Malawi Government

Annual Public Debt Report

FY2022/23

MINISTRY OF FINANCE AND ECONOMIC AFFAIRS

ANNUAL PUBLIC DEBT REPORT

2022/2023

DEBT AND AID MANAGEMENT DIVISION

2023

JULY

ACCRONYMS AND ABBREVIATIONS

ADF	African Development Fund
ADMARC	Agricultural Development and Marketing Corporation
AfDB	African Development Bank
AFREXIM	Africa Export-Import Bank
ATM	Average Time to Maturity
ATR	Average Time to Re-fixing
CNY	Renminbi, official currency of the People's Republic of China
COVID-19	An infectious disease caused by the SARS-CoV-2 virus
DAD	Debt and Aid Management Division
EIB	European Investment Bank
ESCOM	Electricity Supply Corporation of Malawi
EUR	Euro, official currency of European Union member states
FDI	Foreign Direct Investment
FX	Foreign Exchange, currencies other than the Malawi Kwacha
FY	Financial Year of Malawi
GBA	Green Belt Authority
GBP	Pound sterling, official currency of the United Kingdom
GDP	Gross Domestic Product
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
OPEC Fund	OPEC Fund for International Development
IR	Interest Rate
JPY	Japanese Yen, official currency of Japan
MK	Malawi Kwacha, official currency of Malawi
MoFEA	Ministry of Finance and Economic Affairs
MTDS	Medium-Term Debt Management Strategy
NEEF	National Economic Empowerment Fund Limited
PFMA	Public Finance Management Act of 2022
PV	Present Value
RBM	Reserve Bank of Malawi
SDR	Special Drawing Rights, unit of account based on five currencies- United States Dollar, EURO, CNY, JPY and GBP
TDB	Trade and Development Bank
TPD	Total Public Debt
USD	United States Dollar, official currency of the United States of America

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PREFACE

The analyses contained in the *Annual Public Debt Report* are integral elements of the Government of Malawi (GoM's) surveillance of economic and financial market developments that affect public debt. The Report helps Government and other stakeholders to monitor the evolution of the public sector's debt liabilities and its debt-service obligations over time. Statistics in the Report provide early warning signals of possible debt vulnerabilities.

This Report covers loans and debt securities under Budgetary Central Government (BCG) and Central Bank. It also covers publicly guaranteed debt of State-Owned Enterprises (SOEs). In terms of valuation, unless otherwise stipulated, domestic debt is reported at Face Value and external debt is Disbursed Outstanding Debt. In keeping with international standards as stipulated in the Public Sector Debt Statistics Guide, future debt reports will adopt nominal valuation and continue to extend institutional, and debt instrument coverage. Stocks are reported as of end-March 2023 and end-March 2022. Cumulative flows are reported starting from beginning-April 2022 to end-March 2023.

This edition highlights debt management operational issues, fulfills statutory requirements, analyses the drivers of debt growth, outlines efforts to restore debt sustainability, reviews Malawi's external and domestic debt portfolios and performs risk and cost analysis for the FY2022/23. The public debt portfolio review provides an analysis of the public debt composition. The external debt portfolio review focuses on the evolution and composition of debt by holder, creditor and currency. The domestic debt portfolio review focuses on the main instruments and holders of debt. The risk and cost analysis assesses the risks and costs associated with the external and domestic debt portfolios.

An electronic version of this report is available on the Ministry's website: www.finance.gov.mw.

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EXECUTIVE SUMMARY

Since the publication of the previous edition, Malawi continues to face the lingering effects of the COVID-19 pandemic, the ongoing war in Ukraine and the tightening global financial conditions which have resulted in financial sector instability.

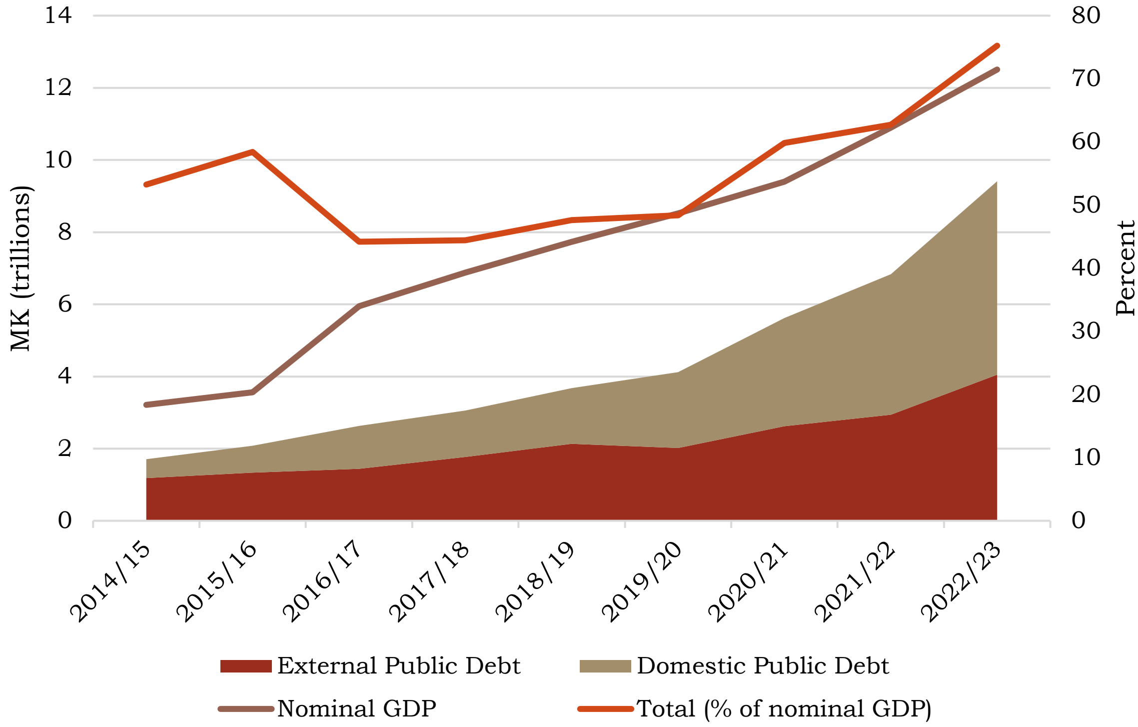
On the back of these imported global challenges, in the period under review, Malawi experienced several shocks, including the worst Cholera outbreak in decades and Cyclone Freddy. The Cyclone, which affected Southern parts of Malawi in early 2023, destroyed maize fields and strategic infrastructure such as roads and schools.

Malawi's overall public and external debt was assessed as in distress by the World Bank and International Monetary Fund (IMF) in November 2022. The Government of Malawi (GoM) is currently engaged in debt restructuring negotiations to restore the sustainability of the debt portfolio and pave the way for an IMF Extended Credit Facility program.

As at end-March 2023, Total Public Debt (TPD) stock stood at MK9.41 trillion (USD9.17 billion), equivalent to 75 percent of FY2022/23 GDP, up by 38 percent from MK6.84 trillion (USD8.37 billion) or 63 percent of GDP as at end-March 2022. Of the TPD stock, USD3.94 billion or 32 percent of GDP was external debt while MK5.36 trillion (USD5.22 billion) or 43 percent of GDP was domestic debt.

As can be seen in Figure 1, external, domestic and total public debt have been on an upward trend since FY2014/15. The debt-to-GDP ratio, however, fell from FY2015/16 to FY2016/17, increased gradually until FY2019/20 and then increased rapidly from FY2019/20 to FY2022/23.

Figure 1: Evolution of Public Debt Since FY2014/15



Sources: MoFEA staff calculations.

The external debt stock consisted of 73 percent Central Government Debt and 27 percent Central Bank debt as at end-March 2023. These proportions have remained the same compared to end-March 2022. Multilateral creditors continue to account for the largest proportion of Malawi's external debt at 68 percent, followed by commercial creditors at 21 percent and bilateral creditors at 11 percent. Since end-March 2022, the total amount owed to multilateral creditors increased by 16 percent, to commercial creditors increased by 3 percent and to bilateral creditors fell by 10 percent.

With a holding of USD1,414.34 million or 36 percent of total external debt, the International Development Association (IDA) continues to be the largest creditor to the Government of Malawi. The second largest creditor is Africa Export Import Bank (AFREXIM) with a holding of 12 percent, followed by the African Development Fund (ADF) and the International Monetary Fund (IMF) at 11 percent and Trade and Development Bank (TDB) at 8 percent. The bulk of the creditors cumulatively held the remaining 22 percent.

Special Drawing Rights (SDR) accounted for 49 percent of the total external public debt. After decomposing the SDR basket into its tradable currencies, the USD accounted for the largest proportion of external debt at 59 percent, followed by the EUR and CNY at 19 percent and 12 percent, respectively. Other currencies accounted for the remaining 10 percent.

The domestic debt stock comprised 85 percent (MK4.48 trillion) Treasury Notes, 13 percent (MK676.39 billion) Treasury Bills, and 4 percent (MK201.69 billion) Promissory Notes. The Promissory Notes were issued to clear audited arrears under the arrears clearance program. In terms of holdings, commercial banks remained the biggest holders of domestic debt and held MK1,998.58 billion. They were followed by the Reserve Bank of Malawi (RBM) at MK1,638.74 billion. The insurance sector came third with a holding of MK579.13 billion. The rest was held by other players, including the household sector.

During the period under review, the MK25 billion guarantee issued to NBS Bank Plc for ADMARC Ltd and the USD7 million Guarantee issued to CDHIB for Salima Sugar Company Limited were discharged. The MK12 billion guarantee issued to CDH Investment Bank for ADMARC Ltd was partly discharged.

Overall, yields on Treasury securities on the primary market continue to edge upwards on the back of the continued increase in domestic financing needs and from geopolitical risks due to the Russia-Ukraine war which is increasing inflationary pressures across the globe. Domestic headline inflation has also risen, driven by both food and non-food items.

Major risks concerning the Malawian public debt status include refinancing risk, interest rate risk and exchange rate risk. The Average Time to Maturity (ATM), an indicator of refinancing risk, is measured at 6.9 years, a decrease from 7 years as at end-March 2022 due to the increased share of Domestic Debt, which has a lower ATM of 2.4 years as well as commercial external debt with lower maturity period. In terms of exposure to exchange rate risk, 41 percent of the Present Value of debt was denominated in foreign currency, implying significant exchange rate risk.

SECTION I: RECENT DEVELOPMENTS THAT HAVE AFFECTED PUBLIC DEBT MANAGEMENT

1.1 Introduction

Public debt is accumulated from government borrowing to finance recurrent and development operations. Borrowing allows Government to spend more than what it raises in tax revenue to stabilise the economy and finance public investment. Public debt can, however, pose a risk to Government, especially when the stock becomes large, making it difficult for Government to meet its debt service obligations.

Public debt can be broadly split into external debt and domestic debt. In Malawi, external borrowing mainly takes place in the form of loans. Moreover, the current policy is to only contract external loans which are concessional.[1] Domestic debt in Malawi, on the other hand, is mainly in the form of securities.

Public debt management in Malawi is currently facing significant challenges. Exports of goods and services experienced a large decline in 2020 and, while they recovered in 2021, they did not do so to the same level as in 2019. In the meantime, imports of goods and services increased even while global prices were rising, and Government expenditure increased due to Government's response to the COVID-19 pandemic. In response to these factors, the Government increased borrowing, resulting in an unsustainable debt burden for Malawi.

1.2 Macroeconomic Developments

Since the publication of the previous edition, global challenges have included the lingering effects of the COVID-19 pandemic, the ongoing war in Ukraine and the tightening global financial conditions which have resulted in financial sector instability. At a regional level, Sub-Saharan Africa has faced a funding squeeze that has increased debt burdens and put pressure on exchange rates

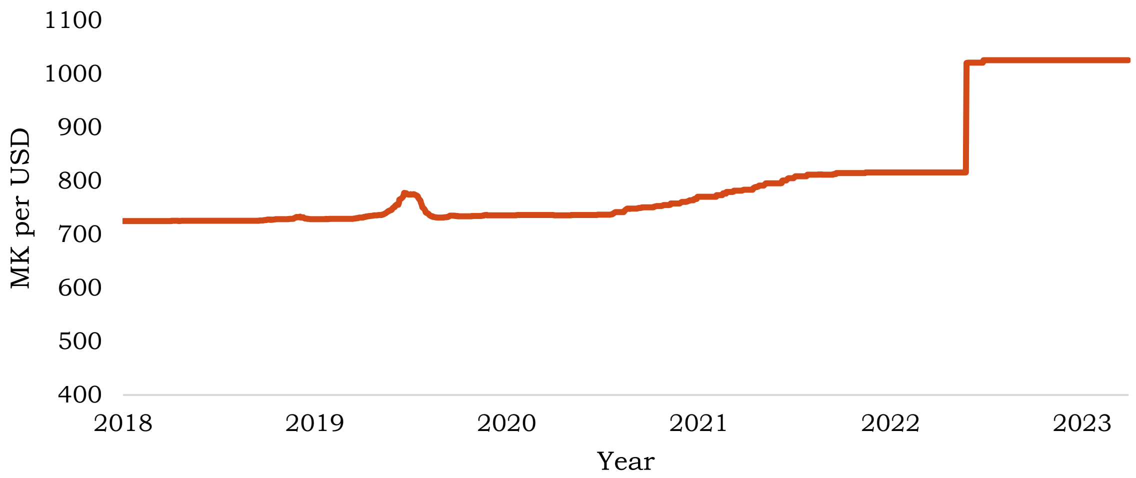
[1] Concessional debt is defined as loans with an original grant element of 35 percent or more.

across the region. These challenges have led to a slowdown in economic activity, with the IMF forecasting growth for the region to decline to 3.6 percent in 2023 from 3.9 percent in 2022 and 4.8 percent in 2022.[2]

On the back of these imported global and regional challenges, in the period under review, Malawi experienced several shocks, including the worst Cholera outbreak in decades and Cyclone Freddy. The Cyclone, which affected the Southern part of Malawi in early 2023, destroyed strategic infrastructure such as roads and schools, had a significant death toll, and negatively impacted agriculture. In this context, real GDP growth fell from an estimated 4.6 percent in 2021 to an estimated 1.1 percent in 2022. In 2023, GDP is projected to grow at 1.9 percent.

Increased pressure on the exchange rate and a shortage of reserves triggered the RBM to devalue the Kwacha by 26 percent in May 2022. As well as contributing to inflation, the alignment worsened the debt position as it increased the Malawi Kwacha value of debt denominated in foreign currency. The evolution of the Malawi Kwacha to US Dollar exchange rate since 2018 is shown in Figure 2.

Figure 2: Daily exchange rate, MK per USD



Source: MoFEA staff calculations based on RBM data

Year-on-year inflation continues to rise and reached 27.0 percent in March 2023. This increase is driven by high global fuel prices, fertiliser, food, prolonged supply chain disruptions and exchange rate pass-through from the

[2] IMF Regional Economic Outlook, Sub-Saharan Africa, April 2023

Kwacha alignment. To rein in inflation, the RBM increased the monetary policy rate from 14 to 18 percent in October 2022. This hawkish monetary policy stance will have a bearing on the interest bill and increase the refinancing risk of Malawi's domestic debt portfolio. Selected macroeconomic indicators from 2018 to 2022 are shown in Table 1.

Table 1: Selected Macroeconomic Indicators

Indicator	2018	2019	2020	2021	2022	2023
Real GDP growth (%)	4.4	5.4	0.8	4.6	1.1	1.9*
Inflation rate (%) (annual percent change in consumer prices)	9.2	9.4	8.6	9.3	21.0	27.0**
Exchange rate, MK per USD (end of period)	729	736	771	816	1,026	1,026**
Primary balance (percent of GDP)	-2.7	-1.9	-2.7	-3.6	-5.0	-3.3*

Source: MoFEA staff calculations
***Projections**
****As at end-March**

1.3 Debt Management Policy Objective

The Government is currently drafting a debt management policy to guide debt management in Malawi. The policy will conform to the legal provisions that govern public debt management as set out in Section 71 of the Public Finance Management Act (2022). The Act specifies that the primary objective of debt management is to ensure that financing needs and debt service obligations of the Government are met adequately, at the lowest possible cost and at a reasonable level of risk, and that the secondary objective is to support the development of a vibrant domestic debt market.

1.4 Fulfilment of Statutory Requirements

Part VIII of the Public Finance Management Act (PFMA) of 2022 outlines the statutory requirements relating to debt management in Malawi. Amongst other things, the Act requires publication of a Medium-Term Debt Management Strategy (MTDS) and an Annual Borrowing Plan (ABP).

1.4.1 Medium-Term Debt Management Strategy

In light of the above, Section 71 of PFMA mandates the Ministry of Finance and Economic Affairs (MoFEA) to develop a MTDS. In keeping with this requirement, the Ministry developed the MTDS covering the years 2022-2026,[3] which was approved by Cabinet in January 2023. The Strategy outlines the Government's plans to achieve the optimal debt portfolio, grounded in a ranking of the risk and cost trade-offs of alternative debt management strategies.

The MTDS considered four strategies as follows:

- Strategy 1: assumed status quo. This was the preferred strategy under the previous MTDS. It maintains the existing instrument mix and is aimed at lengthening the domestic debt maturities by issuing 2- and 3-year Treasury Notes (T-Notes) while increasing the proportion of 5-and 7-Year T-Notes;
- Strategy 2: assumes a moderate increase in external financing whilst domestic financing is similar to Strategy 1;
- Strategy 3: assumes more external financing from the issuance of a USD100 million Diaspora Bond (commercial borrowing) in 2023; and
- Strategy 4: aligned to the programming of the International Monetary Fund under the proposed four-year Extended Credit Facility (ECF) which focuses on maximising concessional financing.

Out of the four strategies, Strategy 4 was the most preferred as it provides lower re-financing and re-fixing risks compared to the other strategies albeit with a higher foreign exchange risk.

The MTDS also sets out key targets the Government intends to use in the reference period as follows:

- Given the high debt burden, the Government will only borrow from concessional external sources to secure the necessary financing for its development objectives;

[3] Available at http://www.finance.gov.mw/index.php/our-documents/annual-debt-reports

- Government will continue to develop the domestic debt market to improve its depth, liquidity and efficiency; and
- To minimise the impact of costs and risks to Government, the indicators in Table 2 shall be used as a guideline to provide measurable and quantifiable targets for monitoring purposes.

Table 2: Key Targets for 2022-2026

Indicator	Figure as of end-March 2023	Target
Domestic debt ATM (years)	2.4 years	Above 3 years
Implied interest rates (%)	9.6 percent	Below 11 percent
FX debt (% of total debt)	40.6 percent	Below 60 percent

Source: Government of Malawi MTDS (2022)

1.4.2 Annual Borrowing Plan

To operationalise the MTDS, Section 72 of the PFMA requires the MoFEA to develop an ABP for each fiscal year. The ABP, which was first developed for FY2023/24,[4] outlines how the aggregate borrowing requirements for the year will be met and includes details on planned borrowing operations over the year, borrowing instruments to be used and, under domestic debt, the indicative timing of borrowings. It also includes information on preferred tenors of domestic instruments and projected disbursements of external financing.

1.5 Newly Signed Loans

During FY2022/23, Government signed new loans totalling USD297.80 million from IDA of the World Bank, OPEC Fund for International Development (OPEC Fund) and ADF of the African Development Bank. The largest of these loans was Shire Valley Transformation Program - Phase 2 under IDA at USD134.00 million followed by Emergency Power Restoration Project also under IDA at USD36.00 million.

[4] Available at http://www.finance.gov.mw/index.php/our-documents/annual-debt-reports

The loans will finance education, social, health, agriculture, energy, transport and water sectors. Table 9 in Annex 1 contains a full list of newly signed loans in FY2022/23.

1.6 Infrastructure Bond Projects

Government continues to raise resources for the Local Currency Infrastructure Development Bond (LCIDB) Programme to finance 15 high-value and high-impact projects.

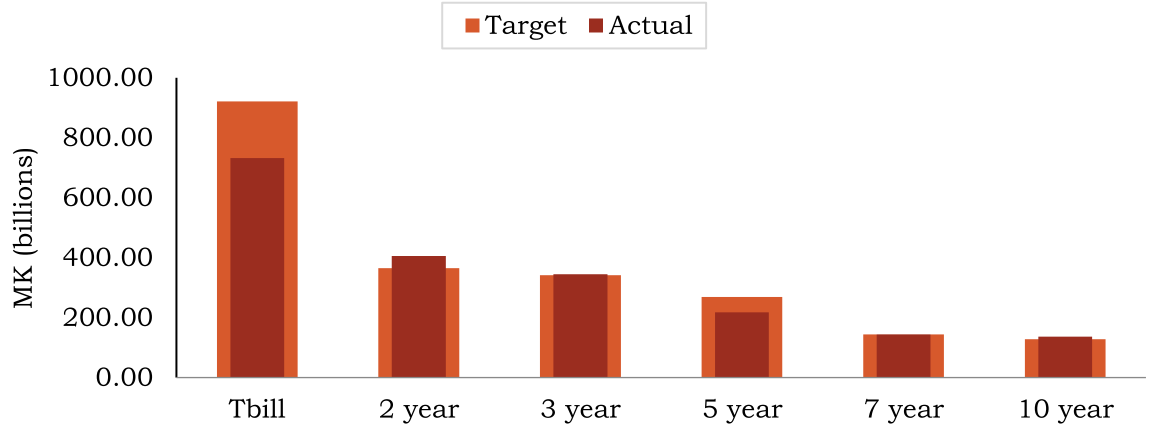
During the reporting period, Government raised MK34.17 billion against a planned MK65.02 billion for the Programme. The proceeds have financed (i) construction of the Aquatic Complex at the Kamuzu Institute for Sports, (ii) construction of the houses for security institutions, (iii) construction of the Nsanje-Marka railway line, (iv) rehabilitation of the Kaphatenga-Benga section of the M5 Road, (v) upgrading of the Dzaleka-Mpalo-Ntchisi-Malamo Road, (vi) upgrading of the Rumphi-Nyika-Chitipa-Ilomba Road and (vii) construction of the Multipurpose (Kholongo) Dam in Mponela, Dowa District.

Going forward, Government will continue issuing the infrastructure bonds to finance the ongoing projects as well as, when ready, the remaining projects under the program.

1.7 Performance of Debt Securities Issuance Calendar

During the FY2022/23, Government in collaboration with RBM, issued quarterly Treasury Securities Issuance Calendars with indicative amounts of Treasury Bills (T-Bills) and T-Notes, which were published on the RBM website. The 2018-2022 and 2022-2026 MTDS and FY2022/23 Annual Borrowing Plan guided the development of the Issuance Calendars. Overall, actual performance was slightly below the target with 91.32 percent of the total target amount being raised. This is a result of liquidity challenges faced by market players. As shown in Figure 3, T-Bills recorded an under-issuance of around MK189.81 billion while T-Notes issuances slightly overperformed by MK1.55 billion. In terms of T-Notes tenors, the highest under-issuance was observed on 5-year notes (MK51.49 billion). Nevertheless, this underperformance was compensated with over-issuances of 2, 3 and 10-year notes.

Figure 3: Issuance Calendar Performance FY2022/23

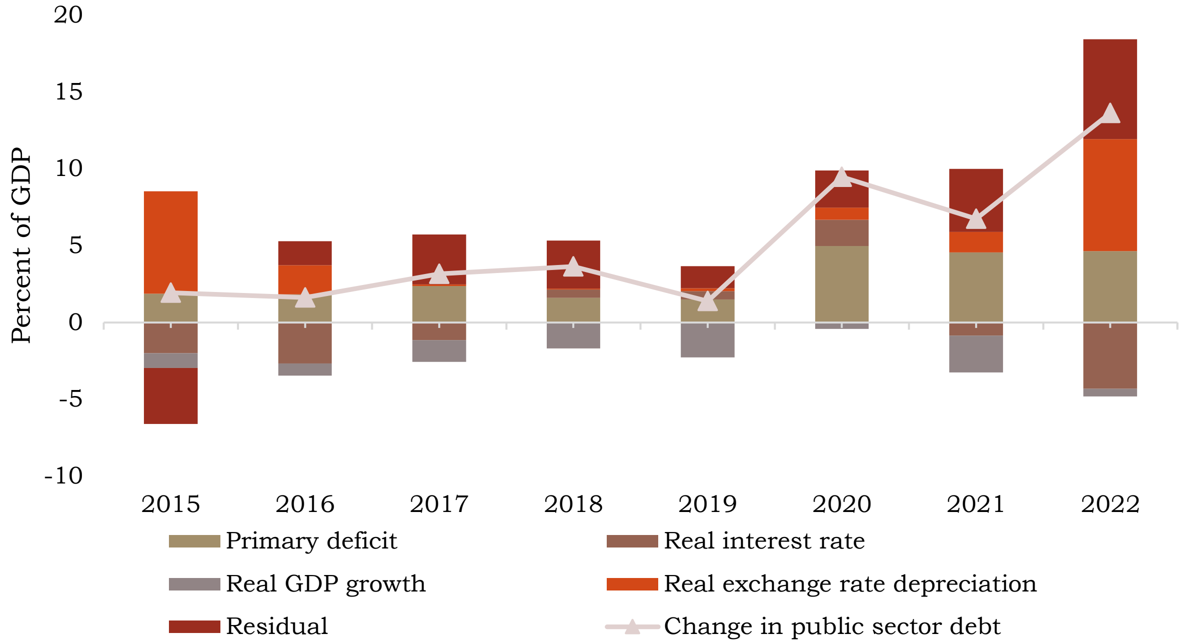


Sources: MoFEA staff calculations.

1.8 Drivers of Debt Dynamics

Malawi's public debt to GDP continues an upward trajectory since reaching the Heavily Indebted Poor Country (HIPC) and Multilateral Debt Relief Initiatives completion point in 2006. Increased public debt levels, persistently high fiscal deficits, and the larger share of high-cost domestic debt, in combination with greater risks related to rollovers, interest rates and currency fluctuations, have resulted in unsustainable public finances. The estimated historical drivers of public debt accumulation are presented in Figure 4. In 2022, public sector debt as a percent of GDP increased by 13 percentage points. The exchange rate alignment and primary deficit were the biggest drivers of this change, contributing 7.30 and 4.64 percentage points to the overall change, respectively.

Figure 4: Drivers of Debt Dynamics



Source: MoFEA staff calculations based on IMF/World Bank DSA data.

1.9 Debt Sustainability

A joint World Bank and IMF Debt Sustainability Analysis (DSA) conducted in the context of the Request for Disbursement under the Rapid Credit Facility and Request for the PMB in November 2022 assessed Malawi's external and overall public debt as in distress. The assessment has been downgraded from a similar exercise conducted under Article IV consultations in November 2021 which assessed overall public and external debt as unsustainable over the medium term. The most recent assessment is due to exceeding the IMF's thresholds for the present value of Malawi's overall public debt-to-GDP, present value of external debt-to-exports, external debt service-to-exports and external debt service-to-revenue ratios over the medium term as shown in Table 3.

The worsening assessment is exacerbated by Malawi's frequent weather-related shocks, high cost of borrowing and the worsening macroeconomic outlook. The Government is currently making efforts to restore debt sustainability as outlined in the following subsection.

Table 3: Public and External Debt Burden Indicators

Indicator	Threshold	2022	2023	2024	2025	2026
PV of total debt (% of GDP)	**35%**	66%	63%	63%	63%	62%
PV of external debt (% of GDP)	**30%**	22%	24%	23%	21%	20%
PV of external Debt (% of exports)	**140%**	202%	177%	165%	153%	138%
External debt service (% of exports)	**10%**	56%	27%	23%	20%	21%
External debt service (% of revenue)	**14%**	43%	25%	20%	18%	18%

Source: MoFEA compilation based on IMF/World Bank DSA data, November 2022

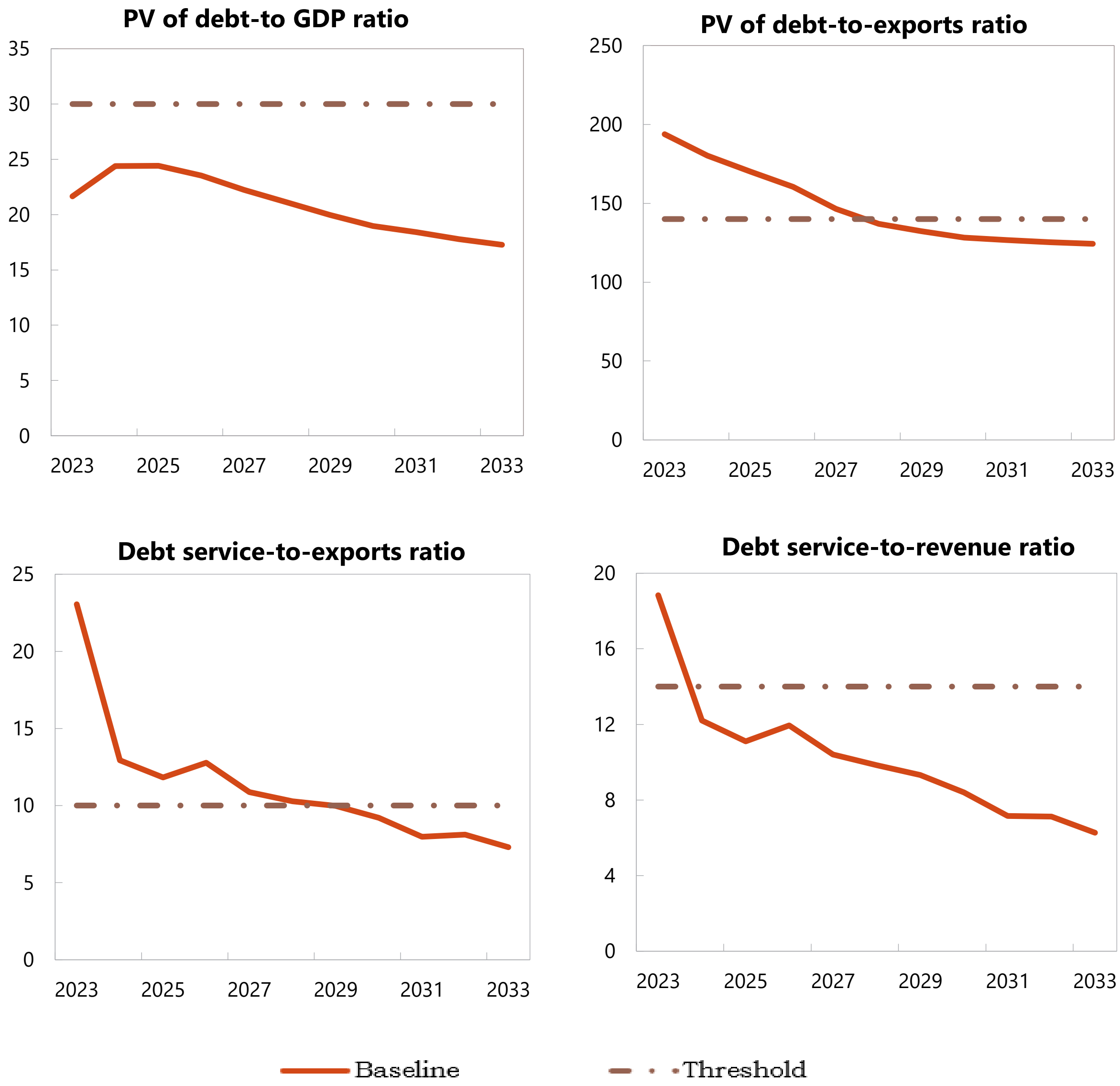
1.9.1 Efforts at Restoring Debt Sustainability

To restore debt sustainability in the medium-term in a credible manner, in May 2022, the Government engaged a legal and financial firm, Global Sovereign Advisory (GSA), to support the restructuring of Malawi's external debt. In October 2022, the Government finalised its Debt Restructuring Strategy. The Strategy aims at bringing back external debt to moderate risk of debt distress in the medium term through a combination of policy reforms, debt treatment and maximising external grant financing from development partners. Under the debt treatment, the Strategy is focused on maturity extensions and reprofiling of scheduled payments to ensure liquidity relief in the near term while also restoring Malawi's external debt sustainability in the medium term. Conditional on the successful completion of the Government's debt restructuring strategy, on a forward-looking basis, external debt would be considered sustainable.

Currently, negotiations are at an advanced stage and, in line with the Strategy, Government is in the process of obtaining financing assurances from its main official bilateral and commercial creditors.

Figure 5 shows the external debt sustainability assessment for Malawi post-restructuring in line with the Government's Strategy. The four key solvency and liquidity indicators demonstrate a downward trajectory in the medium term, allowing Malawi's debt sustainability to be restored.

Figure 5: Indicators of Public and Publicly Guaranteed External Debt Under Post-Debt Restructuring Scenario, 2023–33



Source: MoFEA Debt Restructuring Strategy

1.10 New developments On Debt Recording System

In March 2023, with assistance from Commonwealth Secretariat, the Ministry of Finance and Economic Affairs successfully migrated from Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) to Commonwealth Meridian for managing public and publicly guaranteed debt.

The Commonwealth Meridian will include integration with Integrated Financial Management Information System (IFMIS) and Central Securities Depository (CSD) System at the RBM for effective and timely recording of debt data.

SECTION II: TOTAL PUBLIC DEBT PORTFOLIO AS AT END-MARCH 2023

2.1 Composition of Total Public Debt

As at end-March 2023, the Total Public Debt (TPD) stock stood at MK9.41 trillion, which is equivalent to 75 percent of FY2022/23 GDP. It has increased by 38 percent from MK6.84 trillion,[5] or 63 percent of GDP, since end-March 2022. Both domestic and external debt contributed to this increase with domestic debt rising by 38 percent and external debt expressed in Kwacha also rising by 38 percent. Domestic debt issuances were used to fund the FY2022/23 budget deficit and refinance maturing debt. The increase in external debt expressed in Kwacha terms was largely driven by the alignment of the Kwacha against the dollar by 26 percent in May 2022.

Table 4: Evolution of Public Debt (in Millions)[6]

	2005	2006 (HIPC)	2019/20	2020/21	2021/22	2022/23
Total Public Debt (MK)	426,592	130,846	4,120,444	5,622,950	6,835,595	9,411,295
External (USD)	2,969	452	2,740	3,250	3,598	3,944
Domestic (MK)	73,337	68,957	2,100,180	3,004,457	3,897,819	5,362,526
Nominal GDP (MK)	326,957	430,522	8,520,572	9,395,877	10,897,321	12,507,189
Exchange Rate MWK-USD[7]	119	137	737	805	816	1026
			Percent of GDP			
Total (%)	130	30	48	60	63	75
External (%)	108	14	35	28	27	32
Domestic (%)	22	16	25	32	36	43

Source: MoFEA staff calculations.

[5] FY2021/22 was a short financial year with nine months. Thus, the GDP figure has been annualized to make it comparable to previous years.
[6] The figures for previous years have been revised due to a change in how foreign held debt is treated and revisions for AFREXIM loans and Promissory Notes.
[7] These exchange rates are used throughout the report.

2.2 Analysis of Interest Rates

Loans and debt securities in Malawi's public debt portfolio are on fixed interest rates. However, T-Bill rates reset when rolled over. In terms of implied interest rates, external loans registered a maximum of 1.88 percent while domestic securities registered a minimum of 0.73 percent and a maximum of 19.79 percent.

Table 5: Implied Interest Rates

External Loans	Implied Interest rate (%)	Securities	Implied Interest rate (%)
Existing and New ADF/ IDA/IFAD	0.80	T-Bills	15.69
Concessional-Others	1.16	2Y & 3YT-Notes	13.63
Semi-concessional (USD)	1.88	5Y & 7YT-Notes	17.75
Semi-concessional (CNY)	1.64	10Y T-Notes	19.79
		Promissory Notes	0.73

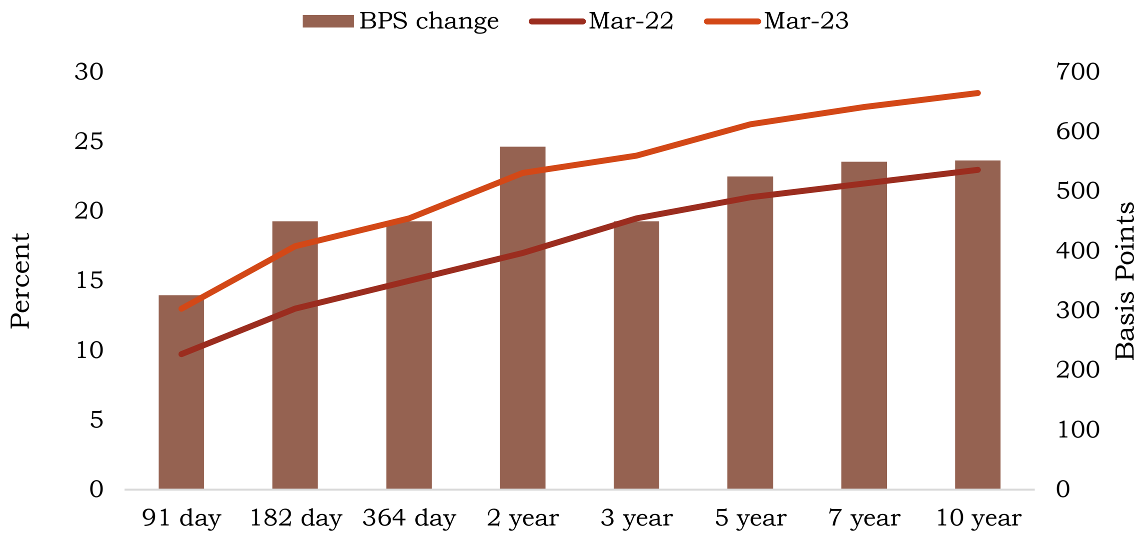
Source: MoFEA staff calculations.

2.3 Treasury Securities Yield Curve

Overall, yields on Treasury securities on the primary market continue to edge upwards on the back of continued increases in fiscal financing needs, exchange rate realignment and rising food and non-food prices, and geopolitical risks due to the Russia-Ukraine war which are putting pressure on inflation across the globe.

As shown in Figure 6, yields on the 91-day T-Bill went up by 326 basis points during the reporting period; while yields on the 182-day and 364-day tenors both went up by 450 basis points. For T-Notes, the biggest leap was on the 2-year tenor at 575 basis points increase.

Figure 6: Domestic Yield Curve for March 2022 and March 2023



Source: MoFEA staff calculations based on RBM data.

2.4 Debt Flows

Total Debt service in the reporting period amounted to MK1.78 trillion. Of this amount, total amortization (principal repayment) was MK1.16 trillion and total interest was MK626.98 billion.

In FY2022/23 domestic debt service amounted to MK1.66 trillion as compared to MK861.8 billion recorded in FY2021/22. This significant increase of about 52 percent is mainly on account of principal repayments, coupon and interest payments. Out of the MK1.66 trillion, amortisation amounted to MK1.07 trillion and interest payments to MK588.31 billion. This is compared with FY2021/22 amortisation and interest payments at MK576.2 billion and MK285.6 billion, respectively. For FY2022/23, domestic debt interest payment accounted for 22 percent of the total FY2022/23 budget.

In FY2022/23, external debt service amounted to MK127.2 billion. Of this amount, amortisation was MK88.5 billion and interest payment was MK38.7 billion. External debt service increased by MK79.8 billion (62 percent) from FY2021/22. The increase is attributed to the alignment of the currency and maturing external debt. Interest paid to non-residents accounted for 1 percent of the FY2022/23 budget.

2.5 Contingent Liabilities

In FY2022/23, Government issued a sovereign guarantee of USD50 Million to BADEA for a fuel financing facility on behalf of the National Oil Company of Malawi. During the same period, two guarantees were fully discharged. These were the MK25 billion Guarantee issued to NBS Bank Plc for ADMARC Ltd and USD7 million Guarantee issued to CDHIB for Salima Sugar Company Limited. Another guarantee, the MK12 billion guarantee issued to CDH Investment Bank for ADMARC Ltd, was partly discharged. The ADMARC guarantees were discharged through a World Bank Grant whilst the Salima Sugar Company guarantee was settled by the company.

In addition to the above, Government issued a Sovereign Guarantee to AUZANO Capital Ltd in September 2022 on behalf of the Smallholder Farmers Fertiliser Revolving Fund of Malawi (SFFRFM). However, due to non-performance of the Guarantee, the Government cancelled this in December 2022. Likewise, the Government Guarantee that was issued to QUAY in December 2021 for the implementation of the Lake Malawi-Lilongwe City Water Supply Project was cancelled due to non-performance.

SECTION III: EXTERNAL PUBLIC DEBT PORTFOLIO REVIEW

Malawi's total external public debt stock as at end-March 2023 amounted to USD3,944.50 million, a 10 percent increase from the end-March 2022 position of USD3,598.45 million. This was on account of an increase in disbursements on project loans and in the RBM's trade-financing facilities.

3.1 External Debt by Holder

As at end-March 2023, Central Government debt accounted for 73 percent of the total external debt, an increase by 11 percent since end-March 2022, and RBM holdings accounted for 27 percent of the total external debt, a 7 percent increase since end-March 2022.

Table 6: External Debt Stock, by Holder (USD Million)

Category	Mar-22	Mar-23	(%) Change
(1) Central Government	**2,615.64**	**2,895.27**	**10.69**
(%) of total	72.69	73.40	
(2) Central Bank	**982.81**	**1,049.23**	**6.76**
(%) of total	27.31	26.60	
Total External (1+2)	**3,598.45**	**3,944.50**	**9.62**

Sources: MoFEA staff calculations.

3.2 External Debt by Creditor

With a holding of USD1,414.34 million (36 percent of total external debt), IDA continues to be the largest creditor to the Government of Malawi. The second largest creditor is AFREXIM with a holding of USD454.34 million (12 percent of total external debt), followed by the ADF at 11 percent, the IMF also at 11 percent and TDB at 8 percent. The bulk of the creditors cumulatively held the remaining 22 percent.

Table 7: External Debt Stock, by Creditor and Creditor Category (USD Million)

Creditor	Mar-22	Mar-23	(%) Change
1. Bilateral	**464.63**	**417.71**	**-10.10**
Export-Import Bank of China (Main-Land)	253.97	223.01	-12.19
Export-Import Bank of India	124.21	111.07	-10.58
Kuwait Fund for Arab Economic Develop.	46.62	48.04	3.04
Saudi Fund for Development	30.05	29.65	-1.37
Compania Espanola De Seguros de Credito	5.48	2.74	-50.00
Abu Dhabi Fund for Development	3.14	2.14	-31.89
Government of Belgium	1.15	1.06	-7.60
2. Multilateral	**2,330.71**	**2,697.00**	**15.72**
International Development Association	1,182.21	1,414.34	19.90
African Development Fund	428.24	449.16	4.88
International Monetary Fund	389.70	439.53	12.78
European Investment Bank	69.14	118.43	71.28
International Fund for Agric. Development	97.55	108.89	11.62
OPEC Fund for International Development	77.15	80.49	4.33
Arab Bank for Economic Development in Africa	69.47	69.99	0.75
Nordic Development Fund	17.25	16.18	-6.19
3. Commercial	**803.11**	**829.79**	**3.32**
Africa Export-Import Bank	598.42	454.34	-24.08
Trade and Development Bank	174.69	323.70	85.30
Baobab Securities	0.00	51.74	
Arab Bank for Economic Development in Africa	30.00	0.00	
Total Public External Debt Stock (1+2+3)	**3,598.45**	**3,944.50**	**9.62**

Source: MoFEA staff calculations.

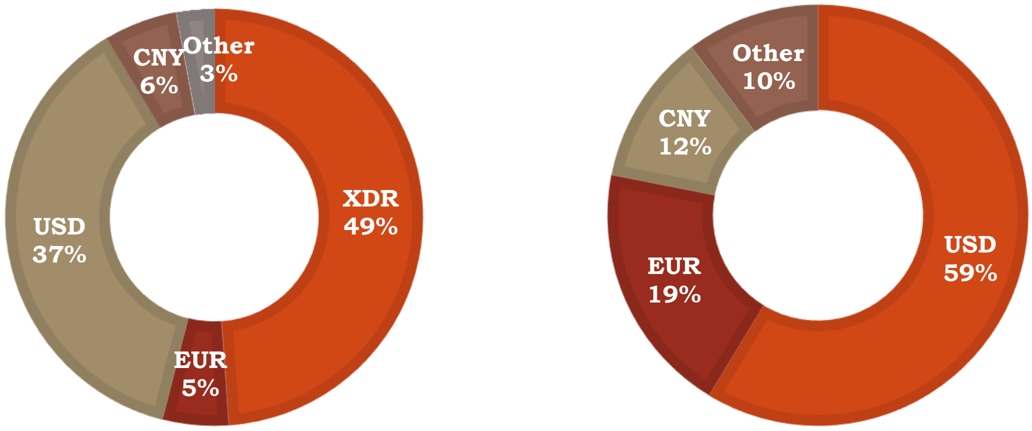
3.3 External Debt by Creditor Category

The external debt portfolio comprises multilateral, bilateral and commercial creditors. As shown in Table 7, multilateral creditors continue to account for the largest proportion of Malawi's external debt at 68 percent, followed by commercial creditors at 21 percent and bilateral creditors at 11 percent. Since end-March 2022, the total amount owed to multilateral creditors increased by 16 percent, commercial creditors increased by 3 percent and bilateral creditors fell by 10 percent.

3.4 External Public Debt by Currency

As at end-March 2023, Special Drawing Rights (SDR) accounted for 49 percent of the total external public debt. After decomposing the SDR basket into its tradable currencies,[8] the USD accounted for the largest proportion of external debt at 59 percent followed by the EUR and CNY at 19 percent and 12 percent, respectively. Other currencies accounted for the remaining 10 percent.[9]

Figure 7: External Debt Stock, by Currency as at end-March 2023



Source: MoFEA staff calculations.

Compared to end-March 2022, the share of SDR has increased from 48 percent to 49 percent. After decomposing the SDR basket into its tradable currencies, the share of currencies remained relatively stable, with USD increasing from 56 percent to 59 percent and Euro decreasing from 21 percent to 19 percent.

[8] USD (43.38%), EUR (29.31%), CNY (12.28%), JPY (7.59%) and GBP (7.44%).
[9] Other currencies in the external public debt include British Pound, Kuwait Dinar, Saudi Riyal, Japanese Yen and Dirham.

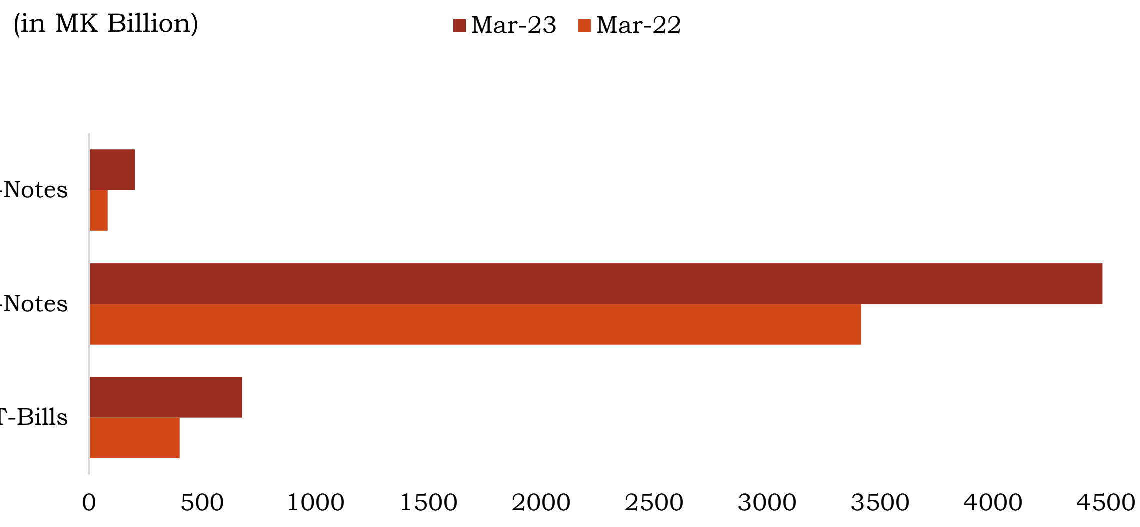
SECTION IV: DOMESTIC PUBLIC DEBT PORTFOLIO REVIEW

At end-March 2023, total domestic public debt amounted to MK5.36 trillion, up by 38 percent from MK3.90 trillion registered as at end-March 2022. The increase is due to the significantly high deficit financing and debt refinancing requirements during the period.

4.1 Domestic Debt by Instrument

Of the MK5.36 trillion domestic debt stock, MK4.48 trillion (84 percent) were T-Notes, MK676.39 billion (13 percent) T-Bills, and the remaining 4 percent were Promissory Notes. Holdings of all types of securities have increased since end-March 2022.

Figure 8: Domestic Debt Stock, by Instrument Type



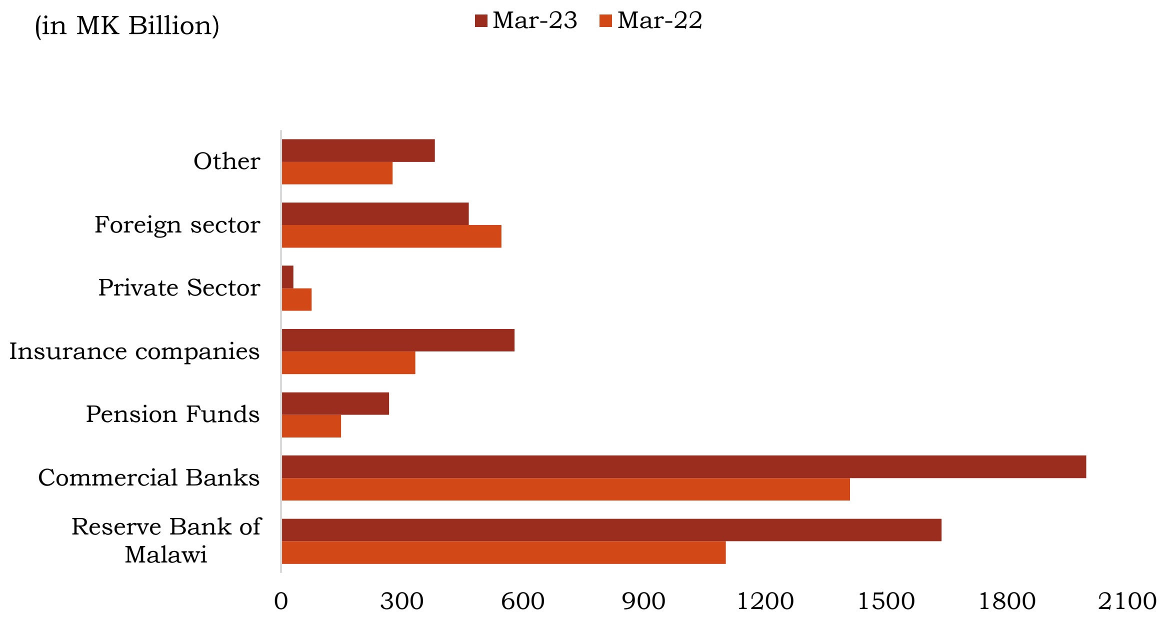
Source: MoFEA staff calculations.

4.2 Domestic Debt by Holder

In terms of holdings, commercial banks remained the biggest holders of domestic debt and held MK1,998.58 billion. They were followed by the RBM at MK1,638.74 billion. The insurance companies, foreign sector, pension funds and private sector held MK579.13 billion, MK465.60 billion, MK268.02 billion and MK30.49 billion, respectively. The rest of the holders, in aggregate, held MK381.97 billion.[10]

[10] other holders include other financial institutions, discount houses, Government/parastatals, corporate sector and households.

Figure 9: Domestic Debt Stock, by Holder



Source: MoFEA staff calculations.

SECTION V: RISK AND COST ANALYSIS

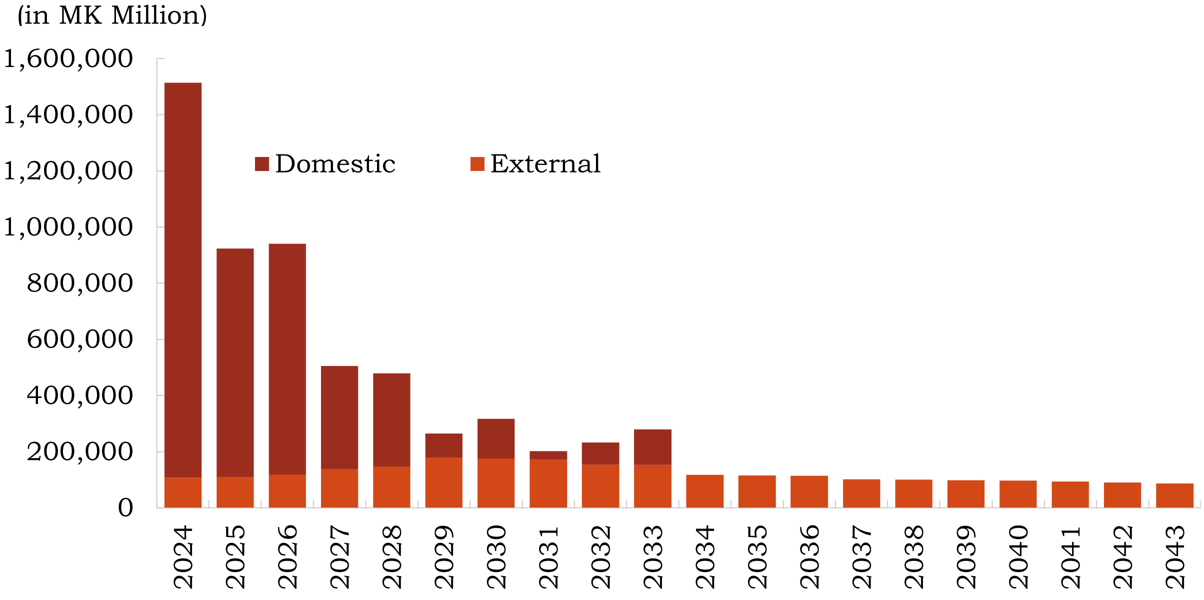
In this section, debt figures only cover Budgetary Central Government (BCG). Domestic debt is reported on a cost-value basis whilst external debt is maintained at disbursed outstanding debt basis.

In terms of risk, Malawi's public debt is exposed to significant refinancing, interest and exchange rate risks. The high refinancing (and/or roll-over) risk and interest rate risk are largely on account of the short-term nature of Malawi's domestic debt portfolio.

5.1 Refinancing Risk Analysis using Redemption Profile

The redemption profile captures the amount of debt that is falling due in a given period. This indicator shows the specific points of a country's debt vulnerability, which is manifested by high debt service payments in the debt repayment schedule. The profile shows that domestic debt is characterised by maturity spikes whilst external debt is smoother with maturities going as far as 2064 (not shown).

Figure 10: Malawi's Debt Redemption Profile, by FY



Source: MoFEA staff calculations.

5.2 Refinancing Risk Using Average Time Maturity

The Average Time to Maturity (ATM) of the debt portfolio indicates that the average holding needs to be repaid in 6.9 years. This is driven by a high proportion of domestic debt, which has original, and remaining maturity periods that are lower as compared to external debt. Specifically, the ATM for domestic debt is 2.4 years whilst external debt is 12.8 years. The ATM for domestic debt has gone down from 2.5 years recorded in March 2022 due to increasing issuances of shorter-term domestic debt whilst the ATM for external debt has gone down from 13.6 to 12.8 years reported in previous year due to the increase in external non-concessional debt (e.g. debt contracted from AFREXIM).

Table 8: Cost and Risk Indicators for Existing Debt (End-March 2023)

Risk Indicators		**External debt**	**Domestic debt**	**Total debt**
Amount (in millions of MK)		2,871,728.2	4,206,215.5	7,077,943.7
Amount (in millions of USD)		2,797.8	4,097.9	6,895.7
Nominal debt as percent of GDP		23.0	33.6	56.6
PV as percent of GDP		14.7	33.6	48.4
Cost of debt	Interest payment (% of GDP)	0.2	5.2	5.4
	Weighted Av. IR (%)	1.0	15.4	9.6
Refinancing risk	ATM (years)	12.8	2.4	6.9
	Debt maturing in 1yr (% of total)	3.4	33.5	20.6
	Debt maturing in 1yr (% of GDP)	0.9	11.3	12.1
Interest rate risk	ATR (years)	12.8	2.4	6.9
	Debt refixing in 1yr (% of total)	3.4	33.5	20.6
	Fixed rate debt incl T-bills (% of total)	100.0	100.0	100.0
FX risk	FX debt (% of total debt)			40.6
	ST FX debt (% of reserves)			48.9

Source: MoFEA staff calculations

5.3 Interest Rate Risk

With all of Malawi's debt being fixed interest rate debt, all interest charges are updated upon roll-over. Thus, the Average Time to Refixing (ATR) is the same as the ATM at 6.9 years.

5.4 Exchange Rate Risk

As for foreign exchange risk, 41 percent of the debt stock was denominated in foreign currency at the end of March 2023. This compared to 40 percent in March 2022. This proportion implies that a sizeable amount of Malawi's debt is susceptible to exchange rate movements. Exchange rate shocks, such as the 26 percent alignment of Kwacha in May 2022 (as shown in Figure 2), can substantially contribute to higher debt service payments in local currency terms, thereby leading to higher payments in the budget than projected.

SECTION VI: CONCLUSION AND WAY FORWARD

Public debt is at a worryingly high level, driven by increases in both external and domestic debt, resulting in high debt service and limited fiscal space, and putting a heavy strain on the public finances. At the same time, Malawi is in dire need of foreign exchange to import key commodities such as fuel. To address this situation, it will be key for Malawi to successfully restructure its debt, as this will allow it to ensure public debt is sustainable and debt service repayments are manageable. Furthermore, this will open up valuable sources of concessional financing and foreign exchange.

Annex 1: Newly signed loans

Table 9: Newly Signed Loans as at End-March 2023

Loan/Project Name	Creditor	Signed Date	Grace Period (Years)	Repayment Period (Years)	Interest Rate (%)	Commitment fee (%)	Original Amount (Million)	Grant Element (%)
Additional Financing for Eastern and Southern Higher Education Africa Centers of Excellency (ACE II)	IDA	1-Aug-22	6	32	0.75	0.5	XDR14.9	53
Additional Financing for Malawi Social Support for Resilient Livelihoods Project	IDA	1-Aug-22	6	32	0.75	0.5	XDR20.3	53
Second Additional Financing for the Malawi COVID-19 Emergency Response and Health Systems Preparedness Project	IDA	1-Aug-22	6	32	0.75	0.5	XDR18.9	53
Emergency Power Restoration Project (Kapichira)	IDA	1-Aug-22	6	32	0.75	0.5	XDR26.8	53
Additional Financing for LL Water and Sanitation Project	IDA	4-Apr-22	6	32	0.75	0.5	XDR8.5	53
SADC Sub-Regional Transport and Trade Facilitation Project (Benga-Nkhotakota- Dwangwa Road Project	OPEC Fund	6-Oct-22	5	15	1.25	0.5	USD20.0	29.4
Shire Valley Transformation Program - Phase 2	IDA	1-Aug-22	6	32	0.75	0.5	XDR99.7	53

Table 9: Newly Signed Loans as at End-March 2023 concluded

Loan/Project Name	Creditor	Signed Date	Grace Period (Years)	Repayment Period (Years)	Interest Rate (%)	Commitment fee (%)	Original Amount (Million)	Grant Element (%)
SADC Sub-Regional Transport and Trade Facilitation Project (Benga-Nkhotakota- Dwangwa Road Project	ADF	9-Dec-22	10	30	0.75	0.5	UA1.6	51
Malawi Agriculture Emergency Food Production Facility	ADF	3-Aug-22	10	30	0.75	0.5	UA15.0	51

Source: MoFEA staff compilations.

Annex 2: Loan Guarantees

Table 10: Loan Guarantees as at End-March 2023

Creditor	Beneficiary	Amount (millions)	Issue date	Status
NBS Bank Plc	Northern Region Water Board	MK12,600	7^{th} December 2021	Active
NBS Bank Plc	Agricultural Development and Marketing Corporation	MK25,000	27^{th} July 2021	Discharged
National Bank of Malawi		MK10,000	27^{th} July 2021	Active
MyBucks Banking Corporation		MK5,000	27^{th} July 2021	Active
CDH Investment Bank (CDHIB)		MK12,000	Nov-17	Partially discharged
Export Development Fund (EDF)		USD14.50	Jul-18	Active
CDHIB		MK22,200	1^{st} October 2020	Active
EDF	National Economic Empowerment Fund Limited	MK8,000	8^{th} March 2020	Active
FDH Bank		MK5,000	28^{th} June 2020	Active
CDHIB	Auction Holdings Limited	MK15,000	7^{th} December 2018	Active
CDHIB	Umodzi Holdings Limited	USD3.12	6^{th} December 2019	Active
NBS Bank Plc	Electricity Supply Corporation of Malawi	MK15,000	Feb-19	Active
FDH Bank		MK15,000	Feb-19	Replaced
CDHIB	Salima Sugar Company Limited	USD7.00	11^{th} March 2016	Discharged
		USD12.00	16^{th} April 2018	Active
		USD6.00	20^{th} October 2019	Active

Table 10: Loan Guarantees as at End-March 2023 concluded

Creditor	Beneficiary	Amount (millions)	Issue date	Status
EDF	National Economic	MK8,0000	8th March 2020	Active
FDH Bank	Empowerment Fund Limited	MK5,000	28th June 2020	Active
TDB	Malawi Leaf	USD83.3	1st November 2021	Active
Quay Energy Corp	Lake Malawi-Lilongwe City Water Supply Project	USD313.45	December 2021	Cancelled in February 2023
BADEA	National Oil Company of Malawi	USD50.00	24th October 2022	Active
AUZANO	Smallholder Farmers Fertiliser Revolving Fund of Malawi	USD170.00	13th September 2022	Cancelled in December 2022

Source: MoFEA staff compilations.