14	NM
7. Ceiling on new nonconcessional external debt maturing in more than one year [7,9]	PC	0	0	145.3	NM	0	0	149.3	NM	0	0	149.3	NM
8. Ceiling on new nonconcessional external debt maturing in one year or less [7,9]	PC	0	0	0	M	0	0	0	M	0	0	0	M
9. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [9]	PC								M				M
Memorandum items:													
Net foreign assets of the RBM (US$ millions)		67		161		158		158		167		173	
Budget support (US$ millions)		111		35		167		67		209		67	
Budget support (millions of kwacha)		35,445		11,130		53,509		21,361		66,878		21,361	
Debt service payments to the World Bank andAfDB (US$ millions)		6		4		7		6		2		2	
Debt service payments to the World Bank and AfDB (millions of kwacha)		1,777		1,376		2,306		1,920		529		529	
Health SWAp receipts (millions of kwacha)		7,234		-4,968		8,834		-4,968		2,433		1,941	
Education SWAp receipts (millions of kwacha)		13,600		14,466		15,567		14,466		2,829		994	
NAC receipts (millions of kwacha)		3,070		1,859		4,030		3,476		971		0	
Program exchange rate (kwacha per US$)		320		320		320		320		320		320	

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

1 Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.

2 "PC" means Performance Criterion, and "IT" means Indicative Target.

3 Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).

4 Target is subject to an adjuster for liquidity reserve requirement.

5 Targets are subject to an adjuster for budget support and debt service payments.

6 Targets are subject to an adjuster for donor-funded social sector expenditures consistent with the TMU.

7 Defined as a cumulative flow from the beginning of the fiscal year.

8 Priority social spending as defined in the TMU and quantified in the authorities'

9 Evaluated on a continuous basis.

10 IMF Country Report No. 14/37

Table 3. Malawi: Quantitative Targets, 2015[1]

	Target type [2]	End-March 2015 (IT)		End-June 2015		End-Sept 2015 (IT)		End-Dec 2015	
		Prog.	Act.	Prog.	Act.	Prog.	Act.	Prog.	Act.
I. Monetary targets (millions of kwacha)									
1. Ceiling on net domestic assets of the RBM [3, 4, 5, 6]	PC	71,574		87,033		73,959		83,792	
2. Ceiling on reserve money[3]	IT	223,402		243,828		248,213		260,545	
II. Fiscal targets (millions of kwacha)									
3. Ceiling on central government's net domestic borrowing [5,6,7]	PC	59,083		37,030		40,407		58,162	
4. Floor on social spending (cumulative from beginning of fiscal year)[8]	IT	205,055		257,430		54,725		146,687	
III. External sector targets (US$ millions, unless otherwise indicated)									
5. Floor on net international reserves of the RBM[3, 5, 6]	PC	475		487		531		537	
6. Ceiling on the accumulation of external payments arrears [7,9]	PC	0		0		0		0	
7. Ceiling on new nonconcessional external debt maturing in more than one year [7,9]	PC	0		0		0		0	
8. Ceiling on new nonconcessional external debt maturing in one year or less [7,9]	PC	0		0		0		0	
9. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [9]	PC								
Memorandum items:									
Net foreign assets of the RBM (US$ millions)		378		390		433		440	
Budget support (US$ millions)		0		18		0		7	
Budget support (millions of kwacha)		0		8000		0		3224	
Debt service payments to the World Bank andAfDB (US$ millions)		8.22		12.12		3.90		7.80	
Debt service payments to the World Bank and AfDB (millions of kwacha)		3,304		4,872		1,568		3,136	
Health SWAp receipts (millions of kwacha)		15,668		15,668		2,114		14,993	
Education SWAp receipts (millions of kwacha)		1,743		3,384		0		0	
NAC receipts (millions of kwacha)		0		0		164		332	
Program exchange rate (kwacha per US$)		402		402		402		402	

Sources: IMF staff projections.

[1] Targets are defined in the technical memorandum of understanding (TMU). Presentation uses stocks for all PCs except for the ceiling on the government's net domestic borrowing.

[2] "PC" means Performance Criterion, and "IT" means Indicative Target.

[3] Defined as stocks. All stocks of NDA adjusted for consistency with the program definition (specified in the TMU).

[4] Target is subject to an adjuster for liquidity reserve requirement.

[5] Targets are subject to an adjuster for budget support and debt service payments.

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

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

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

9 Evaluated on a continuous basis.

Table 4. Malawi: Informal Quantitative Targets

	End-Sept 2014			End-Dec 2014			End-January 2015		
	Informal Targets	Actual	Status	Proj.	Actual	Status	Informal targets	Actual	Status
Ceiling on net domestic assets of the RBM (millions of kwacha)[1]	132,004	121,696	Met	84,632	66,329	Met	94,632	11,918	Met
Ceiling on central government's net domestic borrowing (millions of kwacha)[2]	8,527	19,521	Not Met	44,000	36,172	Met	46,000	58,068	Not Met
Floor on gross official reserves (US$ millions)[3]	450	457	Met	515	586	Met	500	631	Met

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

[1]NDA as reported by the RBM.

[2]Defined as a cumulative flow from the beginning of the fiscal year.

[3]Gross official reserves equal gross reserves assets as defined in the TMU.

Table 5. Malawi: Prior Actions

Measure	Target date	Macro Rationale	Status
Prior Action			
Fiscal policy			
Implement expenditure cuts necessary to limit net domestic financing under the program ceiling for the fiscal year 2014/15 and issue a memo to cabinet outlining new expenditure ceilings.	End-February 2015	To ensure consistency between the budget and the program.	Met
Public financial management			
Ministry of Finance to issue a letter to the central bank to transfer revenues to main government account (MG1)	End-February 2015	First step towards better cash management and reconciliation of accounts.	Met
Incorporate the main government bank accounts in IFMIS, including MG1 account and the six operational accounts, namely (i) salaries, (ii) other recurrent transactions, (iii) development, (iv) statutory, (v) advances, and (vi) deposits.	End-February 2015	Integrate key accounts into IFMIS progressively to ensure an improved accounting, cash management and reconciliation of accounts.	Met
Monetary policy			
Submit to parliament legislative amendments to limit RBM's credit to government to a 10 percent of the previous year's revenue.	End-February 2015	Reduce fiscal dominance to enhance effectiveness of monetary policy.	Met
Financial sector			
Submit to parliament amendments to the Banking Act and Financial Services Act in line with those recommended by March 2013 Fund (LEG) TA mission.	End-February 2015	Promote financial stability by enhancing RBM's bank resolution powers and tools.	Met

Sources: IMF staff and Malawian authorities

Table 6. Malawi: Structural Benchmarks, 2015

Measures	Target date	Macro Rationale
Public financial management		
Publish detailed monthly budget execution data by vote on the Ministry of Finance's website no later than 6-weeks after execution.	End-March 2015	To foster greater fiscal transparency and monitoring.
Reconcile all government bank accounts MG1 and six operational accounts and ways and means for all 2014 transactions signed by the Accountant General and Secretary of the Treasury.	End-March 2015	To strengthen cash planning, reconciliation of accounts, and improving the integrity of the accounting systems.
Review all bank accounts and close redundant and dormant accounts and provide an updated list from the central bank certified by the Accountant General.	End-March 2015	To strengthen cash planning, reconciliation of accounts, and improving the integrity of the accounting systems.
Prepare a report on the flow and stock of arrears at the end of each quarter starting with with end-September 2014 and within two months of the end of each six months.	End-June 2015	To monitor emergence of arrears.
Produce and publish monthly summary bank account control reports.	End-September 2015	To improve transparency and control.
Issue reports by international audit firms on bank reconciliations and summary bank account control reports.	End-September 2015	To improve transparency and restore public confidence.
Issue a report by an International firm confirming the status of implementation of forensic audit recommendations in the PFM domain.	End-December 2015	Foster greater transparency.
Financial sector		
Prepare a strategy to address banking sector wide issues raised by the third-party diagnostics assessments, including the high loan concentration among banks.	End-March 2015	To safeguard the stability of the financial system.
RBM to obtain from all undercapitalized banks to submit detailed, quarterly monitorable recapitalization and restructuring plans showing how they will reach the minimum capital adequacy level within one year.	End-April 2015	To safeguard the stability of the financial system.
RBM to obtain from all banks with significant deficiencies (e.g.: on loan documentation) reported by the diagnostic assessments to submit plans to address the deficiencies within one year.	End-June 2015	To safeguard the stability of the financial system.
RBM to develop contingency plans to intervene and resolve banks if they do not submit or comply with acceptable recapitalization plans.	End-June 2015	To safeguard the stability of the financial system.
Submit to parliament amendments to the AML/CFT Act, the Penal Code, and the Corrupt Practices Act in line with the FATF standard and the United Nations Convention against Corruption (UNCAC).	End-June 2015	To ensure that: (i) enhanced customer due diligence is required with regard to domestic politically exposed persons ; (ii) suspicious transactions are reported when there is a suspicion that funds are the proceeds of a criminal activity ; (iii) there is adequate transparency of legal persons and arrangements; (iv) acts of corruption are adequately criminalized and constitute predicate crimes to money laundering; (v) self-self-laundering is criminalized, and (vi) there are appropriate administrative sanctions for failure to comply with AML/CFT requirements.
RBM issue a detailed report on compliance with regulations on loan classification and provisioning and concentration limits in line with existing directives.	End-September 2015	To safeguard the stability of the financial system.
RBM, in its supervisory capacity, to follow-up on possible breaches of compliance with the AML legal framework by banks revealed by the audit report, by applying supervisory actions mandated by the AML legal framework with regard to any breaches of compliance, including sanctions.	End-December 2015	To ensure compliance with AML standards.

Sources: IMF staff and Malawian authorities

Table 7. Malawi: Cross Rates for Nominal Exchanges Rates and Gold Price for Program

	September 2014
Gold bullion LBM[1] US$/troy ounce	1,236.55
SDR to US$ exchange rate	0.667
Euro to US$ exchange rate	0.775
Yen to US$ exchange rate	107.244
Yuan to US$ exchange rate	6.153
Rand to US$ exchange rate	10.978
UK £ to US$ exchange rate	0.614

Source: IMF (International Financial Statistics)

[1] LBM connotes London Bullion Market

Table 8. Malawi: Social Spending: FY2013/14
Millions of Kwacha

Category	Q1 Actual	Q2 Proj.	Q3 Proj.	Q4 Proj.	Total Proj.
Health Expenditure	**15,321**	**18,822**	**17,782**	**17,223**	**69,146**
Wages	9,280	7,259	7,259	7,259	31,058
Other Recurrent	5,756	9,537	8,497	8,197	31,988
Ministry of Health ORT	2,797	4,785	3,791	3,791	15,165
Local Assemblies ORT	2,893	4,518	4,556	4,256	16,222
Subvented Organisations	66	234	150	150	601
Development expenditure	284	2,025	2,025	1,766	6,100
Education Expenditure	**30,353**	**30,738**	**30,929**	**29,973**	**121,993**
Wages	16,933	14,470	14,470	14,470	60,343
Other Recurrent	13,089	14,858	13,974	13,972	55,891
Ministry of Education ORT	3,378	4,014	3,696	3,696	14,784
Local Assemblies ORT	1,852	2,265	2,059	2,057	8,232
Subvented Organisations	7,859	8,579	8,219	8,219	32,876
Development expenditure	331	1,411	2,486	1,532	5,758
Farm Input Subsidy Program	**5,487**	**31,777**	**13,222**	**0**	**50,485**
Cement and Iron Sheets Subsidy	**0**	**3,000**	**1,000**	**3,000**	**7,000**
Gender, Children, Disability and Social	**436**	**629**	**516**	**514**	**2,095**
Wages	257	231	231	231	949
Other Recurrent	157	250	203	203	814
Development expenditure	22	148	82	80	332
Total Gender, Children, Disability and Social	**436**	**629**	**516**	**514**	**2,095**
Local Development Fund	**178**	**2,072**	**1,125**	**1,125**	4,500
Poverty and Disaster Management Cost	**37**	**25**	**26**	**26**	**114**
Wages	20	9.7	9.7	10	49
Other Recurrent	17	15	16	16	65
Total Social Expenditure	**52,247**	**87,692**	**65,116**	**52,375**	**257,429**

Source: Malawian authorities

Table 9. Malawi: Reporting Requirements

Data Description	Data Freq.	Reporting Agency	Reporting Freq.	Delivery Lag	Delivery Date	Delivery Mode
Gross international reserves, exchange rate, and foreign exchange purchases and sales	D	RBM	W	2	F	E
Reserve money and its components (NDA and NFA), OMO transactions, and RBM conversion of treasury bills; RBM balance sheet	W	RBM	M	30	30	E
Daily exchange rate	D	RBM	W	1	F	E
Treasury bill auction results	W	RBM	W	2	F	E
Spread between bureau midrate and the official exchange midrate	W	RBM	M	30	30	E
Spread between commercial bank midrate and the official exchange midrate	W	RBM	M	30	30	E
International Reserve and Foreign Currency Liquidity Data Template	M	RBM	M	30	30	E
NIR and its components	W	RBM	W	7	F	E
Central government domestic borrowing	M	RBM	M	30	30	E
Interest rates	M	RBM	M	30	30	E
Holdings of local registered stocks and treasury bills	M	RBM	M	30	30	E
Detailed issue and maturity profile for treasury bills	M	RBM	M	30	30	E
Excess reserves by bank	W	RBM	M	30	30	E
Details of project and balance of payment support	M	RBM	M	30	30	E
FCDA Holdings	M	RBM	M	30	30	E
RBM foreign exchange cash flow	M	RBM	M	30	30	E
Foreign exchange exposure limits by bank	M	RBM	M	30	30	E
Bank statements of the Health SWAp account held at RBM	M	RBM	M	30	30	E
Full banking survey (on monthly basis)	M	RBM	M	45	15	E
Financial soundness indicators by banks	Q	RBM	Q	45	T15	E
NAC consolidated statement of sources and uses of funds (cashflow stateme	M	MOF	M	30	30	E
Health SWAp statement of sources and uses of funds	M	MOF	M	30	30	E
Fiscal table (GFS) including revenue, expenditure, and financing	M	MOF	M	30	30	E
Revenue data (from MRA)	M	MOF	M	30	30	E
D\ata on expenditure for domestically financed capital projects	M	MOF	M	30	30	E
New external loans contracted or guaranteed by the central government[1]	Q	MOF	Q	30	T30	E
External debt services (actual and projections)	Q	MOF	Q	30	T30	E
Borrowing of all major parastatals[2]	Q	MOF	Q	45	T15	E
Annual Financial reports of the nine (9) major parastatals and MSB	A	MOF	Q	90	30	H
Report on IMF program performance	Q	MOF	Q	45	T15	E
Statement on new arrears	Q	AuG	Q	45	T15	E
Consumer price index and monthly statistical bulletin	M	NSO	M	30	30	E
Import and export data	M	NSO	M	45	T15	E
Balance of payments, and quarterly statistical bulletin	Q	NSO	Q	45	T15	E
National accounts, balance of payments, and quarterly statistical bulletin	A	NSO	BA	45	T15	E

D-Daily, W-Weekly, M-Monthly, Q-Quarterly, BA-Bi-annual, F-Friday, 30-Every 30th, T30-Every third 30th, E-Electronic, H-Hard Copy

[1] 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.

[2] Agriculture Development and Marketing Corporation (ADMARC), Electric Supply Company of Malawi (ESCOM), Blantyre Water Board, Lilongwe Water Board, Southern Region Water Board, Northern Region Water Board, Central Region Water Board, Malawi Housing Corporation, Malawi Communications Regulatory Authority.