



REPUBLIC OF MALAWI

MINISTRY OF FINANCE

MID YEAR PUBLIC DEBT REPORT

FOR

2020/2021

FINANCIAL YEAR

MARCH 2021

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1. Introduction

This report provides an update on the status of public debt in Malawi as at end December 2020 and reviews recent economic developments in the country that can effect Malawi's future debt trajectory. Comparisons will be made with debt position recorded at end June 2020.

2. Macroeconomic and fiscal developments

Despite the COVID-19 pandemic and its attendant macro-economic impacts across the globe, the macroeconomic environment remained relatively stable in Malawi during the period under review. Inflation remained within single digits for most part of 2020 and registered at 7.6 percent for December 2020. The Malawi Kwacha depreciated against its major trading currencies, in particular the US Dollar by 5 percent in the period under review. This affected the Malawi Kwacha equivalent of external debt.

On the fiscal front however, Government had to contend with a number of challenges which have a bearing on public debt, including the high and rising primary deficit which was financed by domestic debt contracted at high interest rates. The high primary deficit is largely on account of underperformance in revenues, COVID-19 related expenditures, the expenditures on the newly launched Affordable Input Program, high statutory expenditures, including high public wage bill. Further, the Government has a substantial amount of arrears whose payment is underway.

These developments imply that public debt will rise over the short to medium run unless fiscal consolidation measures are undertaken and the spread of the Covid-19 pandemic is brought under control.

3. Total Public Debt Stock

As at end-December 2020, Total Public Debt (TPD) stock amounted to MK4.76 trillion or 54 percent of rebased Gross Domestic Product (GDP¹), up from MK4.13 trillion or 47 percent of rebased GDP, in June 2020. This translates into an increase of 15 percent or 7 percentage points of GDP between the two periods.

The end-December 2020 TPD stock comprised MK2.04 trillion² (23 percent of GDP) external debt and MK2.72 trillion³ (31 percent of GDP) domestic debt.

Table 1: Evolution of Public Debt (millions)

	2005	2006 (HIPC)	2018/19	2019/20	2020	
					JUNE	DECEMBER
Total Public Debt (MK)	426,592	130,846	3,058,238	3,669,238	4,127,736	4,756,824
External (USD)	2,969	452	2,132	2,190	2,388	2,641
Domestic (MK)	73,337	68,957	1,511,176	1,971,910	2,367,221	2,721,209
GDP⁴	326,957	430,522	7,727,897	8,517,596	8,815,340	8,815,340
Total Public Debt (% of GDP)	130	30	40	43	47	54

Source: Ministry of Finance

4. External Public Debt

As at end December 2020, at 83.87 percent (US\$2,214.78 million) of total external debt, multilateral creditors continued to account for the largest

¹ GDP was rebased in 2017

² Exchange rate used US\$1=MK 770.8367

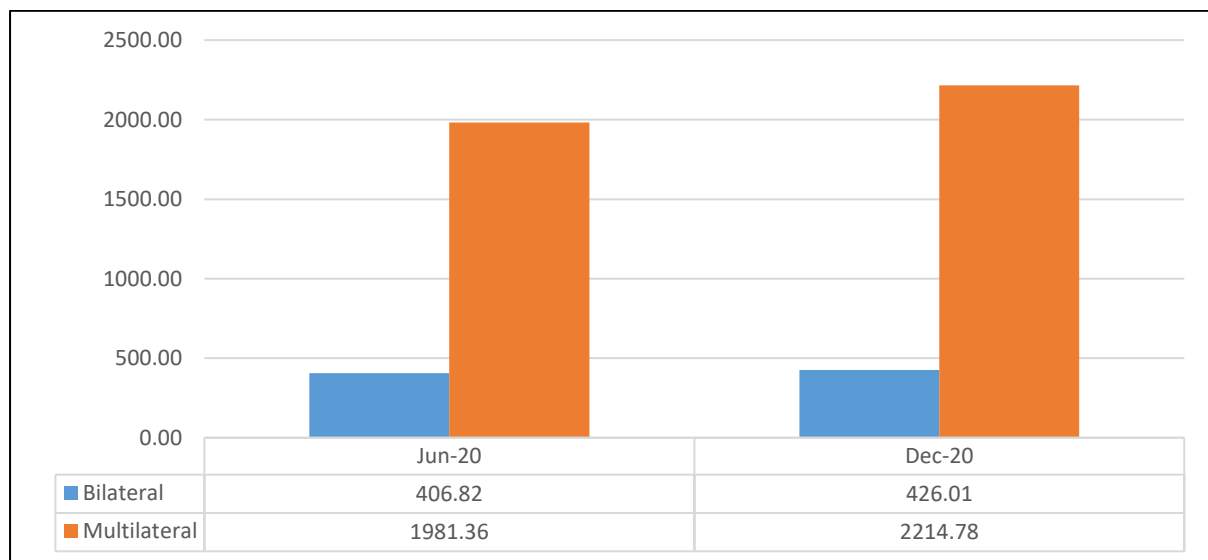
³ In terms of Cost Value (principal), domestic debt stock amounted to MK 2.32 trillion

⁴ Figures from 2018 are based on rebased GDP. For 2018/19 and 2019/20 figures are fiscalised whilst the 2020 figure is based on calendar year.

proportion of Malawi's external debt. This is compared with US\$1,981.36 million (82.97 percent of total external debt) reported in June 2020.

Bilateral creditors accounted for 16.13 percent of all external debt (US\$426.00 million). This is an increase from June 2020 position which was US\$406.82 million representing 17.03 percent of total external debt. As of end December 2020, Central Government owed no debt to commercial creditors.

Figure 1: External Debt by Creditor Type (USD millions)



Source: Ministry of Finance

The top five external creditors to Malawi are the World Bank, presented as the International Development Association (IDA) on position one; the International Monetary Fund (IMF) overtook the African Development Fund(ADF) to become the second biggest creditor; the People's Republic of China was forth and India was fifth.

Table 2: Total External Debt by Creditor (USD millions)

Creditor	Total Outstanding		% Change
	Jun-20	Dec-20	
International Development Association	1014.85	1104.25	0.09
International Monetary Fund	323.36	432.31	0.34
African Development Fund	364.37	396.40	0.09
Export-Import Bank of China (Main-Land)	197.07	218.97	0.11
Export Import Bank of India	139.35	135.97	-0.02
International Fund for Agricultural Development	85.30	88.88	0.04
OPEC Fund for International Development (OFID)	70.48	71.93	0.02
Arab Bank for Economic Development in Africa (BADEA)	60.38	59.85	-0.01
Kuwait Fund for Arab Economic Development	43.08	43.16	0.00
European Investment Bank	43.05	42.14	-0.02
Saudi Fund for Development	21.84	22.95	0.05
Nordic Development Fund	19.57	19.01	-0.03
Abu Dhabi Fund for Development	4.14	3.77	-0.09
Government of Belgium	1.34	1.20	-0.11
TOTAL	2388.18	2640.79	0.11

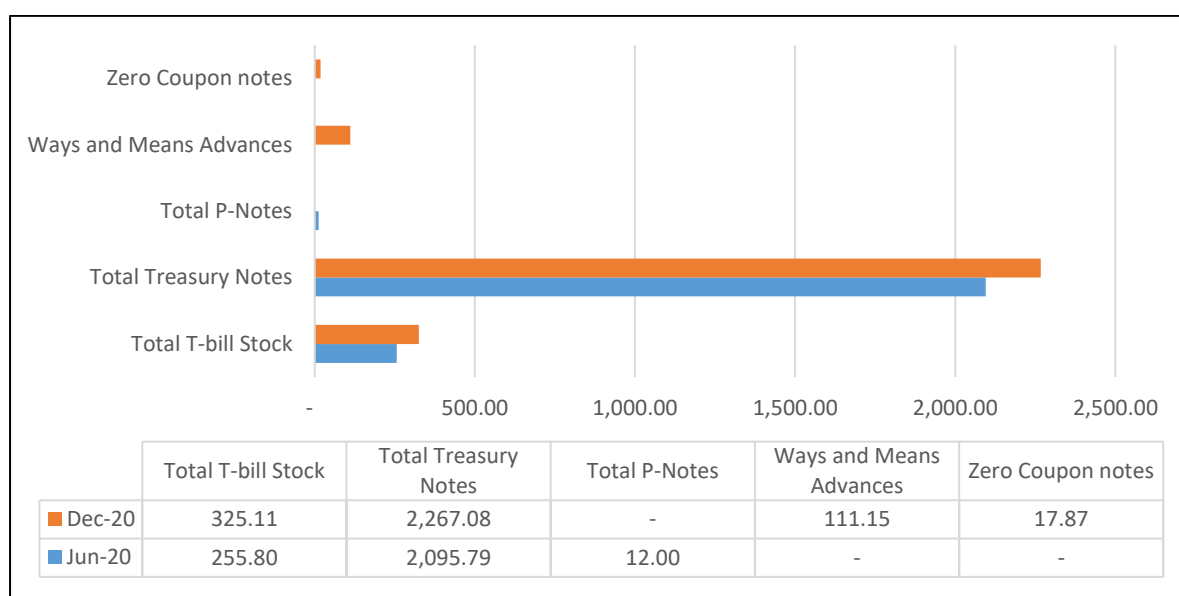
Source: Ministry of Finance

During the first six months of 2020/21FY, the increased external debt stock is mainly attributed to loan disbursements made to cushion the economy from the effects of COVID-19 pandemic. Notably, the IMF disbursed US\$101.96 million under the Rapid Credit Facility. In addition, the ADF provided US\$24.48 million as direct budget support. IDA disbursed US\$120.28 million under various projects. Likewise, EXIM Bank of China registered significant disbursement under the newly contracted loan –National Fibre Backbone Phase II.

5. Domestic Public Debt

As at end December 2020, out of the domestic debt stock of MK2.72 trillion, 83.31 percent were Treasury Notes. This was a reduction from 88.67 percent recorded in June 2020. Holdings of Treasury Bills went up from 10.82 percent in June 2020 to 11.95 percent in December 2020. The holdings of Ways and Means Advances from the RBM were 4.08 percent and Zero-Coupon Promissory Notes were at 0.66 percent.

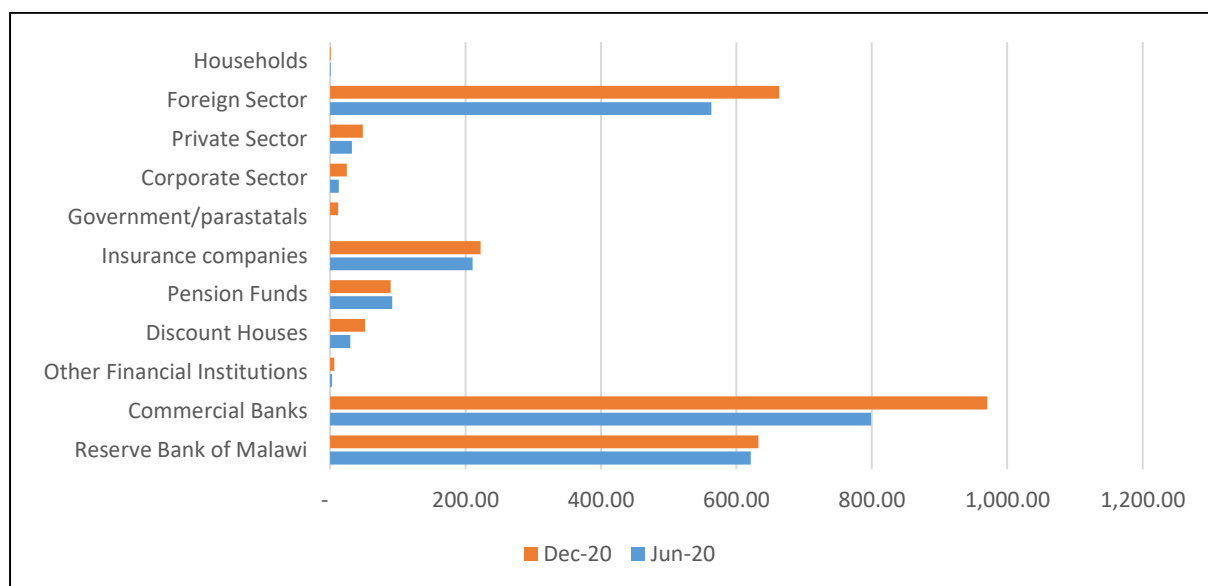
Figure 2: Domestic Debt by Instrument (MK billions)



Source: Ministry of Finance

In terms of domestic debt holders, commercial banks remained the biggest holders and increased their holdings of domestic debt securities from MK798.98 billion in June 2020 to MK970.25 billion in December 2020. They were followed by the Reserve Bank of Malawi which increased its holdings from MK621.30 billion to MK632.43 billion during the same period. The Foreign sector also increased its holdings. Worth noting is the increase of holdings by households albeit a small increase from MK0.93 billion to MK1.23 billion during the period under review.

Figure 3: Domestic Debt by Holder (MK billions)



Source: Ministry of Finance

6. External Debt Sustainability

Treasury is in the process of carrying out a Debt Sustainability Analysis (DSA). In the absence of such analysis, the report borrows from a similar analysis done jointly by the World Bank and IMF in the context of the September 2020 request for emergency financing under the IMF's Rapid Credit Facility. The results of the Joint Bank-Fund DSA shows that Malawi's external debt portfolio remains sustainable over the medium term with all sustainability indicators falling below recommended thresholds as presented in table 3 below. However, the country faces a moderate risk of external debt distress with limited space to absorb shocks as it is highly vulnerable to export related shocks. The capacity to absorb export-related shocks is expected to deteriorate further because of the slow export recovery in the wake of the COVID-19 pandemic. Considering domestic debt, however, the country faces a high risk of debt distress.

Table 3: External Debt Burden Indicators

Indicator	Threshold	2020	2021	2022	2023	2024	2025
PV of external debt (% of GDP)	40%	20.3%	21.9%	22.5%	22.7%	22.5%	22.3%
PV of external Debt (% of exports)	180%	152.2%	156.2%	152.1%	146.8%	139.7%	133.1%
Debt service (% of exports)	15%	6.8%	9.3%	10.9%	10.2%	10.0%	9.2%
Debt service (% of revenue)	18%	5.4%	7.1%	8.9%	8.1%	7.7%	7.1%

Source: Ministry of Finance calculations based on IMF data

7. Debt Management Developments during the first half of 2020/21FY

7.1 External debt

During the period under review, a total of eight concessional loans were contracted with a total commitment of US\$319.8 million. IDA, ADF, IFAD, OFID, EIB and EXIM China provided these loans mainly in support of Agriculture Sector, Water Sector, Information and Communication Technology Sector and in response to COVID-19 pandemic.

7.2 Domestic debt

7.2.1 Liquidity Management Operations

Government faced very large maturities in September 2020 amounting to around MK400 billion. This posed a significant liquidity challenge to Government. Active planning to address this issue started in 2019 through Liquidity Management Operations (LMOs). The first operation was the Bond Buy-Backs which was reported in the 2019/20 FY Annual Debt Report. Under this option, Government used resources amounting to MK30.7 billion and

bought back some securities that were maturing in September 2020. This operation was conducted in January 2020.

After this operation, the bulk of the LMOs were in form of Bond Switches which were carried out between August and September 2020. This operation involved two undertakings: (a) a premature dis-investment of old securities and (b) re-investment in new securities. Therefore, some securities which were due to mature in September 2020 were switched into new securities with different maturities into the future. In total, securities with a combined original Face Value of MK231.8 billion (and MK167.5 billion cost) were switched. Going forward, strategies to avoid accumulation of large maturities in particular years have been adopted in the development of domestic securities issuance calendars.

7.2.2 Domestic Arrears

In an effort to clear domestic supplier's arrears, during the period under review, Government instituted an audit and verification exercise of the arrears that have been accumulated by its Ministries, Departments and Agencies. Upon verification, Government will securitise the arrears using Zero Coupon Promissory Notes (ZCPNs). As of end December 2020, a total of MK17.87 billion in ZCPNs were issued in favour of ADMARC (MK12 billion) and National Bank of Malawi (MK5.87 billion). The latter was for some loan repayment arrears under the Lilongwe-Salima Water Project (a guaranteed loan contracted by Lilongwe Water Board).

8. Domestic Contingent Liabilities

As previously reported in the 2019/20FY Annual Public Debt report, Government's key contingent liabilities arise from explicit guarantees issued to State Owned Enterprises. In the first six months of the 2020/21FY, Government issued one-off guarantee to the tune of MK22.2 billion to ADMARC. The

purpose of the guarantee was to enable ADMARC purchase commercial crops for resale under its commercial function. The guarantee was in favour of CDH Investment Holdings and has a tenor of nine months. With this guarantee, the stock of Government Guaranteed Debt went up to MK175.9 billion representing 2.00 percent of GDP as of end December 2020 from the reported MK159.5 billion in June 2020⁵ or 1.81 percent of GDP.

⁵ There were repayments under the guarantees to the tune of MK5.87 billion

ANNEXURE: LOANS SIGNED BETWEEN JUNE 2020 AND DECEMBER 2020

LOAN	CREDITOR	SIGNING DATE	GRACE PERIOD (YEARS)	REPAYMENT PERIOD (YEARS)	INTEREST RATE/ANNU M	OTHER LOAN TERMS	LOAN AMOUNT IN MILLION (ORIGINAL CURRENCY)	EQUIV IN MILLION US\$	GRANT ELEMENT
Malawi Watershed Services Improvement Project	IDA	10-Dec-20	6	32	0.75	-	XDR 57.1	78.5	53
Financial Inclusion and Entrepreneurship Scaling Project	IDA	5-Nov-20	6	32	0.75	-	XDR 62.7	86	53
Covid-19 Response Support Programme	ADF	2-Nov-20	10	30	0.75	Commitment fee 0.5%	UA 17.9	22.68	51
Supplementary Financing for the Promoting Investment and Competitiveness in the Tourism Sector	ADF	2-Nov-20	10	30	0.75	Commitment fee 0.5%	UA 0.32	0.46	51
Sustainable Agriculture Production Programme	IFAD	11-Nov-20	10	30	0.75	-	XDR 7.3	10.1	58
Transforming Agriculture through Diversification and Entrepreneurship Programme	OFID	25-Nov-20	5	15	1	Service charge of 1%	USD 20	20	36
Additional Financing for Treatment Works III Project	EIB		5	20	1.45	-	Euro 2.5	3.03	36
Malawi National Fibre Backbone Phase II Project	EXIM	18-Aug-20	6.5	20	1	Management Fee 0.25% and Commitment fee 0.25%	CNY 693	99	35