MACRO-FISCAL PROFILE

MALAWI

May 2016

Key Indicators	
Population (2014)	18.0 million
Per capita GDP (2014, current USD)	$1,200
Average population growth rate (2010–2014)	3.1%
Government revenue as % of GDP (2014)	22.8%
Country income classification	Low

Source: World Bank, 2015; CIA, 2016.

Country Policy and Institutional Assessment Ratings (1 = low, 6 = high), 2014	National	SSA Mean
Efficiency of revenue mobilization	4.0	3.5
Equity of public resource use	3.5	3.3
Fiscal policy	3	3.1
Macroeconomic management	3	3.5
Quality of budgetary and financial management	3	3.1

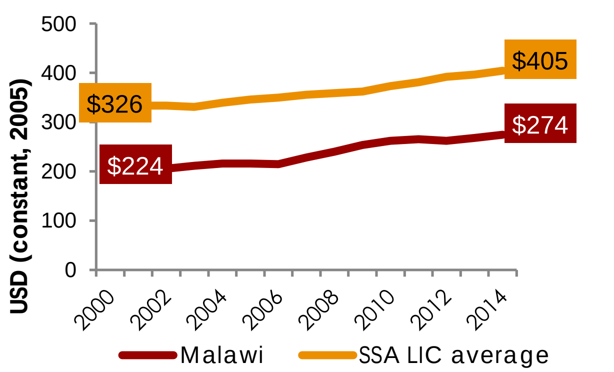
Source: World Bank, 2014.

Macroeconomic Forecasts

Indicator	2013	2014	2015 (est.)	2016 (proj.)	
Real GDP growth	5.2%	5.7%	2.9%	4.0%	4.9%
GDP per capita growth	2.0	2.6	-0.2	0.9	1.8

Source: Bhatia and Mwanakatwe, 2016; IMF, 2015.

Figure 1: GDP per Capita Growth



Source: World Bank, 2015.

Overview

Malawi's recent macroeconomic performance has been uneven, with significant negative effects on gross domestic product (GDP) growth from weather-related events and withdrawal of external funding. Heavy floods and a subsequent drought cut maize yields by 30% in 2015. The "Cashgate" scandal in 2013, related to misuse of public funds, led to a stoppage of on-budget support from donors equivalent to 4.5% of GDP. Malawi also has a limited export base with restricted potential for growth. Exports of tobacco, sugar, and tea accounted for two-thirds of total exports in 2013, down from nearly 80% in 2008. Overall exports declined in nominal terms in 2015, but are expected to grow again from 2016 on. Dependence on agricultural commodities and a lack of export diversification expose Malawi to external demand shocks. Resource revenues were 14% of GDP in 2013 (World Bank, 2015). Although Malawi has benefited from lower oil prices, the overall import-export outlook is negative due to continuing depreciation of the Malawi kwacha versus the U.S. dollar. In the long term, low agricultural productivity, poor infrastructure, a deteriorating business environment, volatile external fund flows, and a rising population all pose risks to sustained growth. The aggregate effect of these external factors is that medium-term macroeconomic conditions are projected to be difficult, exacerbated by internal trends.

Responding to persistent high inflation during fiscal year (FY) 2014/15, the central bank raised interest rates under a tight monetary policy regime, which, accompanied by a credit crunch, dampened economic activity. Recent efforts to raise lending have not yet paid off, despite key interest rates being negative in real terms. The government of Malawi (GOM) also faces internal fiscal challenges. A recent increase in the costs of a wage bill, compounded by a shortfall in tax revenue, has added extra stress to government finances.

Political Economy

Indicators regarding policy response and governance efficiency indicators for Malawi are nearly average for countries in sub-Saharan Africa (SSA). Tax administration is weak, though Malawi's tax revenue to GDP ratio is above that of several neighboring countries, at 16.3% (FY 2014/15, actual), despite recent rebasing of the GDP series. The previous government undertook several significant macroeconomic reforms in 2012.

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The government in power since 2014 has followed a broadly pro-growth policy, including openness to foreign investment and a positive business environment. It has committed to reforms in public financial management practices to encourage a resumption of budget support. However, the government also accepts that levels of external budget support will not reach previously typical levels. In the short term, an ongoing food crisis exists in Malawi, with an estimated 2.8 million people suffering from food insecurity after extreme climate events; thus, the GOM will focus its spending on the agricultural sector and disaster relief, along with changes to increase the sustainability of health financing.

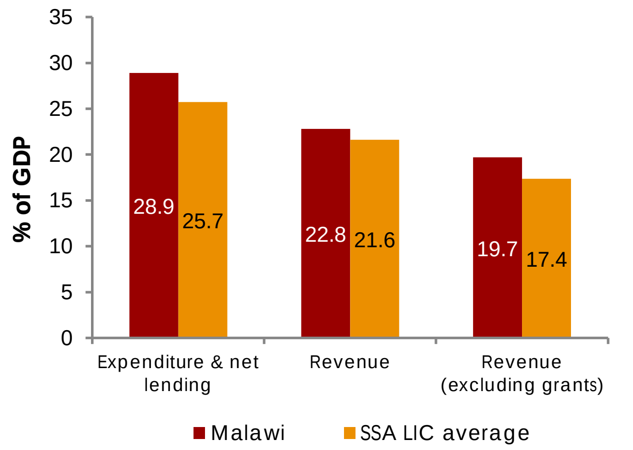
GDP and Economic Growth

Recent macroeconomic crises led to a downgrade in the International Monetary Fund's GDP growth estimate for Malawi in 2015, to 3% from nearly 6%. This downgrade interrupts a recent upward trend in real GDP growth of above 5% annually. Going forward, growth is expected to improve in 2016, to 4.5%. In the period 2011–2013, a decline occurred in real GDP per capita (Figure 1). This number is estimated to be US$352 at 2015 exchange rates. Given this current trajectory, Malawi will remain a low-income country (LIC) in the medium term, based on the World Bank threshold.

Government Revenue and Expenditure

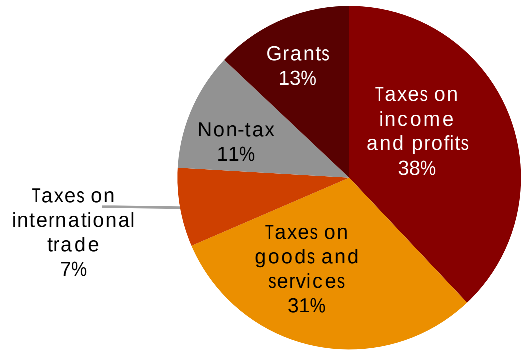
Malawi has slightly higher revenue as a percentage of GDP than the average for LICs (Figure 2). The decline in grant revenue, primarily due to a drop in on-budget support, accounted for nearly 7 percentage points of GDP between FYs 2013/14 and 2014/15. Increasing tax collection and other sources of domestic revenue will be important in covering the shortfall. This effort will require strengthening value-added tax collection, improving tax audits of large taxpayers, and broadening the tax base (Figure 3).

Figure 2: Government Revenue and Expenditure (2014)



Source: Bhatia and Mwanakatwe, 2016.

Figure 3: Revenue (2014)



Source: IMF, 2015.

On the expenditure side, the new government elected in 2014 responded to demands for increases in public sector salaries—an increased outlay equivalent to 1.25% of GDP. The GOM increased public spending through the hiring of 10,500 new teachers in FY 2014/15. It faces a crowding out of capital and infrastructure spending due to its high wage spending and debt payments. In FY 2014/15, 26% of the central GOM budget was spent on wages, 15% on interest payments, and only 20% on development (itself 82% foreign funded). Subsidies and internal transfers took 18% of GOM outlay. Spending on subsidies and transfers has remained stable in real terms; a reform of the fuel subsidy program has helped to reduce spending obligations. Based on the government's recent pronouncements, further expenditure cuts are expected in the FY 2016/17 budget.

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