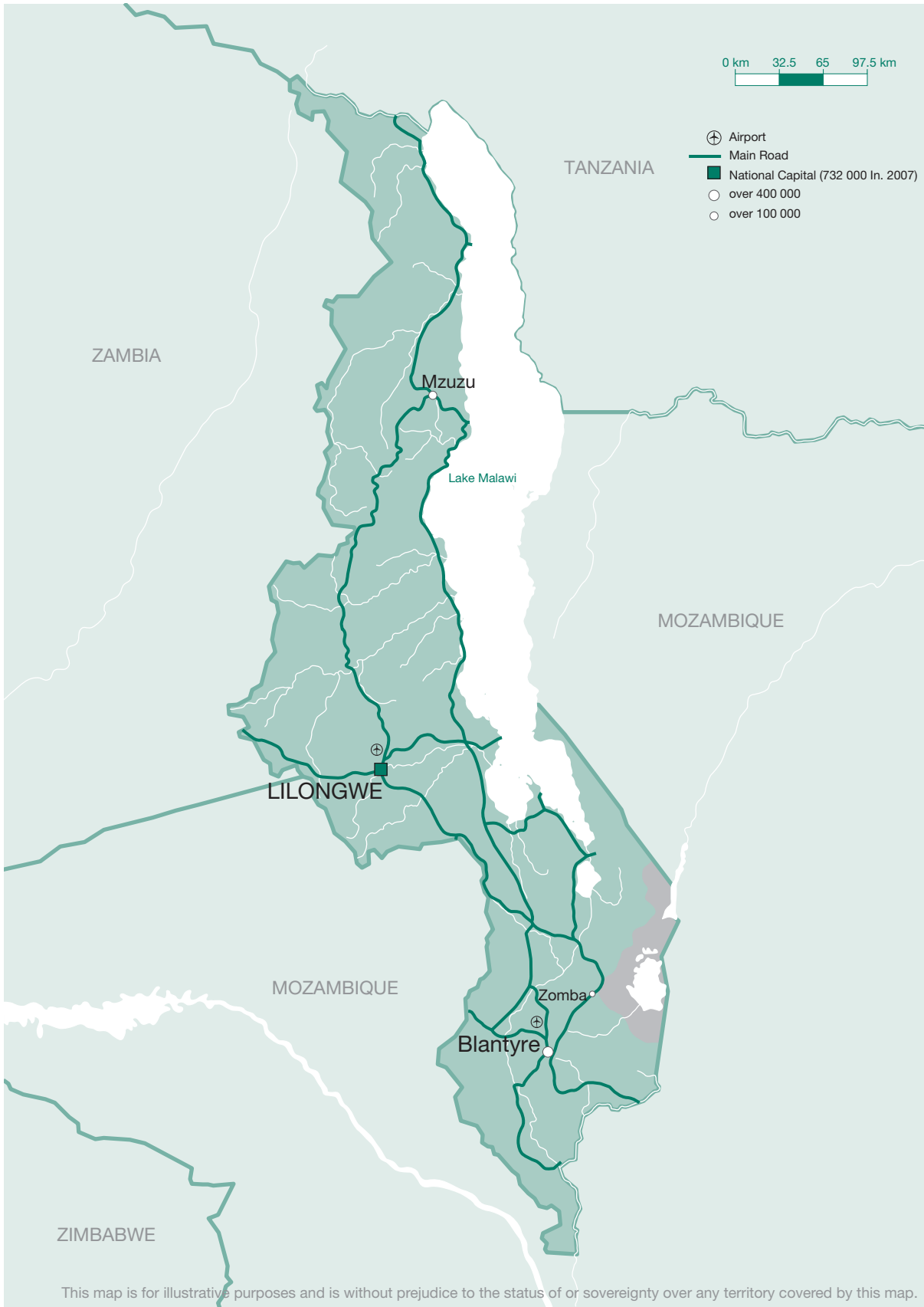


Malawi  
2011





# Malawi

## Overview

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The political and macroeconomic environment remained stable in Malawi through 2010. Malawi's real gross domestic product (GDP) is estimated to fall to 6.7% in 2010 from 7.6% in 2009. The slight reduction in real GDP growth is largely attributed to reduced agriculture output for maize and tobacco due to the drought experienced in some parts of the country at the beginning of the 2009/10 growing season. The main driving force for economic growth in 2010 has been strong performance in mining and quarrying, construction, financial and insurance services and information and technology. Real GDP growth is forecast at 6.4% in 2011 and 6.0% in 2012 reflecting stability in uranium output and levelling off of productivity gains in the agriculture sector as the agricultural growth rate has peaked.

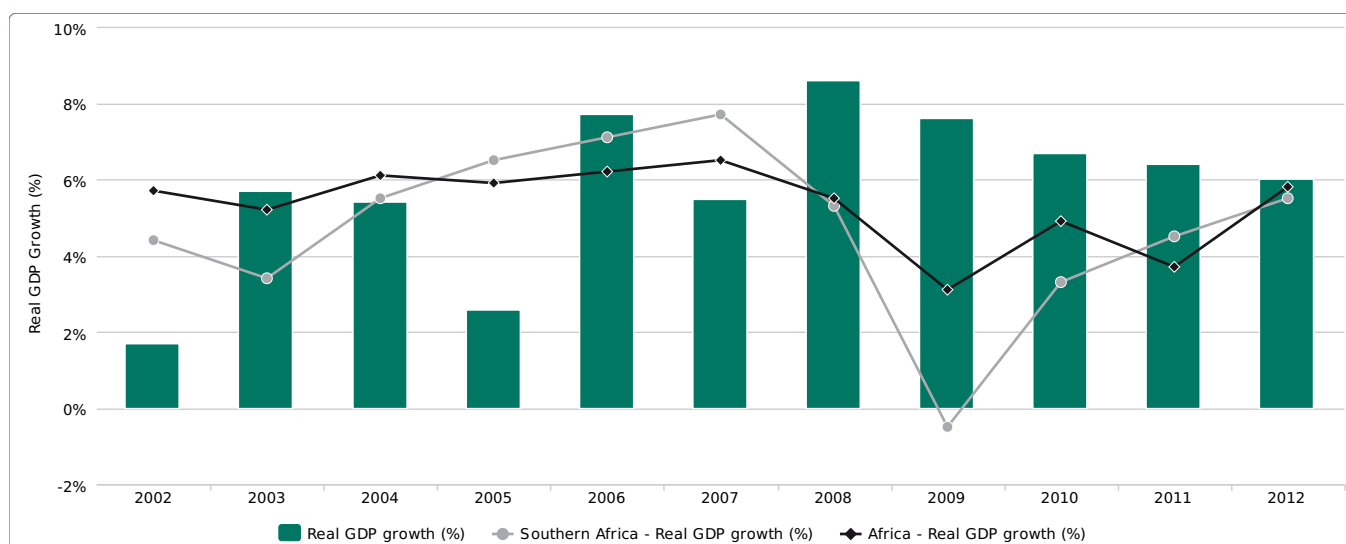
The recent global financial crisis had a limited impact on Malawi's economy. However, the key sector affected was the export sector, which faced fluctuating international prices (tea, coffee, tobacco) resulting in worsened terms of trade. Official development assistance (ODA), foreign direct investment (FDI) and remittances to Malawi also declined following the global credit crisis. In order to mitigate the impact of the global recession on the Malawi economy, the Reserve Bank of Malawi, among other initiatives, maintained the bank rate at 15.0% and issued Repurchase Agreements (REPO) instruments to combat inflationary pressures.

Malawi has made considerable progress on most Millennium Development Goals (MDGs) targets. According to Malawi's MDG report 2010, the country is on track to attain five of the eight MDG targets by 2015. The five MDG targets that are likely to be achieved are the eradication of extreme poverty, reduction of infant mortality, combating HIV/AIDS, malaria and other diseases, ensuring environmental sustainability, and developing global partnership for development. The three MDG targets in doubt are achieving universal primary education, reducing gender inequality and maternal mortality.

In 2010, the Government of Malawi (GoM) continued with the execution of the Farm Inputs Subsidy Programme (FISP). The FISP in its sixth year of implementation was designed to achieve food security and raise smallholder's income through increased maize and legume production. In the 2010/11 agricultural season, the Government FISP package include subsidies of 160 000 metric tonnes of fertiliser for maize; 8 000 metric tonnes of improved maize seeds and 1 600 metric tonnes of legume seeds. The FISP has been a very successful programme since introduction, leading to record surpluses in maize production including 1.3 million metric tonnes in 2008/09. Although Malawi experienced a prolonged period of abnormal dry weather in some areas in 2010, the country still recorded a surplus of about 900 000 metric tonnes of maize above annual food requirement.

Malawi's Emerging Partners (EPs) have concentrated on infrastructural development, agriculture, education and health. The EPs' investment has generated employment especially for Malawi's youth and their goods are found to be cheaper than western alternatives on the market. The overall advantage is that they are complementing traditional partners and not substituting them. The increasing importance of EPs notwithstanding, the share of traditional partners such as the UK, the USA and the EU in trade, ODA and FDI flows to Malawi is still significant. However, the increasing presence of China and India in Malawi comes with a number of challenges including flooding the market with cheaper Chinese and Indian goods which make local industries uncompetitive.

Figure 1: Real GDP growth (S)



Source: IMF and local authorities' data; estimates and projections based on authors' calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink <http://dx.doi.org/10.1787/888932404294>

Table 1: Macroeconomic indicators

	2009	2010	2011	2012
<b>Real GDP growth</b>	7.6	6.7	6.4	6
<b>CPI inflation</b>	8.4	7.7	7.6	6.2
<b>Budget balance % GDP</b>	-3.6	-1.1	-6.3	-7.4
<b>Current account % GDP</b>	-2.1	1.1	-1.6	-3.3

Source: National authorities' data; estimates and projections based on authors' calculations. Figures for budget balance refer to fiscal year July (n-1)/ June (n).

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink <http://dx.doi.org/10.1787/888932406650>

## Recent Economic Developments and Prospects

Table 2: GDP by sector (in percentage)

	2005	2010
<b>Agriculture, forestry, fishing &amp; hunting</b>	34.7	31.7
<b>Agriculture, livestock, fishery, forestry and logging</b>	-	-
<b>of which agriculture</b>	-	-
<b>of which food crops</b>	-	-
<b>Mining and quarrying</b>	1.3	2.1
<b>Mining, manufacturing and utilities</b>	-	-
<b>of which oil</b>	-	-
<b>Manufacturing</b>	8.7	10.5
<b>of which hydrocarbon</b>	-	-
<b>Electricity, gas and water</b>	1.5	1.3
<b>Electricity, water and sewerage</b>	-	-
<b>Construction</b>	5.3	4
<b>Wholesale and retail trade, hotels and restaurants</b>	18.8	18.4
<b>of which hotels and restaurants</b>	-	-
<b>Transport, storage and communication</b>	6.7	8.5
<b>Transport and storage, information and communication</b>	-	-
<b>Finance, real estate and business services</b>	6.7	8.1
<b>Financial intermediation, real estate services, business and other service activities</b>	-	-
<b>General government services</b>	3.4	3.2
<b>Public administration &amp; defence; social security, education, health &amp; social work</b>	-	-
<b>Public administration, education, health</b>	-	-
<b>Public administration, education, health &amp; other social &amp; personal services</b>	-	-
<b>Public administration, education, health &amp; social work, community, social &amp; personal services</b>	-	-
<b>Public administration, education, health &amp; social work, community, social services</b>	-	-
<b>Other community, social &amp; personal service activities</b>	-	-
<b>Other services</b>	12.8	12.2
<b>Gross domestic product at basic prices / factor cost</b>	100	100

**Source:** Authors' estimates based on National Statistical Office, Ministry of Economic Planning and Development.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932407619>

In 2009 real GDP growth expanded by 7.6%, driven by the agricultural sector, mining and quarrying activities

against the backdrop of commencement of newly commissioned Kayelekera mine, information and communications. Real GDP in 2010 is estimated at 6.7% which is less than the growth in 2009 but above the 6% Malawi Growth and Development Strategy (MGDS) targets. The slowdown is due to poor agricultural harvest recorded in 2010 following drought in some parts of Malawi at the beginning of the 2009/10 growing season. However, some key sectors such as mining and quarrying; construction; information and technology; financial and insurance services witnessed strong growth. In 2011 and 2012, the real GDP growth is expected to moderate to 6.4% and 6.0% respectively.

Agriculture remains the mainstay of Malawi's economy, accounting for a 32% share of GDP with 60% of the total exports coming from tobacco alone. This revealed clearly that the economy of the country is largely undiversified. The agriculture sector recorded a growth rate of 13.9% in 2009 following bumper yields on account of good weather during the 2008/09 season and the Farm Input Subsidy Programme. Growth in the agricultural sector slowed down to 1.5% in 2010 as a result of dry spells that affected most parts of the country at the onset of the 2009/10 crop season. The sector is expected to grow by 6.4% in 2011 subject to good weather and further expansion expected in the sugar sub-sector. One threat for the country, however, is the current global campaign against the use of additives to burley tobacco in cigarette manufacturing. Burley tobacco, the main type of tobacco grown in Malawi is naturally bitter and manufacturers need to use additives to make it palatable to smokers. Since tobacco is the main foreign exchange earner for the country, a ban on these additives to burley tobacco would have serious repercussions on the foreign exchange availability.

Mining and quarrying is gradually taking a greater share of Malawi's economy. The sector is expected to grow by 83% in 2010 compared to about 9% in 2009. This is driven by uranium production at the Kayelekera Uranium Mine in Karonga and high demand for coal for tobacco processing and industrial use. For the same reason, the mining and quarrying sector is forecasted to grow by 72% in 2011. The on-going road, Nsanje inland port and other public construction works are expected to drive growth in the construction sector by about 17% in 2010.

Following country-wide expansion of the mobile phone industry (especially by the country's largest operator, Bharti Airtel) as well as innovations in the electronic finance and telecommunications sub-sectors, the information and communications sector is projected to grow by 15.3% in 2010 and 11.1% in 2011. Similarly, the Financial and Insurance Services sector is estimated to grow by 11.5% in 2010, from 7.5% in the preceding year, on account of expansion of ATM services and introduction of mobile banking.

Manufacturing accounted for about 10% of GDP in 2009. The main activities are in agro-processing which is expected to grow by 7.5% in 2010 from 4.7% in 2009. Energy and foreign exchange shortages continued to undermine operations in the manufacturing sector as some firms are scaling down operations. This situation may degenerate with serious negative effects on Malawi's economy if the problems are not addressed quickly.

Public investment and private consumption are estimated to be the key drivers of real GDP in 2010. The situation is projected to remain the same in 2011 and 2012. In fact, public investment is expected to register the largest growth in value in 2010. These public investments include construction work in housing, transport (roads, the Shire Zambezi waterway and Nsanje inland ports), energy and key welfare areas such as health, water and education sectors. The export sector is expected to pick up in 2011 and 2012 with the possibility of niobium and other uranium mines opening in the country.

Table 3: Demand composition

	Percentage of GDP (current price)		Percentage changes, volume			Contribution to real GDP growth		
	2002	2009	2010	2011	2012	2010	2011	2012
<b>Gross capital formation</b>	16.1	26.3	16.6	13.9	6.1	4	3.7	1.7
Public	5.6	14.1	18	13	7	2.3	1.9	1.1
Private	10.6	12.2	15	15	5	1.7	1.8	0.6
<b>Consumption</b>	97.2	99	4.9	4	5.3	5.2	4.2	5.4
Public	8.6	10.2	5	3.9	3.9	0.5	0.4	0.4
Private	88.6	88.8	4.8	4	5.4	4.6	3.8	5
<b>External sector</b>	-13.4	-25.3	-	-	-	-2.4	-1.4	-1.1
Exports	20.8	23.4	9.1	10.2	10.3	1.3	1.5	1.6
Imports	-34.2	-48.7	8.4	6.5	5.9	-3.7	-2.9	-2.7
<b>Real GDP growth rate</b>	-	-	-	-	-	6.7	6.4	6

**Source:** Data from local authorities; estimates (e) and projections (p) based on authors' calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

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## Fiscal Policy

The GoM, with the support of development partners, has been implementing a number of reforms since 2006 to improve fiscal management. These reforms are being implemented within the framework of the Public Financial and Economic Management (PFEM) Action Plan. One of the key reforms includes the rolling out of the Integrated Financial Management and Information Systems (IFMIS) to local assemblies, tax administration in areas of improved VAT and introduction of Electronic Tax Register (ETR). The country is also embarking on reforms to widen the tax base in order to capture more tax revenue from the informal sector. The 2009/10 budget estimates have been prepared based on the Medium Term Expenditure Framework (MTEF) principles. According to official sources, GoM planned to reinvigorate the medium-term fiscal framework by 2011.

Consequently, fiscal revenue collection has been strong. Domestic revenues have increased to 33.9% of GDP in 2009/10, from 31.9% of GDP in 2008/09. It is estimated to fall marginally in the medium term on account of the projected decline in grants and the expectation of moderate economic growth. There was under performance of grants in the 2009/10 fiscal year as development partners' disbursements were far less than commitments. For instance, not all the money expected from donors was delivered to the National AIDS Commission (NAC) and the health Sector Wide Approach (SWAP). The size of public spending as measured by total expenditures as a percentage of GDP has been growing over the years. In particular, government capital expenditure has been experiencing a gradual rise on the account of ongoing construction in transport and housing sector. The total expenditure and net lending for 2009/10 is projected at 35.0% of GDP. This is forecast to increase to 37.9% in 2010/11 and fall marginally to 37.3% of GDP in 2011/12.

Malawi's domestic debt stock as at end December 2010 stood at 154.7 billion Malawian kwachas (MWK) compared to MWK 172.6 billion in December 2009 as a result of a drop in the levels of domestic debt including treasury bills, and outstanding Ways and Means advances. Nevertheless, Malawi's fiscal deficit has been forecast to rise from 1.1% of GDP in 2010 to 6.3% in 2011 and 7.4% of GDP in 2012 as grants experience a gradual decline. The deficit will be financed mainly by domestic and external concessional borrowing.

Table 4: Public finances (percentage of GDP)

	2002	2007	2008	2009	2010	2011	2012
<b>Total revenue and grants</b>	24.1	31.7	30.1	31.9	33.9	31.5	29.9
Tax revenue	15.3	16.6	17.6	16.5	18.8	17.9	17.5
Oil revenue	-	-	-	-	-	-	-
Grants	6.9	13.6	10.9	13.8	11.7	10.9	9.6
Other revenues	-	-	-	-	-	-	-
<b>Total expenditure and net lending (a)</b>	31.9	33	32.8	35.5	35	37.9	37.3
Current expenditure	24.6	21.3	21.1	26.7	24.7	26.4	25.5
Excluding interest	19.4	17.8	18.9	24	22	24	23.5
Wages and salaries	6.9	5.1	5.5	5.7	5.7	5.8	5.8
Goods and services	8.1	6.6	7.7	11.9	10.4	12	11.8
Interest	5.1	3.5	2.3	2.7	2.7	2.4	1.9
Capital expenditure	7.4	11.5	11.7	8.8	10.2	11.5	11.8
<b>Primary balance</b>	-2.8	2.2	-0.4	-0.8	1.5	-3.9	-5.4
<b>Overall balance</b>	-7.9	-1.3	-2.7	-3.6	-1.1	-6.3	-7.4

a. Only major items are reported.

Source: Data from local authorities; estimates (e) and projections (p) based on authors' calculations.  
Fiscal year July (n-1)/June (n)

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932409557>

## Monetary Policy

Over the years, Reserve Bank of Malawi (RBM) monetary policy stance has been based on controlling monetary growth to achieve low and stable inflation rates and accumulate external reserves. In line with the arrangement with the IMF, government policies have been geared towards building up reserves to about three months of prospective imports by 2012.

For almost three years, the Malawian kwacha has been relatively stable at MWK 140 against the US dollar. GoM had strongly resisted pressure especially from development partners to allow depreciation of local currency. A *de facto* fixed exchange rate regime was adopted between 2006 and 2009 preventing the nominal exchange rate to balance demand and supply leading to foreign exchange shortages. However, the exchange rate of Malawian kwacha against the US dollar depreciated to 150.8 at end-December 2010 from 141.7 as at end December 2009. The Malawian kwacha is forecast to depreciate to MWK 153.0 / USD in 2011 in line with government commitments to the International Monetary Fund (IMF).

Broad money (M2) rose by 24.4% from MWK 139.6 billion in 2008 to MWK 173.8 billion in 2009 and by December 2010 it had risen further to MWK 203.9. According to RBM, growth in M2 was shored up by increased economic activity coupled with sizeable government's recourse to central bank resources. The annual rates of inflation have generally been declining and are contained within single digits over the past four years thanks to the increase in domestic food production following the agricultural input subsidies in 2006. From an average of 8.4% in 2009, inflation declined to 7.7% in 2010. Inflation is expected to ease further to 7.6% in 2011 and 6.2% in 2012 as global oil prices decline marginally and crop harvest increases.

The RBM's policy rate remained constant at 15% since 2007, but was revised downwards to 13% in August 2010. Consequently, the lending rate has declined from 19.25% in 2007 to 17.67% as at December 2010. However, the savings rate is very low at 4.14% in December 2010. The rate is too low for depositors to get a positive return on saving as the interest rate on savings is less than the rate of inflation.

## External Position

Malawi recorded 17.1% of GDP trade deficit in 2009 due to high import costs of petroleum fuel and fertilisers. In the same vein, the higher growth in imports than exports in 2010 also led to a deficit trade balance of 15.7% of GDP in spite of the increase in uranium exports. Malawi's trade deficit is expected to continue in the medium term, but widen marginally to 16.3% of GDP in 2011 and narrow to 15.6% in 2012. Service debts are expected to remain generally in deficit, due to the persistent high cost of transportation in and out of the country.

Current transfer as a percentage of GDP increased from 17.1% in 2009 to 21.0% in 2010 on account of the increase in donor disbursement following the approval of Extended Credit Facility (ECF) for Malawi in February 2010. Current transfers will slow in the medium term following cuts in donor funding. Overall, the current account is expected to improve from a deficit balance of 2.1% of GDP in 2009 to surplus balance of 1.1% of GDP in 2010. It is projected to worsen to a deficit balance of 1.6% of GDP in 2011 and 3.3% in 2012 as donor inflow dwindles and uranium export stabilises.

In 2010, the IMF approved a USD 79.4 million Extended Credit Facility (ECF) between 2010 and 2012. The first review of Malawi's progress under the ECF was completed in December 2010. The ECF replaces Poverty Reduction and Growth Facility (PRGF) and Exogenous Shocks Facility (ESF), which expired in August 2008 and December 2009 respectively.

Malawi's continued implementation of structural reforms and strong macroeconomic performances have attracted increasingly more ODA and FDI. Net ODA as a percentage of GDP increased from 16% in 2006 to 22% in 2009. FDI that dipped to USD 100 million in 2009 from USD 215.3 million in 2008 on account of the secondary effects of the global financial crisis, recovered to USD 180 million in 2010. The main countries of origin of FDI are Australia in the mining sector, South Africa in the communication sub-sector and India in the telecommunications sector.

The total external debt has been rising and in December 2010, it was reported at USD 1 010 million (representing 19% of the GDP) up from USD 900 million (representing 16.8% of the GDP) in December 2009. The increase was mainly due to disbursement by multilateral and bilateral creditors which exceeded principal repayments. Meanwhile, Malawi's gross foreign-exchange reserves rose from USD 252.4 million in 2009 to USD 371.4 million by end-December 2010 (2.2 months of import cover), largely as a result of increased donor inflows.

Services debts are expected to remain generally in deficit, due to persistent high cost of transportation in and

out of the country.

Table 5: Current account (percentage of GDP)

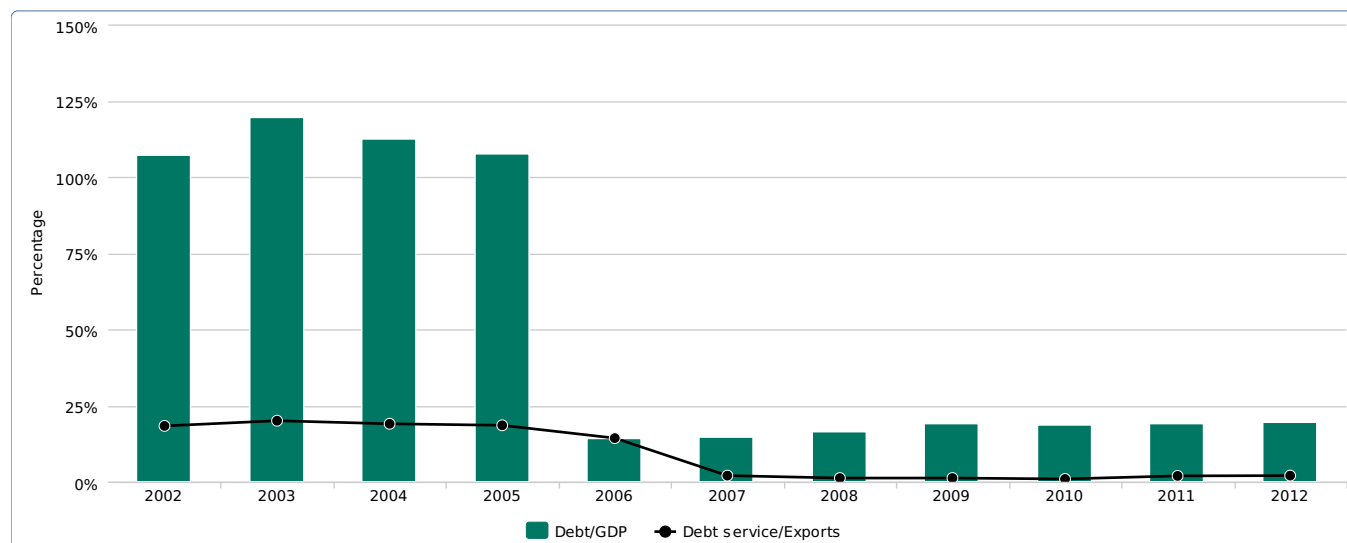
	2002	2007	2008	2009	2010	2011	2012
<b>Trade balance</b>	-6.8	-24.7	-18.6	-17.1	-15.7	-16.3	-15.6
Exports of goods (f.o.b.)	15.5	19.5	23.9	21.3	23.6	23.6	23.8
Imports of goods (f.o.b.)	22.3	44.2	42.5	38.4	39.3	40	39.4
<b>Services</b>	-0.2	-0.6	-0.6	-0.6	-0.5	-0.4	-0.4
<b>Factor income</b>	-1.4	-1.1	-0.7	-1.6	-3.7	-2.4	-3
<b>Current transfers</b>	0.3	16.8	19.6	17.1	21	17.6	15.6
<b>Current account balance</b>	-8.1	-9.6	-0.3	-2.1	1.1	-1.6	-3.3

**Source:** Data from local authorities; estimates (e) and projections (p) based on authors' calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932410526>

Figure 2: Stock of total external debt (percentage of GDP) and debt service (percentage of exports of goods and services)



**Source:** IMF and local authorities' data; estimates and projections based on authors' calculations.

Figures for 2010 are estimates; for 2011 and later are projections.

StatLink  <http://dx.doi.org/10.1787/888932404294>

## Structural Issues

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### Private Sector Development

Economic development in Malawi is constrained by several infrastructural and structural inadequacies, which affect the private sector. Inadequate infrastructure in transportation, telecommunications, power and water supply all hamper private sector growth. Other challenges to growth are foreign exchange shortages, fuel shortages and multiple taxation and administrative barriers to trade.

Road transport is the main method for imports and exports, but its high cost affects the competitiveness of Malawian products and consumer prices. A lack of capital investment restrains the potential of rail and air transportation. Despite the recent countrywide expansion of Information and Telecommunication (ICT) services in Malawi, access to telecommunications services in terms of telephone, mobile and Internet services is still limited, with coverage reaching less than 3% of the population.

As a net oil importer and landlocked country, Malawi is vulnerable to volatility in international oil prices. Perennial fuel shortages have, at times, either paralysed or severely inhibited the operations of different sectors of the economy. They have caused a decline in output by manufacturers, making Malawian exports uncompetitive. The fuel shortages have been blamed on both the rehabilitation work on the Tete bridge in Mozambique and a shortage of foreign exchange needed to import fuel.

Inadequate and intermittent power supply also constrains business and economic growth. The current installed energy and power capacity is 285 megawatts (MW) against a demand of 324 MW resulting in an average of 63 blackouts per year.

The government has introduced a number of regulatory and administrative reforms aimed at improving the business climate. For example, the Department of Physical Planning empowered city planning committees to concentrate on large projects leaving approvals for minor projects to technical committees. This reduced the time required for building-construction approvals. As well, the approval time for construction permits was reduced to a cap of 60 days. The Malawi Revenue Authority expanded its rapid customs clearance procedures by implementing a risk-based customs system for business entities. Other reforms in 2010 include the establishment of the Credit Reference Bureau, to improve access to credit, launch of the financial sector development strategy and improvement of a number of economic laws. In spite of these reforms, Malawi performed poorly in the 2011 World Bank's *Doing Business* survey ranking 133 out of 183 economies, one place lower than in the 2010 survey.

### Other Recent Developments

To consolidate the gains from the Farm Inputs Subsidy Programme to improve agricultural production and food security, the government is implementing several initiatives. The Green Belt Initiative is primarily a plan to use available water resources to decrease reliance on weather patterns through a series of innovative irrigation schemes. This includes incorporating both smallholder and estate irrigation along Lake Malawi and major rivers; the rehabilitation of existing irrigation systems; and civil and construction works of 42 000 hectares of the Shire Valley Irrigation project. The government has made budgetary provision in the 2009/10 and 2010/11 fiscal years for the Green Belt Initiative. It established a University of Agriculture and Natural Resources. The construction of modern silos in Mangochi, Mzuzu and Luchenza is also a part of the government initiative to improve agricultural production. Furthermore, in the course of 2010, the Ministry of Agriculture and Food Security in collaboration with development partners launched the Agriculture Sector Wide Approach (ASWAp) 2010-14. The ASWAp focus areas are food security and risk management, agri-business and market development and sustainable land and water management. The government also signed the Malawi Comprehensive African Agriculture Development Programme (CAADP) compact with the Africa Union's New Partnership for Africa's Development (NEPAD). These programmes are expected to boost agricultural production, improve food security and aid employment creation.

A major investment plan for 2011 and 2012 is the Kapichila Phase III hydropower project, which is expected to boost electricity supply and reduce power outages. Malawi also expects to undertake major electricity-generation rehabilitation works with support from the US Millennium Challenge Account (MCA). In the rural areas, the government is implementing the Rural Electrification Project using hybrid solar-wind power generation systems.

One of the major government responses to the persistent fuel shortages is the construction of an oil pipeline from the Indian Ocean port of Beira in Mozambique to Nsanje in southern Malawi, at an estimated cost of USD 140 million. The current means of transporting fuel, via road, is associated with both delays and high costs.

Other recent economic developments in 2010 include:

- the introduction of mobile banking services by some Malawian Banks including the Opportunity International Bank of Malawi (OIBM) in conjunction with the two mobile phone network operators - Airtel (formally Zain) and Telekom Networks Malawi (TNM). This initiative enables mobile phone users to receive and transfer money across bank accounts, as well as pay for goods and services via mobile phones;
- an increase in uranium extraction as the operations of the uranium mine in Kayelekera, which began operating in 2009 at close to full capacity;
- a formal commission for the Nsanje World Inland Port, the terminus of the Shire-Zambezi waterway project.

The Shire-Zambezi waterway project, begun in 2009, will provide a 238-kilometre direct waterway transportation system between Nsanje in southern Malawi and the port of Chinde in Mozambique. Upon completion, Malawi will no longer be landlocked, which should reduce import and export costs significantly.

For the first time in Malawi's history, the government began a national registration programme with the issuance of national identity cards to all citizens. The programme is expected to aid policy making and planning for socio-economic services.

Following the enactment of a credit bureau law, a private company, the Credit Reference Bureau (CRB), opened offices in Malawi. The CRB is expected to enhance access to credit and reduce the numbers and incidence of loan default through providing financial institutions easy access to credit-history information of loan applicants.

In November 2010, in Punta Del Este, Uruguay, at the fourth Conference of the Parties, the 172 parties of the World Health Organization Framework Convention on Tobacco Control (WHO-FCTC) treaty proposed to ban or restrict tobacco additives used to make cigarettes more appealing to new smokers. The ban will seriously affect the production of burley tobacco in the world. Malawi will be heavily hit by the ban as one of the world's leading producers of burley tobacco, growing nearly 200 million kilograms per year. The crop accounts for about 60% of total annual foreign earnings and 13% of GDP. The proposal to ban additives further amplifies the need for diversification of the country's agro-economy. Although diversification has been a government goal, there has been minimal progress. Farmers have been urged to increase production of crops such as pigeon peas, cassava, cotton, tea and coffee, among others, in a bid to expand Malawi's export base. Until crop diversification and production of other crops is successful, Malawi is still reliant on tobacco crops, hence, although seemingly contrary to the process of crop diversification, a cigarette manufacturing plant is in the pipeline for 2011.

In order to boost the tourism and hospitality sector, the government is undertaking construction and rehabilitation works at several airports, including those at Likoma, Kamuzu International, Chileka and Karonga. Work is also ongoing at the construction of an international conference centre, a new five-star hotel and 20 presidential villas. Furthermore, the government plans to build a modern Institute of Tourism in Lilongwe to address the shortage of skilled labour in the sector. In the 2011 World Economic Forum *Travel and Tourism Competitiveness Index*, Malawi was ranked 121 out of 139 countries. While the country ranked fairly high in environmental sustainability (42) and natural resources (46), its performance in the category of business environment and infrastructure is dismal placing it at 133 out of the 139 countries surveyed for the Index. A scenic and diverse natural environment – including nine national parks and wildlife reserves, such as Lake Malawi National Park, which is a United Nations Educational, Scientific and Cultural Organization (UNESCO) World Heritage Centre – presents abundant growth opportunities in the tourism sector.

Overall, development is hindered by numerous issues, including poor tourism infrastructure, weak human resource capacity, the credit crunch arising from the global economic crisis, persistent foreign exchange and fuel shortages, unfavourable weather patterns and the effects of climate change.

## Emerging Economic Partnerships

China is the single-most important emerging partner (EP) for Malawi. Malawi established diplomatic ties with China at the end of 2007. The relationship and co-operation between the two countries has garnered visible and tangible results. For example, China provided USD 45 million in grants for the new parliament building and USD 55 million for the 101-kilometre Karonga-Chitipa road. China also provided concessional loans of USD 90 million for a construction project in the capital, Lilongwe, consisting of a new five-star hotel, an international conference centre and 20 presidential villas and USD 80 million for the construction of a University of Science and Technology. Other commitments include financing to construct a new stadium, with a capacity to seat 40 000, in Lilongwe. China also has investments in the cotton processing industry in Balaka.

Chinese FDI, which was just USD 0.96 million in 2006, jumped to USD 11.25 million by 2009; over 55% of the investment is in manufacture. In 2009, the total bilateral trade volume between the two countries reached USD 82 million, which has almost doubled compared to USD 44 million in 2007. The export volume from Malawi to China in 2009 was USD 17 million, while imports from China were USD 65 million in the same period. Since 2008, China has provided 53 government scholarships to Malawian students. About 200 officials, technicians and specialists from Malawi have been invited to China for seminars and training programmes. Seventeen Chinese doctors work in Kamuzu Central Hospital and Mzuzu Central Hospital.

The second most important EP is India. Co-operation with India is primarily in agricultural development and pharmaceuticals. India has recently provided Malawi with cumulative lines of credit worth USD 180 million, largely for agriculture development (especially for irrigation projects under the Green Belt Initiative) and partly for pharmaceuticals (especially HIV-related medicines). From India's perspective, Malawi is attractive as a potential source of minerals, particularly uranium. Malawi is also backing India's bid to secure a permanent seat on the United Nations Security Council.

Brazil and Cuba are also EPs with diplomatic ties and trade and co-operation agreements, albeit at different degrees. In 2010, Brazil pledged funds for the school-food programme in some districts of Malawi. Malawi has signed a technical co-operation agreement with Brazil, and agreed to open an embassy in Brazil. Economic partnerships with Cuba are in the social sphere, specifically in the areas of education and professional training (especially medical doctors) and social work.

Malawi has been receiving development assistance from Arab donors, including from the Arab Bank for Economic Development in Africa (*Banque Arabe pour le Développement Économique en Afrique* [Badea]) and the Kuwait Fund. In 2010, Iran and Malawi agreed to co-operate in various fields, and Iran expressed interest in investing in mining and agriculture in the country.

The increasing importance of EPs notwithstanding, traditional partners (United Kingdom, United States and European Union) in terms of trade, ODA and FDI flows to Malawi remain significant. However, as Chinese investment is highly visible, the impression is that China is the leading partner. The number of migrants from China adds to this impression. Chinese migration to Malawi has become the second highest (Indians who have been in Malawi for over a century form the highest group of migrants). Data from the Ministry of Home Affairs shows that over 40% of all expatriate permits approved in 2009 were issued to Indians, Chinese and Pakistanis, with India leading with 184 citizens (28.2%), 54 Chinese (8.3%) and 28 Pakistani (4.3%).

It is very important to note that the EPs are complementing the traditional partners and not substituting for them. The principal reason is that traditional partnerships have provided economic support for the national budget, projects and dedicated grants; in other words, traditional development assistance rather than the often project-based support or loans from EPs. In general, traditional partners support the government's foreign reserve position and seek to assist in achieving internal and external balances. Support from traditional partners can be cumbersome to access, difficult to account for and can sometimes be intrusive and undermine sovereignty because of strict accountability requirements. In contrast, EP support is more demand-driven, less tied and more "user friendly". Both Chinese and Indian aid entails more "aid-in-kind" rather than a cash transfer. On the down side, Chinese-led construction projects are implemented by Chinese companies with a significant share of Chinese workers and, in most cases, construction materials and equipments come from China.

The EPs present new challenges and opportunities. The overall advantage is that they present non-traditional sources of aid, which can complement the traditional sources. The EPs' investment has increased employment and economic activities in Malawi. Additionally, Chinese and Indian goods are cheaper than western alternatives on the market. Therefore, their goods potentially increase consumer and total surplus due to the fact that for the same amount of money, Malawians can access more and a broader variety of goods and services. For instance, generic Indian pharmaceuticals are cheaper than brands from traditional partners and thus facilitate better access to health care services. However, the increasing presence of China and India in Malawi comes with a number of challenges including the unending debate and allegation of poor quality and counterfeit products. Flooding the market with cheaper Chinese and Indian goods makes local industries uncompetitive, forcing them

to adapt or face extinction.

## Political Context

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Malawi's 2009 presidential and parliamentary elections were declared free and peaceful by national and international election observers. Civil society organisations contribute to development processes by constantly influencing policy decisions in various sectors of the Malawi economy. Consequently, Malawi has improved in the Transparency International 2010 *Corruption Perception Index* to 85 out of 178 countries from 89 out of 180 in the 2009 index. In the Economist Intelligence Unit's *Democracy Index 2010*, Malawi ranks 85<sup>th</sup> out of 167 countries, up by 14 places from 99 out of 167 in 2008. The 2010 *Ibrahim Index of African Governance* ranked Malawi 22<sup>nd</sup> out of 53 countries, with an overall score of 51.7 out of 100, the same score as the previous year; nevertheless, Malawi's ranking improved by one place. Even though there has not been any conviction of prominent public or private sector officials in Malawi, the Malawi Electoral Commission (MEC) was suspended in December 2010 following an audit report showing that MKW 1.4 billion (USD 9.3 million) disappeared from the MEC account without justification.

Malawi's government has undertaken a number of initiatives aimed at strengthening governance and the rule of law, including the establishment of a Democratic Governance Sector Working Group (SWG) to facilitate co-ordination of the democratic governance interventions in the country. The signs of progress in governance areas and the improvement in global ranking notwithstanding, concerns remain. These include the reported use of state resources by incumbents for campaigning purposes; limited means for citizens to hold their elected representatives to account; inter-party conflicts; and the recently approved media-ban law that empowers the Minister of Information to ban any publication considered to be operating against the public interest. Most groups outside government, including the donor community and the media, condemned the media-ban law considering it a threat to democracy and freedom of expression.

The ruling Democratic Progressive Party (DPP) under the leadership of Malawi's President, Bingu Wa Mutharika, has the majority of seats in parliament. Various legal battles with government and internal leadership wrangles within the Malawi Congress Party (MCP) and the United Democratic Front (UDF) have made the two main opposition parties less effective. As a result, the DPP-led government has managed to pass several bills including the national budgets (2009/10 and 2010/11) without strong opposition. Meanwhile, the last local government elections were held in 2000 and Malawi has had no local councillors since 2005 as elections were not held in 2005 and 2010 as required by the country's 1995 constitution. Malawi's 1995 constitution stipulates that local government elections should be held every five years. However, with the recent amendment of the Local Government Act, Malawi's president has been given sole powers to decide when to conduct the local government elections.

The local government elections (LGEs), initially scheduled for May 2010, were postponed to 23 November 2010 and later again postponed to April 2011. As of the end of January 2011, MEC offices were not open raising fears that the LGEs will not be held as scheduled. Meanwhile, four by-elections were held in Malawi in 2010. Two in mid-January, in Machinga South-East necessitated by the UDF incumbent, who was declared ineligible and Lilongwe North-West, due to the death of the MCP incumbent. The other two by-elections were held in October because of the deaths of the incumbents in Dowa South-East and Mangochi Malombe constituencies. The ruling DPP confirmed their popularity by winning three out of the four positions contested during the by-elections, while the United Democratic Front (UDF) retained the Machinga South-East seat.

In August 2010, four ministers were removed from office in a cabinet reshuffle. The reshuffle saw Peter Mutharika, the President's brother move from the Ministry of Justice and Constitutional Affairs to the Ministry of Education and the appointment of the first lady, Callista Mutharika, to the cabinet, with responsibility for maternal, infant and child health. In another development, in 2010, the Vice President, Joyce Banda, and former cabinet minister, Khumbo Kachali, were expelled from their positions as first and second vice presidents of the DPP as a result of accusations of anti-party activities. Media reports linked their dismissal to political manoeuvring over the president's succession plans.

In 2010, two homosexual men were convicted and sentenced to 14 years in prison following their public engagement as couple. However, due to national and international pressure, including from some Malawians donors, they were granted presidential pardons and released from prison.

President Mutharika was appointed chair of the African Union (AU) in January 2010 for a period of one year. The appointment strengthened President Mutharika's popularity and international influence, especially in African politics. President Mutharika inaugurated the new parliament building in Lilongwe on 21 May 2010. The magnificent building, funded by China, is expected to create a conducive environment for members of parliament to interact with the electorate and other interest groups. Most of the principal officers including the speaker, the president, the leader of the house and leader of opposition were allocated office spaces in the new building. Office spaces for other parliamentarians are planned for the next phase.

## Social Context and Human Resource Development

The government suggests that Malawi is making progress on all eight MDGs. However, the Malawi MDG report for 2010 reveals that the country is on track only in five MDGs. These include eradicating extreme poverty; reducing infant mortality; combating HIV and AIDS, malaria and other diseases; ensuring environmental sustainability; and developing global partnerships for development. The remaining three MDGs on achievement of universal primary education; promotion of gender equality and empowering women; and reducing maternal mortality are unlikely to be attained by 2015.

The Malawi MDG Report 2009 notes that poverty declined from 54% in 1990, to 39% in 2009. Poverty is expected to decline further to 37% in 2010 and to 27% by 2015 due mainly to the consistent implementation of the FISP; the Malawi Rural Development Fund (MARDEF); the One Village One Product (OVOP) scheme; and the Youth Enterprise Development Fund. Progress through programmes such as these are helping to lower youth unemployment; the youth unemployment rate, registered at 4% in 2009 is forecast to follow a similar downward trajectory to 3.8% in 2010 and 1.9% by 2015. Yet, in spite of these positive developments, the United Nations Development Programme (UNDP) - *Human Development Report 2010* (HDR) reveals that Malawians' overall well-being is still low with a poor score of 0.385 on the Human Development Index, ranking 153 out of 169 countries in 2010. Nevertheless, the HDR 2010 reports that the life expectancy of Malawi has improved to 54.6 years from 52.4 in the previous year.

Malawi has achieved some progress in the MDG of promoting gender equality and empowering women, but is below the MDG target and is seemingly moving backwards according to other international indices. For example, the HDR-Gender Inequality Index increased between 2009 and 2010 from 0.490 to 0.708 (with a measure of zero indicating full equality between men and women). Although more women were appointed into the public service sector, including a female vice president for the first time in Malawi's history, and the number of women in parliament has moved up from 13% in 2008 to 22% in 2010, these successes do not mirror Malawian society as a whole. Malawi is 28 percentage points short of the 50% MDG target goal of proportion of seats held by women in the parliament and 35 percentage points short of reaching the 50% goal of the share of women in wage employment in the non-agriculture sector. Another area of concern is maternal health. Maternal mortality is significantly high at the estimated 807 per 100 000 live births in 2009. At the current trend, it is forecast that maternal mortality will not come down to meet the target of 155 per 100 000 live births by 2015. Malawi's HIV/AIDS prevalence rate, according to the MDG Report 2009, was 12.0% in 2009. The rate is estimated to fall to 6.0% by 2015, but not enough to achieve the MDG target of 0% by 2015. The poor trends in the health sector may be reversed with improvement in health care facilities, the health delivery system and increases in the number of skilled personnel.

According to government sources, the MDG goal of reducing child mortality will be attained and surpassed. The children under-five mortality rate per live birth reduced from 189 deaths per 1 000 in 2000 to 122 deaths per 1 000 in 2009. Malawi has also made improvements in immunisation rates with 84% of one-year old infants immunised against measles in 2009 and is likely to meet the 100% target goal by 2015. Improvements in child and infant mortality can be attributed to improved household food security and access to safe drinking water. For example, the proportion of Malawians with access to safe drinking water rose from 75% in 2006 to 81% in 2009 (above the 2015 MDG target of 74%). Access to basic sanitation has also increased from 88% in 2006 to 93% in 2009).

Malawi is making progress towards achieving universal primary education in line with the national Education Sector Plan (NESP). The net enrolment rate (NER) has been increasing from 79% in 2008 to 83% in 2009. It is projected that the NER will reach 92% in 2015, 8 percentage points less than the MDG target of 100%. The increases in the NER are mainly due to the free primary education policy and the abolition of uniforms as a prerequisite to attend primary school. Youth literacy has also increased from 82% in 2008 to 84% in 2009. Conversely, violations of children's right to protection, child abuse, exploitation and discrimination are increasing daily. For example, an estimated 3.1 million children are reported to be growing up in violent homes and witnessing domestic violence.

Recent development gains, particularly in economic growth, food security and the MDGs may decelerate or even halt due to limited resources and inadequate capacity in both the public and private sector to implement programmes that will improve basic social services. This knowledge is spurring the government to implement, fully or partially, most programmes and policies outlined in the Malawi Growth and Development Strategy 2006-11. The government is committed to the Education Sector-wide Approach and the implementation of the NESP. It is constructing additional classrooms at the primary, secondary and tertiary levels and scaling up school-food programmes. In the health sector, the government is constructing and upgrading health facilities, training health personnel and increasing the availability and accessibility of antenatal services. In the 2009/10 financial year, the government has undertaken the rehabilitation and expansion of Zomba Central Hospital as well as completing the construction at the Orthopaedic Centre at the Kamuzu Central Hospital. Government

measures to improve socio-economic conditions in Malawi are ongoing in both the education and health sectors: sectors that directly support economic development.