International Monetary Fund

Malawi and the IMF

Press Release:
IMF Executive Board Completes First Review Under the Extended Credit Facility for Malawi and Approves US$20 Million Disbursement
December 19, 2012

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

December 5, 2012

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

December 5, 2012

Madam Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431
USA

Dear Madam Lagarde:

On July 23, 2012, the Executive Board of the International Monetary Fund (IMF) approved Malawi's request for a new three year arrangement under the Extended Credit Facility (ECF) in the amount of SDR 104.1 million (150 percent of quota). The arrangement covers Malawi's fiscal years 2012/13 through 2014/15. This letter and the attached Memorandum of Economic and Financial Policies (MEFP) report on recent economic developments, performance under our ECF-supported program, and policies for the rest of FY2012/13 and over the medium term.

The overarching goal of our program remains to reduce poverty in Malawi through sustainable growth and wealth creation. In this connection, the program focuses on achieving and maintaining macroeconomic stability, boosting real GDP growth, and scaling up social-protection programs to mitigate the adverse impact of adjustment measures on the poor. Structural reforms under the program emphasize enhancing domestic revenue mobilization, further improving public financial management, ensuring the operational independence of the Reserve Bank of Malawi (RBM), deepening the financial sector, and improving the investment climate.

The external environment has been more difficult than envisaged at the inception of the program. Lower-than-expected tobacco and sugar proceeds and higher foreign exchange requirements to clear the backlog of private sector external payments arrears put substantial pressure on the exchange rate. Also, the price of maize—the main staple food in the country—has increased considerably in the last few months, as drought conditions in parts of the country impacted negatively on output. It is estimated that nearly 2 million people (about 12 percent of the total population) face food deficits and need assistance in the period before the next harvest (March/April 2013).

Notwithstanding the challenges we faced, most of the quantitative targets for September were met, including those on net international reserves, government's net domestic borrowing, and the contracting of non concessional external borrowing. However, the performance criterion on the level of the RBM's net domestic assets was missed on account of the extension of liquidity support to the banking system in order to avert a payments system crisis. The indicative target on social spending was also not achieved due to delays in the procurement of fertilizers for the farm input subsidy program. All the structural benchmarks scheduled for implementation by end-September were met, and we are on course to meet all those due to be implemented by end-December.

We request a waiver for the nonobservance of the end-September 2012 NDA target, based on corrective measures that we are implementing (MEFP paragraphs 17 and 24). The level of liquidity support to the banks has fallen substantially and the RBM is exercising increased oversight of a few banks that continue to have difficulty meeting prudential liquidity requirements. On the basis of our overall performance, and on the strength of policies set forth in the attached MEFP, we request that the Executive Board of the IMF complete the first review under the ECF arrangement and release the second tranche of SDR 13.02 million (18.75 percent of quota). We also request the modification of the performance criteria for end-December 2012 and end-March 2013, to reflect the updated macroeconomic framework presented in the MEFP, and the establishment of performance criteria for end-September 2013.

We believe that the policies set forth in the MEFP 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 IMF staff on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP, in accordance with the IMF policies on such consultation. Moreover, we will provide the IMF with such information as the IMF requests in connection with the progress in implementing the policies and reaching the objectives of the program.

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

Yours sincerely,

/s/	/s/
Dr. Ken Lipenga (MP) 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. MALAWI: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICES, 2012/13–2014/15

I. INTRODUCTION

1. This memorandum supplements the Memorandum of Economic and Financial Policies (MEFP) attached to our Letter of Intent dated July 9, 2012. It describes recent developments and performance under the ECF arrangement through September 2012, summarizes the Government's recently launched Economic Recovery Plan, and elaborates on policies and structural reforms for the rest of FY2012-13 and the medium term.

2. The main objectives of the program remain macroeconomic stability, sustained high and inclusive growth, and delivery of social-protection programs to mitigate the adverse impact of adjustment measures on the poor. Structural reforms under the program emphasize enhancing domestic revenue mobilization, strengthening public financial management, ensuring the operational independence of the Reserve Bank of Malawi (RBM), deepening the financial sector, and improving the investment climate.

3. The government has implemented strong adjustment measures. Shortly after her elevation to the presidency in April 2012, President Joyce Banda authorized the implementation of a set of bold measures to address long-standing internal and external imbalances in the economy. The key measures entailed: (i) a devaluation that increased the price of foreign exchange by about 50 percent and adoption of a floating exchange rate regime; (ii) removal of restrictions on foreign exchange transactions by banks and foreign exchange bureaus; (iii) relaxation of surrender requirements on export proceeds, allowing them to flow to commercial banks instead of mainly to the RBM; and (iv) increases in the retail prices of petroleum products and adoption of an automatic adjustment mechanism to keep prices in line with import costs. Concurrently, the RBM tightened monetary policy by raising its policy rate and through sales of foreign exchange.

4. The reforms elicited positive responses initially. Increased availability of foreign exchange from private sources eased the shortage of key items such as fuel, and the parallel market for foreign exchange virtually disappeared. Malawi's development partners pledged increased financial assistance, especially in the form of budget support.

5. The external environment has become more difficult than envisaged at the inception of the program. Lower-than-expected tobacco and sugar proceeds and higher foreign exchange requirements to clear the backlog of private sector external payments arrears put substantial pressure on the exchange rate. Continued depreciation of the exchange rate and drought-induced increases in local food prices pushed inflation above its envisaged path. It is estimated that nearly 2 million people (about 12 percent of the total population) are at risk of famine in the period before the next harvest in March/April 2013.

6. The government has recently launched the Malawi Economic Recovery Plan (ERP) which seeks to sharpen priorities within the extensive set of programs and projects in the second Malawi Growth and Development Strategy (MGDS II). The ERP lays out action plans over the short- and medium-term to make rapid progress toward poverty reduction through economic growth and wealth creation. It identifies commercial agriculture, tourism, energy, mining, transport infrastructure, and information and communication technology as key sectors and activities that can lead growth and achieve quick development results.

7. The government is committed to achieving the Millennium Development Goals (MDGs) through the implementation of MGDS II which has been aligned with MDG outcomes. Four MDGs are likely to be met by 2015: (i) reduce child mortality; (ii) combat HIV and AIDS, malaria and other diseases; (iii) ensure environmental sustainability; and (iv) develop global partnership for development. The remaining four are unlikely to be met: (a) eradicate extreme poverty and hunger; (b) achieve universal primary education; (c) promote gender equality and empower women; and (d) improve maternal health. The recently published Integrated Household Survey (conducted in 2010/11) indicates that rapid growth during 2005–10 did not have an appreciable impact on rural poverty. The government will strengthen its efforts to promote more inclusive growth.

II. Recent Economic Developments

8. Real GDP growth is now projected to fall from 4.3 percent in 2011 to 1.9 percent in 2012. The downward revision for 2012 (from 4.3 percent in the original program) is driven by contractions in the agriculture and manufacturing sectors. Maize production in 2012 is estimated at 3.6 million metric tons, a 7 percent drop from the level in 2011 but still higher than the estimated national requirement of 2.8 million metric tons. The decline is attributable to poor and erratic rainfall in the southern half of the country during the 2011/12 growing season. Tobacco production is estimated to have fallen from 237,000 metric tons in 2011 to only about 80,000 metric tons in 2012, reflecting low prices offered on the auction floors in 2011 and an overvalued exchange rate which served as a disincentive to tobacco growing last year. The manufacturing sector contracted by about 6 percent in 2012, largely due to scarcity of foreign exchange and fuel in the first half of the year. During the second half of the year, the pace of recovery has been slow due to both supply and demand side factors. Although the private sector has cleared most of its external payments arrears, external lines of credit have not yet been re-established as banks and suppliers have adopted a wait-and-see attitude, on concerns of possible policy reversals. On the demand side, there has been reduced uptake of products due to significantly lower disposable incomes associated with the depreciation of the exchange rate and rising inflation.

9. Inflation has accelerated in the aftermath of the devaluation and contraction in domestic food production. On a year-on-year basis, headline consumer inflation increased from 12.4 percent in April to 28.3 percent in September, with both the food and non-food

components of the CPI rising sharply. The non-food CPI has a large import content and as a result, its evolution is influenced strongly by exchange rate movements. In mid-November, the price of foreign exchange had increased by an additional 30 percent since the May devaluation. Factors that have contributed to this marked depreciation of the exchange rate include: the clearance of private sector external payments arrears (estimated at about US$500 million), perceptions in the market of continued scarcity of foreign exchange based on the low level of official international reserves, and weak performance of foreign currency-generating products (tobacco and sugar).

10. Year on year growth in reserve money fluctuated between 38 percent and 72 percent in the first half of 2012, driven by credit to government. After peaking at 80 percent in July the growth rate decelerated sharply to 20 percent in September. Since July, RBM lending to banks has been the principal source of growth in reserve money. Broad money growth remained steady in the range of 31–34 percent a year between January and July 2012 before falling to 20 percent in September. Credit to the government and to the private sector were the principal sources of growth in broad money in the first half of the year. Subsequently, the government reduced its net borrowing, and lending to the private sector has become the principal source of broad money growth.

11. The RBM increased the bank rate from 13 percent to 16 percent in April and to 21 percent in July. Banks responded by increasing both their deposit and lending rates, with prime lending rates increasing from about 18 percent to about 30 percent and the rate on 3-month fixed deposits rising from the 2–6 percent range to about 16 percent. There has also been increased activity on the inter-bank market, reflecting improved liquidity in a number of banks that have become providers of liquidity to some banks.

12. Fiscal performance in FY2011/12 was weaker than envisaged in the last MEFP. The overall deficit was 1.5 percent of GDP larger than projected, driven by lower grants and higher expenditures. Domestic interest payments and development expenditures accounted for the higher level of expenditures. The larger deficit was financed mainly by domestic borrowing. In the first quarter of FY2012/13, fiscal performance was in line with the program.

13. Low production of Malawi's main export, tobacco, translated into significantly lower sales volumes on the auction floors in 2012 compared to 2011. The volume of sales fell to one third of the level in 2011 and only half of what was projected at the beginning of the season. The value of sales fell by 40 percent (from US$294 million to US$178 million), reflecting higher unit prices paid to farmers. Thus, the supply of foreign exchange to the local foreign exchange market declined sharply. Exports of tobacco, however, remained comparable to the level achieved in 2011 due to large stocks of inventories. Sugar exports also declined as a result of drought in central and southern parts of the country. The import bill increased in 2012 due to higher international fuel prices, as well as increased volumes of

fertilizer imports in response to positive price incentives for tobacco production (reflecting the change in exchange rate policy). The import coverage of international reserves has improved slightly from exceptionally low levels in the first half of 2012 due to increased donor assistance to Malawi.

III. Performance Under the Program

14. Most of the quantitative targets for end-September 2012 were met (Table A1). In particular, the target on government net domestic borrowing was met comfortably. The targets on net international reserves and on external borrowing were also met. The performance criterion on the level of the RBM's net domestic assets and the indicative target on reserve money were missed on account of the extension of liquidity support to the banking system in order to avert a payments system crisis. With respect to the indicative target on priority spending, the government fell short by about MK11 billion, emanating largely from delays in awarding contracts for the procurement of fertilizers for the Farm Input Subsidy Program (FISP). The government made changes to the procurement process with the aim of ensuring increased value for money. The rolling out of other social protection programs (e.g., public works and cash transfer programs) started in the second quarter of FY 2012/13 (October–December) and as a result, we expect increased social spending in this quarter to make up for the shortfall in the first quarter. External grants were broadly in line with programmed levels for the first quarter.

15. All the structural benchmarks scheduled for implementation by end-September were met (Table A2). The Malawi Revenue Authority (MRA) began publishing its monthly revenue collections in newspapers in July, and the RBM posted the financial stability report for March 2012 on its website in August. The Ministry of Finance established quarterly spending ceilings for the first and second quarters. We are on course to meet all the structural benchmarks scheduled for implementation by end-December 2012.

16. Among the set of bold measures implemented by the new administration was a substantial increase in fuel prices to bring them in line with the actual import cost and the restoration of an automatic pricing mechanism to ensure pass through of world prices of fuel. In line with this decision the pump price has been adjusted since July 2012. While there was some delays in adjustment of the pump price in October, the recent adjustment in pump price in November reflected world fuel price developments since the last domestic pump price adjustment.

17. The banking system experienced tight liquidity conditions soon after the May devaluation. Initially, almost all banks resorted to the RBM discount window to meet their liquidity needs. In part, the tight liquidity situation reflected RBM withdrawal of liquidity from the system through foreign exchange sales to the market (a monthly average of US$55 million during May-July). As signs of the liquidity squeeze intensified—e.g., as

evidenced by banks having difficulty settling interbank transactions—the RBM provided liquidity to the banks, including through uncollateralized lending at a premium over the bank rate, in order to avert a crisis. The increased lending to banks was the principal factor behind the non-observance of the end-September NDA performance criterion. In order to bring down NDA, the RBM closed the uncollateralized lending window on [November 30] and has also undertaken open market operations to withdraw liquidity as part of the effort to stabilize the exchange rate. It has also stepped up its monitoring of the frequency of recourse to its discount window by individual banks.

IV. Medium-term Framework

18. The main changes to the medium-term macroeconomic framework compared to the MEFP that accompanied Malawi's ECF request are:

- Significantly slower growth in 2012, reflecting the estimated contraction in agricultural output and slower-than-expected pace of recovery in other sectors. A strong rebound in growth is envisaged, beginning in 2013, based on the assumption of a return to normal rainfall patterns and improved access to foreign exchange, and taking into account improved price incentives for tobacco production.

- Upward shift in the inflation path for 2012 and the first half of 2013, reflecting recent significant depreciation of the exchange rate and sharp increases in prices of domestically produced food (especially maize). Inflation is projected to decelerate rapidly during the next harvest season (2013 Q2) in response to increased supply of food and the lagged effect of tighter monetary and fiscal policies.

- Little change in external debt and total public debt indicators. In particular, projected external debt service remains low at less than 5 percent of exports for the foreseeable future.

V. Policies

19. The most pressing challenge facing the government and the RBM is stabilization of the exchange rate in order to avoid a depreciation-inflation spiral. Given the current circumstances—low international reserves and the onset of the lean season for foreign exchange inflows—a tightening of both monetary and fiscal policies is called for.

A. Exchange Rate Policy

20. We remain committed to a flexible exchange rate regime to allow the kwacha to adjust to domestic and international developments. The main objective of our exchange rate policy is to contribute to enhancing Malawi's external competitiveness. The RBM determines the official exchange rate at the beginning of each business day as a weighted average of

rates established by commercial banks the previous day. The RBM will continue to make the case for a flexible regime to the public, emphasizing that, given the very low level of international reserves, a return to a fixed exchange rate regime will come with a high risk of a quick return to an overvalued exchange rate and the associated problems of foreign exchange shortages that plagued the country in the last few years. The RBM will intervene in the foreign exchange market mainly to ensure orderly market conditions, and will continue to build up its international reserves in order to provide the economy with a buffer against exogenous shocks.

B. Monetary Policy and Financial Sector Issues

21. The main objective of monetary policy is the achievement of stable low inflation. Other objectives include contributing to a sustainable balance of payments position and to economic growth. The RBM has a liquidity forecasting framework which it uses to guide its monetary operations. The RBM will continue to develop its instruments of indirect monetary control and strengthen its ability to implement monetary policy through changes in interest rates, underpinned by open market operations. The use of treasury bills for monetary operations will be formalized in a Memorandum of Understanding (MOU) between the RBM and the Ministry of Finance by end-December 2012. The MOU will indicate clearly that the Ministry of Finance will be responsible for meeting the interest costs of treasury bills used for monetary operations.

22. In order to contain rising inflation pressures, the RBM has tightened monetary policy by winding down its uncollateralized lending to banks and will stand ready to implement further measures using all instruments available to it to stabilize the exchange rate and contain second round effects of increased fuel prices and utility tariffs. The RBM intends to pursue a more proactive communications strategy toward financial markets and the general public to aid stakeholders better understand its monetary policy actions.

23. Before the devaluation, the banking system was flush with liquidity, a significant portion of which reflected the lack of foreign exchange to meet customers' foreign payments obligations. As part of a financial inclusion drive, some banks embarked on expansion drives to reach a wider customer base. A number of banks used the available liquidity to extend long-term loans and were unable to unwind their long positions quickly when foreign exchange availability improved after the devaluation and customers sought to pay down their external arrears. In order to provide relief to the hardest hit banks and to avoid failure of the payment system and associated adverse impacts on the economy, the RBM introduced a window for providing short term uncollateralized loans to banks that had run out of securities for borrowing through the regular discount window at rates that were initially significantly higher than the policy rate. Safeguarding the payment system and sustaining financial inclusion was the main rationale for RBM support to a couple of banks which have more branches and agencies than the other banks. Most banks have adjusted their balance sheets to the new conditions, though a few continue to have difficulties.

24. Banks have initiated a number of actions to address the liquidity problems they faced after the devaluation. These include deposit mobilization campaigns, curtailment or outright freezing of new loans, recalling overdue loans, securitization of loans, sale of securities, injection of fresh capital, and suspension of expansion drives. The RBM is conducting in-depth assessments of banks that have continued for a long time to rely heavily on borrowing from the RBM or the interbank market to meet liquid reserve requirements. The RBM will enforce its prudential regulations, and if warranted, require the banks to submit time-bound restructuring plans. Restructuring is likely to include securitization of some assets, curtailing the levels of lending and putting on hold expansion plans.

25. Notwithstanding the challenges being faced by some banks, financial stability indicators suggest that the banking sector in Malawi remains sound. Non-performing loans are at low levels—their share as a ratio of total loans was 6.4 percent as at end-September 2012. However, the deterioration in the macroeconomic environment in the last two years and the slow pace of recovery have elevated the risks to banks' portfolios. The RBM has intensified its monitoring and surveillance of the financial system with a view to detecting at an early stage emerging threats to financial stability.

26. The RBM is undertaking a review of the RBM Act with a view to recommending amendments to modernize it. In order to enhance the operational independence of RBM, the government agrees to include an amendment to limit the outstanding amount of the government's total borrowing of all kinds from the RBM. Currently, the RBM Act limits the amount of advances to the government but has no limits on other forms of RBM lending to the government (e.g., through holdings of treasury bills). In line with the recommendations of the recent Safeguards Assessment, the review of the Act will also cover amendments to strengthen RBM's governance structure and its legal and financial autonomy. Proposed amendments will be ready for discussion with government in December 2012, and for submission to parliament by the government by June 2013.

C. Fiscal Policy

27. The difficult macroeconomic environment characterized by high inflation and continuing depreciation of the exchange rate has put the FY2012/13 budget under stress. In order to meet the increased need for resources to deliver reasonable levels of public services, the government has appealed to development partners to provide additional assistance over and above pledges reflected in the FY2012/13 budget. We now expect to receive about US$662 million in external grants this fiscal year (including US$234 million in budget support), compared to an estimate of US$598 million (of which US$208 in budget support) in the original budget. The additional resources will allow the government to increase expenditure in several critical areas, including social spending and goods and services to maintain basic functions of the government.

28. The government is acutely aware that sole reliance on monetary policy to stabilize the exchange rate and contain inflation may further slow down the recovery in the economy. Thus, fiscal policy needs to contribute to the effort, especially since loose fiscal policies in the last few years have left a legacy of huge domestic arrears that are a major factor in the liquidity problems of some banks. To that end, the government will aim to save some of the additional resources that have become available in order to support the objective of boosting international reserves from the current very low levels. The FY2012/13 budget will be revised to reflect a net buildup in government deposits (or "net repayment" to the banking system) equivalent to about ½ percent of GDP.

29. Revisions to the revenue outlook reflect expectations that corporate income tax collection is likely to fall short of budget estimate (because of slower-than-expected recovery in manufacturing and likely losses by banks), but increased collections from PAYE and VAT are expected to more than make up for the shortfall. On the expenditure side, the largest revisions were increases in the allocations to fertilizer purchases for FISP and goods and services, on account of the impact of the more depreciated exchange rate.

30. On behalf of the government, the World Food Program launched an appeal for US$60 million to undertake emergency operations to deliver food to nearly 2 million people who are food insecure because of drought in some parts of the country. At mid-November, about US$47.2 million had been raised, including government's contribution of approximately 72,500 MT of maize valued at about US$16.4 million.

31. The government will continue its efforts to strengthen revenue administration and broaden the tax base. The government will enhance its enforcement mechanisms through increased audits and use of modern information and communication technology (ICT) systems to improve revenue collection. Tax revenues are expected to improve through the adoption and use of electronic fiscal devices in the enforcement of VAT and the use of computerized cargo scanners coupled with the implementation of web-based ASYCUDA System for Customs. At the request of the Malawi Revenue Authority (MRA), an IMF technical assistance mission recently visited Malawi to provide advice on a number of issues, including: (i) automating and managing taxpayer compliance to support a full self-assessment system; and (ii) developing and implementing best practice performance indicators for tax and customs administration.

32. In order to strengthen the commitment control and avoid the accumulation of arrears, the Commitment Module in IFMIS is now being piloted having passed Acceptance Testing and should be rolled out soon. In readiness for the roll-out, user training of relevant officers has already been done and a Press Statement to the general public on the procurement rules will be released. Under the Multi-Donor Funded Financial Reporting and Oversight Improvement Project (FROIP), we are also reviewing IFMIS accounting business processes and functional requirements through consultations. These processes should result in better utilization of IFMIS through improvement in financial procedures, as the system will be

reconfigured to allow financial transactions to be processed with very little manual intervention. Information sharing has improved. For instance, daily sharing on total amounts of cheques issued with RBM's Liquidity Management Committee Secretariat is being done. With respect to cash management, data that we have started gathering will improve the forecasting of deficit financing and inform short-term borrowing requirements, allowing us to move away from automatic resort to Ways and Means Advances.

33. The government has initiated steps to reduce the risks to the budget posed by contingent liabilities and operational losses of state-owned enterprises. The contingent liabilities are mainly loans from banks and payment arrears while the operational losses arise from administratively set prices and tariffs that are below cost-recovery levels and generate substantial implicit and explicit subsidies. The government recognizes that the operations of the recently established National Oil Company of Malawi (NOCMA), including government-guaranteed loans for fuel imports, pose severe risks to the budget. For state-owned enterprises, risks are now being mitigated through the approval of realistic tariffs, and NOCMA's operations will be restricted to the management of strategic fuel reserves. The bulk of fuel importation for regular use will remain with the private sector.

34. Most of the MK72 billion stock of arrears indicated in the June MEFP have been verified and certified by National Audit Office. These arrears were accumulated over the last three years by government ministries and departments and parastatals (on behalf of government) to suppliers of goods and services and contractors undertaking construction projects. Several of the suppliers and contractors took out loans from banks which they have not been able to service because of nonpayment by the government. In order to assist the suppliers and contractors, as well as the banks, the government has issued them promissory notes worth MK [38] billion. The promissory notes will be redeemed over a period of four years starting from FY 2013/14.The reference rate for the notes is the 91 day treasury bill of the most recent auction immediately preceding interest payment. This transaction is being incorporated into the medium term fiscal framework.

D. Business Climate and International Competitiveness

35. Although the recent liberalization of the exchange rate regime has addressed the issue of overvaluation of the kwacha—a key step towards enhancing Malawi's international competitiveness—the government recognizes that further steps are required, especially removal of structural bottlenecks—e.g., reliable and adequate supply of energy—that are holding back growth and diversification of the economy.

36. Malawi ranks low globally and behind its neighbours in indicators of the business environment. For example, it ranks 129th out of 144 countries in the 2012/13 Global Competitiveness Indices (GCI) of the World Economic Forum, and 155th out of 183 countries in the World Bank's 2013 Doing Business Report. Major challenges in doing business in Malawi cited by the private sector include: (i) lack of access to finance;

(ii) inadequate infrastructure; (iii) inefficient government bureaucracy; (iv) policy instability; (v) uncompetitive tax incentives and tax regime; and (vi) inadequate educated and skilled work force. The government is determined to address these competitiveness issues by removing regulatory hurdles in the areas of starting a business, obtaining permits, registering property, enforcing contracts and trading across borders. The Ministry of Industry and Trade has embarked on a program to create a pro-business environment in consultation with stakeholders in the private sector, civil society, and public sector.

37. The government has developed a National Export Strategy (NES) through a participatory process involving a broad range of stakeholders. The NES, which is expected to be launched in [date], supports the second Malawi Growth and Development Strategy (MGDS II) and the Economic Recovery Plan (ERP) by presenting a strategy to develop Malawi's capacity to export. The NES is a prioritised road map for developing Malawi's productive base to allow for both export competitiveness and economic empowerment. This strategy focuses on four main areas: (i) export-oriented clusters for diversification; (ii) conducive environment; (iii) supportive economic institutions to build the productive base of the economy; and (iv) competencies, skills and knowledge development. These components will be implemented through the NES' implementation mechanism, which is based on the Trade, Industry and Private Sector Development Sector Wide Approach. This SWAp will be largely funded by donors and contain seven technical working groups whose mandate will be to ensure the implementation.

VI. Information Sharing, Data Quality and Capacity Building

38. In order to enhance economic policy making, we will strengthen processes and practices to achieve timely information sharing in the following areas: (i) delays in reconciliation of fiscal and monetary accounts involving the Malawi Revenue Authority, MOF and RBM, which have recently produced large statistical discrepancies between above-the-line fiscal data and below-the-line financing data from the RBM; and (ii) inadequate provision of information on government operations to feed into the RBM's liquidity forecasting framework that guides monetary operations.

39. The government is grateful for the assistance it has received from the IMF and other partners to build capacity for the compilation and dissemination of economic statistics. We continue to need assistance to improve the quality of a wide range of statistics, including national accounts, prices, and the balance of payments. We are also in need of assistance to build capacity for the production of high frequency indicators of economic activity to guide timely policy making.

VII. Program Monitoring

40. Program implementation will be monitored with quantitative financial targets and structural benchmarks (Tables A1 and A2). Modifications to the quantitative targets for December 2012, March 2013 and June 2013 are proposed to reflect the updated

macroeconomic framework. The second review is scheduled to be completed by mid-March 2013 based on the end-December 2012 test date, the third review by mid-June 2013 based on the end-March 2013 test date, and the fourth review by mid-December 2013 based on the end-September test date. Definitions of key concepts and indicators, as well as reporting requirements, are set out in the accompanying Technical Memorandum of Understanding.

ATTACHMENT II. TECHNICAL MEMORANDUM OF UNDERSTANDING (TMU)

I. INTRODUCTION

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.

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

II. QUANTITATIVE PERFORMANCE CRITERIA: DEFINITIONS AND DATA SOURCES

A. Floor on Net International Reserves of the RBM

3. **Definition of net international reserves (NIR) of the RBM:** The NIR of the RBM is defined as gross reserves minus IMF and other short-term liabilities. The values of all foreign assets and liabilities will be converted into U.S. dollars at each test date using the program cross exchange rates for the various currencies and then converted into kwacha using the program exchange rate for the U.S. dollar–kwacha exchange rate. The program exchange rate of the Malawi Kwacha to the U.S. dollar is set at MK320 = US$1. The corresponding cross exchange rates and program gold price for the duration of the program are in Table 3.

4. **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).

5. **This concept includes the following:** (1) monetary gold holdings of the RBM; (2) holdings of SDRs; (3) the reserve position in the IMF; (4) foreign convertible currency holdings; (5) deposits held in foreign central banks, the Bank for International Settlements, and other banks; (6) loans to foreign banks redeemable upon demand; (7) foreign securities; and (8) other unpledged convertible liquid claims on nonresidents. It excludes the following: (1) any foreign currency claims on residents; (2) capital subscriptions in international institutions; (3) foreign assets in nonconvertible currencies; (4) 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; (5) gross reserves that are in any way encumbered or pledged, including, but not limited to: (i) assets blocked when used as collateral for third party loans and third-party payments, pledged to investors as a condition for investing in domestic securities, (ii) assets lent by RBM to third parties that are not available before maturity, and are not marketable; and foreign reserves blocked for letters of credit.

6. **Gross reserve liabilities of the RBM** are defined as the sum of the following: (1) SDR allocations; (2) outstanding medium and short-term liabilities of the RBM to the IMF; and (3) all short-term foreign currency liabilities of the RBM to nonresidents with an original maturity of up to, and including, one year.

7. **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 and loan financing from the IMF, and donor inflows (in kwacha) 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.

8. **Adjustment clause on NIR—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$30 million above the program baseline (See Table 1). The floor on NIR of the RBM will be adjusted downward by the full amount up to a maximum of US$ 10 million by which the cumulative receipts from the budget support are less than the program baseline. Budget support is measured as the cumulative flow from the beginning of the fiscal year.

9. Adjustment clause on NIR—donor accounts for the social sector (including health, education, and other 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 (in kwacha) from the U.S. dollar–denominated donor accounts for SWAps and NAC held in the RBM are smaller than the donor inflow (in kwacha) to those accounts in the program baseline. The downward adjustment will be capped at US$ 30 million. Donor inflows are measured as the receipts (in kwacha) by the budget from the beginning of the fiscal year.

10. **Adjustment clause on NIR—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 (ADB) fall short of (exceed) the program baseline. The cumulative amount will be measured from the beginning of the fiscal year.

11. The total downward adjustment to NIR from a shortfall of (i) budget support and (ii) donor 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 (ADB) relative to the program assumptions will be capped at US$40 million. 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$30 million above the program baseline and by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of the program baseline.

12. For this target and those for external debt and arrears, valuation will be in U.S. dollars, using the above defined program exchange rates.

13. Data on NIR, including its components, will be reported by the RBM on a weekly and end-month basis.

B. Ceiling on the Net Domestic Assets of the Reserve Bank of Malawi and Reserve Money

14. **Definition of net domestic assets (NDA) of the RBM:** NDA of the RBM are defined in kwacha terms as end-quarter reserve money less NFA of the RBM at the program exchange rate. Reserve money consists of currency issued by the RBM and balances of commercial banks' accounts with the RBM. It includes required reserves held for Malawi kwacha deposits and any other domestic currency reservable liabilities and other demand and time deposits held with the RBM. The NDA program ceilings are the indicative money targets defined below less the NFA of the RBM.

15. **Definition of NFA of the RBM:** The NFA of the RBM are defined as the above-defined NIR plus other foreign assets of the RBM—including but not limited to: (1) capital subscriptions in international institutions; (2) foreign assets in nonconvertible currencies; and (3) gross reserves that are in any way encumbered or pledged, less any medium- and long-term foreign liabilities of the RBM.

16. **Adjustment clause on NDA—budget support:** The ceiling on NDA of the RBM will be adjusted downward by the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline. The ceiling on NDA of the RBM will be adjusted upward by the amount by which the cumulative flow of receipts from budget support are less than the program baseline, up to a maximum of US$10 million. The kwacha value of the cumulative shortfall (excess) will be calculated at the program exchange rate. Budget support is measured as the cumulative flow from the beginning of the fiscal year.

17. **Adjustment clause on NDA—donor pool accounts for the social sector (including health, education, and other SWAps, and NAC):** The ceiling on NDA of the

RBM will be adjusted upward by the amount by which the donor inflows (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 (in kwacha) to those accounts in the program baseline. The upward adjustment will be capped at US$30 million. Donor inflows are measured as the receipts received (in kwacha) by the budget. Donor inflows are measured from the beginning of the fiscal year.

18. **Adjustment clause on NDA—debt service payments:** 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 (Table 1). The cumulative amount will be measured from the beginning of the fiscal year.

19. The total upward adjustment to NDA from a shortfall of (i) budget support (ii) donor 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 (ADB) relative to the program assumptions will be capped at US$40 million. The downward adjustment to NDA will reflect the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline and by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of the program baseline.

20. **Adjustment clause on NDA—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 percentage 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).

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

21. **Definition of CGDB:** CGDB is computed as the sum of (1) net borrowing from the RBM (including ways and means advances, loans, holdings of local registered stocks, government bonds, and holdings of treasury bills minus deposits); (2) net borrowing from commercial banks (including advances, holdings of local registered stocks, and holdings of treasury bills minus deposits); (3) net borrowing from nonbanks (including, but not limited to, holdings of local registered stocks and holdings of treasury bills); and (4) holdings of promissory notes. The treasury bills and locally registered stocks are valued at cost rather than face value. The ceiling is measured as the change in the stock of CGDB since June 30, 2012, 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. They will be treated the same as borrowing from the private sector (as their accounts are outside the definition of government) and therefore as domestic borrowing. Asset sales or privatization revenues will be accounted for under financing as a separate category, separate from domestic or foreign financing in calculating CGDB.

22. **Definition of domestic arrears:** Domestic arrears are overdue payment obligations of the central government other than external payment arrears, including on wages and salaries, pensions, transfers, domestic interest, goods and services, obligations arising from court cases, legally established compensation claims, 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.

23. **Adjustment clause on CGDB—budget support:** The ceiling of CGDB will be adjusted downward (upward) by the full amount by which cumulative kwacha receipts from budget support are greater (less than) the program baseline. The upward adjustment will be capped at US$10 million. In the event of excess budget support, the ceiling on CGDB will be adjusted by the full amount less US$30 million. The kwacha value of the cumulative shortfall (excess) will be calculated at the program exchange rate. Budget support is measured as the cumulative flow from the beginning of the fiscal year.

24. **Adjustment clause on CGDB—donor accounts for the social sector (including health, education, and other SWAps, and NAC):** The ceiling on CGDB will be adjusted upward by the full amount by which the donor inflows (in kwacha) from the U.S. dollar–denominated donor accounts for health, education, and other SWAps, and NAC held in RBM are smaller than the donor inflows (in kwacha) to those accounts in the program baseline. The upward adjustment will be capped at US$30 million. Donor inflows are measured as receipts received (in kwacha) by the budget. Donor inflows are measured from the beginning of the fiscal year.

25. **Adjustment clause on CGDB—debt service payments:** 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. The cumulative amount will be measured from the beginning of the fiscal year.

26. **The total upward adjustment to CGDB** from a shortfall of (i) budget support (ii) donor 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 (ADB) relative to the program assumptions will be capped at US$40 million. The downward adjustment to NDA will reflect the full amount by which the cumulative receipts from the budget support are greater than US$30 million above the program baseline and by the full cumulative amount by which debt service payments to the World Bank and the African Development Bank (ADB) fall short of the program baseline.

D. Ceiling on External Payment Arrears

27. **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.

E. Ceiling on Nonconcessional External Debt

28. Definition **of nonconcessional external debt:** The definition of debt, for the purpose of the limit, 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; 12**274–(00/85) August 24, 2000; and 14416-(09/91), August 31, 2009. For program purposes, short-, medium-, and long-term debt is nonconcessional if it includes a grant element of less than 35 percent, as indicated in Decision No. 11248-(96/38), April 15, 1996. The ceiling on nonconcessional 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. 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.

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

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

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

III. Quantitative Indicative Targets and Structural Benchmarks

32. **Definition of reserve money:** Reserve money is defined as the sum of currency issued by the RBM, including the vault cash of commercial banks, and balances of commercial bank accounts with the RBM. It includes required reserves held for kwacha deposits, other domestic currency liabilities, and other demand and time deposits held with the RBM. The reserve money targets are the projected end-quarter values starting with end-September r 2012 to end-December 2013.

33. **Definition of social spending:** Using functional classification of expenditure, social spending is computed as the sum of central government spending on health, education, the farm input subsidy program, and government social protection (comprising the government expenditures by the ministry of gender, children and social welfare, the ministry of disability and elderly affairs, and the local development fund) . 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 be adjusted downward to meet fiscal targets of the program (Table 4).

IV. Reporting of Certain Transactions in the Fiscal Accounts

34. **Donor pool–funded expenditures in support of the SWAps:** The Government of Malawi has embarked on an integrated program of service delivery in the health and education sectors (the so-called SWAps). In support of the health and education SWAps, some donors pool resources (the donor pool), and release these resources through normal government procedures (i.e., recurrent budget or development Part II budget) to the relevant sector. Financial flows into and out of this account will be reported on a monthly basis from the beginning of the fiscal year.

35. **Farm input subsidy program:** The government has embarked on a program of subsidizing agricultural inputs, in particular, fertilizer, to smallholder farmers to improve agricultural production, financed by the budget. The spending on the farm input subsidy program will be reported quarterly from the beginning of the fiscal year.

V. Exchange Regime

36. **Avoiding multiple currency practices and exchange restrictions:** The RBM will ensure on-going assessment of the foreign exchange regime with support from IMF to ensure the consistency of the regime with Malawi's obligations under Article VIII. The RBM will continue to work towards ensuring that the spread between the official exchange rate and other market determined rates (bureau and parallel market rates) fall within 2 percent. The RBM will abide by the continuous PC on non-introduction or intensification of exchange restrictions and multiple currency practices.

VI. REPORTING REQUIREMENTS

37. Monitoring of the program requires that the information listed in Table 5 below be reported to the IMF within the timeframe indicated.

Table 1a. Malawi: Quantitative Targets (September 2012)[1]

	Criteria [2]	End-Mar 2012 Stock Act.	End-June. 2012 Stock Proj.	End-June. 2012 Stock Act.	Sept. 2012 Prog.	Sept. 2012 Act.	Status
I. Monetary targets (millions of kwacha)							
1. Ceiling on net domestic assets of the RBM [3,4, 5, 6]	PC	116,861	114,579	142,513	109,417	117,737	NM
2. Ceiling on reserve money[3]	IT	89,168	76,178	101,398	88,210	95,657	NM
II. Fiscal targets (millions of kwacha)							
3. Ceiling on central government's net domestic borrowing [5,6,7]	PC	176,588	178,847	188,853	-11,988	-41,220	M
4. Floor on social spending [8]	IT				39,034	27,959	NM
III. External sector targets (US$ millions, unless otherwise indicated)							
5. Floor on net international reserves of the RBM[3, 5, 6,9]	PC	-20	-63	-74	17	17	M
6. Ceiling on the accumulation of external payments arrears [7,10]	PC				0	0	M
8. Ceiling on new nonconcessional external debt maturing in more than one year [7,10]	PC				0	0	M
9. Ceiling on new nonconcessional external debt maturing in one year or less [7,10]	PC				0	0	M
10. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [10,11]	PC						M
Memorandum items:							
Net foreign assets of the RBM (US$ millions)		-107	-148	-158	-82	-85	
Budget support (US$ millions)					86	89	
Budget support (millions of kwacha)					21,945	23,210	
Debt service payments to the World Bank and African Development Bank (millions of kwacha)							
Health SWAp receipts (millions of kwacha)					5,248	7,732	
Education SWAp receipts (millions of kwacha)					8,378	7,227	
NAC receipts (millions of kwacha)					4,777	1,538	
Program exchange rate (kwacha per US$)		260	260	260	260	260	

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.
8 Priority social spending as defined in the TMU and quantified in the authorities' budget.
9 Adjusted for Letters of credit with cash cover as at end-March and end-June.
10 Evaluated on a continuous basis.
11 Other standard PCs include introducing or modfying MCPs, concluding bilateral payments agreements that are inconsistent with Article VIII, and imposing or intensifying import restrictions for balance of payment reasons.

Table 1b. Malawi: Quantitative Targets (December 2012–September 2013)[1]

	Criteria [2]	End-Sept. 2012 Act.	End-Dec. 2012 Prog.	End-Dec. 2012 Rev. Prog.	End-Mar. 2013 Prog.	End-Mar. 2013 Rev. Prog.	Indicative End-Jun. 2013 Prog.	Indicative End-Jun. 2013 Rev. Prog.	End-Sept. 2013 Prog.
I. Monetary targets (millions of kwacha)									
1. Ceiling on net domestic assets of the RBM [3,4, 5, 6]	PC	117,737	118,542	118,293	106,256	132,082	100,930	114,444	94,132
2. Ceiling on reserve money [3]	IT	95,657	97,809	96,615	99,120	99,095	105,830	107,845	111,830
II. Fiscal targets (millions of kwacha)									
3. Ceiling on central government's net domestic borrowing [5,6,7]	PC	-41,220	18,500	-17,756	11,609	4,444	0	-15,021	-5,218
4. Floor on social spending [8]	IT	27,959	94,044	95,156	121,798	144,922	151,899	185,511	
III. External sector targets (US$ millions, unless otherwise indicated)									
5. Floor on net international reserves of the RBM [3, 5, 6]	PC	17	19	32	71	-3	118	79	155
6. Ceiling on the accumulation of external payments arrears [7,9]	PC	0	0	0	0	0	0	0	0
8. Ceiling on new nonconcessional external debt maturing in more than one year [7,9]	PC	0	0	0	0	0	0	0	0
9. Ceiling on new nonconcessional external debt maturing in one year or less [7,9]	PC	0	0	0	0	0	0	0	0
10. Prohibition on the imposition or intensification of restrictions on the making of payments and transfers for current transactions [9,10]	PC								
Memorandum items:									
Net foreign assets of the RBM (US$ millions)		-85	-80	-68	-27	-103	19	-21	55
Budget support (US$ millions)		89	86	170	151	176	208	234	49
Budget support (millions of kwacha)		23,210	21,945	49,038	38,926	54,934	53,864	73,542	15,752
Debt service payments to the World Bank and the African Development Bank (US$ millions)		0		2		1		3	7
Debt service payments to the World Bank and African Development Bank (millions of kwacha)		0		684		420		827	2,174
Health SWAp receipts (millions of kwacha)		7,732	5,364	7,876	7,771	10,778	7,771	11,173	3,224
Education SWAp receipts (millions of kwacha)		7,227	13,221	9,614	17,073	14,994	19,049	18,194	4,800
NAC receipts (millions of kwacha)		1,538	7,315	5,101	10,019	8,719	12,220	12,281	3,563
Program exchange rate (kwacha per US$)		260	260	320	260	320	260	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.

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

9 Evaluated on a continuous basis.

10 Other standard PCs include introducing or modfying MCPs, concluding bilateral payments agreements that are inconsistent with Article VIII, and imposing or intensifying import restrictions for balance of payment reasons.

Table 2. Malawi: Structural Benchmarks, 2012–13

Measure	Status/Target Date	Macro Rationale	Status
Prior Actions			
Approval of the arrangement			
Parliamentary passage of a budget for FY 2012/13 in line with program objectives		Toward fiscal sustainability	Met
First review			
Shut down RBM's uncollateralized lending to banks			
Structural benchmarks			
Fiscal transparency			
Publish monthly revenue collections of the Malawi Revenue Authority in newspapers within two weeks of the end of the month.	7/31/2012	Build credibility after recent incidents of inflation of revenue data by the Ministry of Finance.	Met
Public financial management			
Provide Ministries, Departments and Agencies with quarterly spending ceilings consistent with quarterly fiscal targets in the program, and enforce ceilings.	Begin in Sept 2012 for FY2012/13 Q2 and quarterly thereafter	Keep spending within available resource envelope.	Met for Q2
Verify existing stock of government domestic arrears and formulate a plan for settling verified claims.	31-Dec-12	Ascertain magnitude of government obligations.	
Configure the IFMIS Purchase Order (PO) module to support commitment control.	31-Dec-12	To restrain creation of arrears.	
Progressively extend processes for capturing donor funded project transactions in IFMIS to all projects where bank accounts are controlled by the government of Malawi.	31-Mar-13	Fuller accounting for impact of aid flows on the budget.	
Monetary Policy			
Amend RBM Act to limit the outstanding amount of RBM's total lending to government.	30-Jun-13	Reduce fiscal dominance to enhance effectiveness of monetary policy.	
Financial sector			
RBM to publish a financial stability report on a semi-annual basis, with a lag of no more than four months. Start with publication of report for quarter ending March 2012.	Semi-annual, starting in July 2012.	Promote financial stability.	Met
Obtain approval and begin implementation of the Financial Sector Development Strategy	31-Dec-12	Financial deepening.	

Table 3. Malawi: Cross Rates for Nominal Exchanges Rate and Gold Price for the 2012–13 Program

	September 30, 2012
Gold bullion LBM[1] US$/troy ounce	1,774.810
SDR to US$ exchange rate	0.648
Euro to US$ exchange rate	0.773
Yen to US$ exchange rate	77.570
Yuan to US$ exchange rate	6.341
Rand to US$ exchange rate	8.305
UK £ to US$ exchange rate	0.618

Source: IFTS, RBM

[1] LBM connotes London Bullion Market.

Table 4. Malawi: Breakdown of Social Expenditures in 2012/13

	2012/13	Q1 Act.	Q2	Q3	Q4
Health Expenditure					
Wages	14,736.67	3,932.97	3,364.00	3,670.00	3,769.70
Other Recurrent					
Ministry of Health ORT	9,606.48	1,988.59	2,510.00	2,550.00	2,557.89
Local Assemblies ORT	9,076.92	2,287.18	2,100.00	1,336.87	3,352.87
Subvented Organisations	100.00	25.00	25.00	25.00	25.00
Development Part II	3,461.00	479.68	993.00	800.00	1,188.32
Total Health	36,981.07	8,713.41	8,992.00	8,381.87	10,893.78
Education Expenditure					
Wages	35,946.48	8,531.71	8,251.71	9,400.00	9,763.07
Other Recurrent					
Ministry of Education ORT	12,537.59	2,657.99	3,100.00	3,400.00	3,379.60
Local Assemblies ORT	5,691.99	1,778.59	1,170.00	1,210.00	1,533.40
Subvented Organisations	19,149.03	4,567.73	4,500.00	5,000.00	5,081.30
Development Part II	5,126.45	1,128.63	1,100.00	1,300.00	1,597.82
Total Education	78,451.55	18,664.65	18,121.71	20,310.00	21,355.19
Farm Input Subsidy Program	54,904.50	100.00	34,742.00	14,742.00	5,320.50
Gender, Children and Social Welfare					
Wages	518.29	129.57	129.57	129.57	129.57
Other Recurrent	169.53	49.17	49.17	30.00	41.19
Development Part II	295.00	62.09	62.09	62.09	108.73
Total Gender, Children and Social Welfare	982.81	240.83	240.83	221.66	279.49
Disability and Elderly Affairs					
Wages	53.40	12.88	12.88	12.88	14.75
Other Recurrent	158.94	82.09	30.00	30.00	16.85
Development Part II	80.75	10.00	30.00	30.00	10.75
Total Disability and Elderly Affairs	293.09	104.97	72.88	72.88	42.35
Local Development Fund	13,783.87	120.00	5,000.00	6,000.00	2,663.87
Poverty and Disaster Management Cost Centre under the Office of the President and Cabinet	113.53	15.22	27.45	37.45	33.42
Total Social Expenditure Projections	**185,510.42**	**27,959.09**	**67,196.87**	**49,765.86**	**40,588.60**
Cumulative Quarterly Targets		**27,959.09**	**95,155.95**	**144,921.82**	**185,510.42**

Source: Malawi authorities.

Table 5: 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
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 statement)	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 financied 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 eight (8) 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, Air Malawi, Electric Supply Company of Malawi. M*alawi Development Corporation,* Malawi Housing Corporation, Malawi Postal Corporation, Malawi Telecommunications Ltd., Northern Regional Water Board.