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### Press Statement by IMF Staff Mission to Malawi

The following statement was issued today in Lilongwe by a staff mission from the International Monetary Fund (IMF):

"An IMF mission visited Lilongwe during February 19 - March 3 to review performance under the IMF Staff Monitored Program (SMP). In view of the satisfactory performance to date, the mission began discussions on policies for a Poverty Reduction and Growth Facility (PRGF) arrangement. These discussions are progressing well, and the mission welcomes the government's attention to a sustainable medium-term macroeconomic framework and impediments to economic growth. There are, however, uncertainties related to the impact of the recent dry spell on agricultural output and on the budget. The government and donors are working together to develop an appropriate food security policy. Therefore, the mission and government have decided to continue PRGF discussions after more information is available in April to ensure that the budget and the PRGF take full account of the current situation.

"During the IMF mission in July 2004, the Government of Malawi requested an SMP in support of the government's efforts to rebuild its track record of economic policy implementation. The program aims to address macroeconomic imbalances by containing government borrowing and holding down inflationary pressures. These objectives are set out in *quantitative targets*, such as borrowing and discretionary spending. The program also includes *structural targets* to improve financial management, in particular budget monitoring and expenditure control. The IMF staff monitors the government's progress in implementing the SMP every three months.

"The mission team is encouraged by the new government's commitment to enforce stricter public expenditure management, as unbudgeted expenditures were the cause of a worsening macroeconomic situation in recent years. Likewise, the government's policy of zero-tolerance for corruption is very important. The achievements made in both of these

areas in a short time are impressive and are already providing economic and social benefits.

"There are now signs that Malawi's economy is improving: the domestic debt situation has eased and credit to the private sector has begun to expand. We now expect growth to rise to just under 5 percent in 2005, in part because of a strong expansion in private sector activity. Inflation has increased to 14 percent due to rising food prices and the previous monetary expansion, but is expected to decline to 11 percent by the end of the year. However, these projections may need to be revised to reflect the implications of the dry spell.

"The government met critical quantitative targets through the first half of the fiscal year (July-December). Notably, discretionary spending and net domestic financing to the government were below their ceilings due to the government's effort to control spending and stay within the 2004/05 budget. The government breached the ceiling on civil service wages, however, due to unexpected complications arising in the implementation of the pay reform scheme introduced in October. The pay reform is a medium-term project, and the overruns and other needed adjustments need to be resolved in the upcoming budget. Aided by the good performance of the government and the resumption of donor support, the Reserve Bank of Malawi (RBM) also met the targets on net foreign and net domestic assets.

"The government completed all structural targets under the SMP through end-January. Importantly, the RBM activated the credit control module of the government's payments system. This system now rejects all payments in excess of the ministries' credit ceilings set by government and based on the approved budget. This alone should greatly reduce spending pressures over and above the budget allocations. In addition, the government has made significant progress in instituting a set of regular processes to monitor and improve expenditure control at the ministry level.

"The mission team welcomes the progress made under the SMP. The new government is demonstrating its commitment to sound macroeconomic policies, and in particular, the need to arrest debt accumulation. It is critical that the government continue to observe spending levels in the program and for the RBM to be more aggressive in mopping up the monetary overhang and to take any necessary steps to contain inflation, as broad money growth has been running above target."

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