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Country presentation

by

THE GOVERNMENT OF MALAWI

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COUNTRY REPORT

THIRD UNITED NATIONS CONFERENCE OF LEAST DEVELOPED COUNTRIES

BRUSSELS, 14-20 MAY 2001

PRESENTATION OF THE GOVERNMENT OF MALAWI

PROGRAMME OF ACTION FOR THE DEVELOPMENT OF MALAWI 2001-2010

February 2001

Note: This report has been prepared under the responsibility of the National Economic Council, after consultation with members of the National Preparatory Committee consisting of Ministry of Finance and Economic Planning, Ministry of Commerce and Industry, Ministry of Foreign Affairs and International Co-operation and the University of Malawi (Centre for Social Research and Agricultural Policy Research Unit) Technical Support was provided by the UNDP and the European Union.

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ACRONYMS

ACB	Anti-Corruption Bureau
ACP	African - Caribbean-Pacific
ADMARC	Agricultural Development and Marketing Corporation
AGOA	African Growth and Opportunities Act
AIDS	Acquired Immunodeficiency Syndrome
CEDAW	Convention on the Elimination of all forms of Discrimination Against Women (
CG	Consultative Group
CIF	Cost, freight and Insurance
COMESA	Common Market for Eastern and Southern Africa
CPI	Consumer Price Index
CES	Capacity Enhancement and Studies
EEC	European Economic Community
EPZ	Export Processing Zones
ESCOM	Electricity Supply Commission of Malawi
FDI	Foreign Direct Investment
GATT	General Agreement on Tariff and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
GSP	Generalised System of Preferences
GTZ	German Technical Cooperation
HIPIC	High Indebted Poor Countries
HIV	Human Immunodeficiency Virus
ILO	International Labour Organisation
IMF	International Monetary Fund
LDC	Less Developed Country
MACRA	Malawi Communications Regulatory Authority
MASAF	Malawi Social Action Fund
M & E	Monitoring and Evaluation
MCCI	Malawi Confederation of Chamber's of Commerce
MCI	Ministry of Commerce and Industry
MEPC	Malawi Export Promotion Council
MIPA	Malawi Investment Promotion Agency
MTEF	Medium Term Expenditure Framework
MOF	Ministry of Finance
MW	Megawatts
NEAP	National Environmental Action Plan
NECO	National Electricity Council of Malawi
NGO	Non-Governmental Organisations
NRA	National Roads Authority
OAU	Organisation of Africa Unity
ODA	Overseas Development Assistance
PAP	Poverty Alleviation Program
PMC	Project Management Committee
PMS	Poverty Monitoring Systems
PRSP	Poverty Reduction Strategy Program
PWP	Public Works Program
RBM	Reserve Bank of Malawi

SADC	Southern Africa Development Community
SAID	Southern Africa International Dialogue
SDR	Special Drawing Rights
SPI	Starter Pack Initiative
TEVET	Technical Entrepreneurship and Vocational Education Training
UFW	Unaccounted For Water
UNCTAD	United Nations Conference on Trade and Development
USA	United States of America
WTO	World Trade Organisation

EXECUTIVE SUMMARY

Introduction.

1. In the first 15 years after independence, Malawi's gross domestic product (GDP) grew at an average annual rate of nearly 6%. But the fruits of this growth were poorly distributed, and growth itself was narrowly based on estate owned agriculture, and large public and private conglomerates protected by pervasive barriers to entry. As a result, at the end of this period Malawi emerged with one of the worst sets of human welfare indicators in the World

2. In line with the UNCTAD Conference on the LDCs held in September 1990, which adopted the Paris Declaration and Program of Action for Least Developed Countries, Malawi, during the 1990s continued undertaking adjustment programs aimed at consolidating reforms that started in the previous decade. The government development policy was aimed at developing a market oriented and export-led growth strategy. In view of the negative per capita growth in the 80s, the government's objective in the 90s was to raise the rate of per capita income growth, to more than 0.6 per cent per annum

3. The new decade brings significant challenges because of the significant social, political and economic changes that have taken place during the last decade. These changes have increased the demand on the country's scarce resources. To meet these challenges, Malawi has developed its national shared vision, which articulates the people's aspirations by the year 2020 and is in the process of developing a Poverty Reduction Strategy, a short and medium term framework that will be used to attain the goals and objectives as stated in the Vision 2020.

Economic Performance

4. Developments on the political scene as well as climatic factors explain some of the macroeconomic developments during the 1990s. The period was characterised by episodes of drought, deterioration in the terms of trade and macroeconomic management slippage attributed to political transition period from one party state to plural politics during the first half of 1990s. The annual GDP growth rate for the period under review declined but on average the rate for the period was about 4 per cent per annum.

5. Economic growth in Malawi was attributed to episodes of strong agricultural performance, combined with booming economic activity in the distribution sector following the implementation of the economic liberalization program. However, during the years of drought the economy suffered from food shortages. In years with favourable weather climate such as during 1998/99 season, the economy had maize surplus in excess of 500,000 tonnes partly as a result of a starter pack initiative, which saw government distributing free seeds and fertilizer to smallholder farmers.

6. On the other hand, the manufacturing sector's performance in the 1990s, despite the government undertaking major reforms, was below expectations. The

heavily import dependent manufacturing sector was negatively affected by the depreciation of the Kwacha exchange rate, stiff competition brought about by the influx of cheap imports of manufactured goods, and structural weaknesses in the environment

7. The physical infrastructure which support economic and development activities was weak during the period. For example, Malawi experienced major operational inefficiencies, both in electricity generation and distribution in 1990s, resulting in frequent blackouts

8. On the social front, Malawi intensified its efforts to fight poverty. The new Government in 1994 adopted poverty alleviation as its central theme in the government development agenda. One of the highly successful Poverty Alleviation Program was the Malawi Social Action Fund

9. In terms of trade, Malawi's terms of trade deteriorated in the 1990s. It was also clear that the average shares of total trade (to GDP) in general, and of exports in particular did not change significantly in the 1990s. There was no marked difference between the 1980s and 1990s averages of the main trade aggregates. The share of trade in GDP was, however, significant and comparable to similar economies.

10 Malawi's competitive position was the lowest among SADC. This reflects the unfavourable economic environment for investment flows in the 1990s, at least relative to similar countries in the region. The stock of foreign direct investment in Malawi was small in magnitude but increased steadily. As a whole it seems to be comparable to the average for African countries

11. The prevalence of AIDS was a major development challenge during the decade. It was estimated that 15 percent of the age group 15-49 was affected by AIDS. Over 300,000 Malawians have already died. Life expectancy of economic productive population dropped during the period and was at the end of the decade at 38 years. At the end of the decade, 70% of hospital beds were occupied by people with HIV/AIDS and by 1998, 210,000 children under 15 years of age had lost their mothers to AIDS. Government, at the end of the decade, successfully developed a National Strategic Framework for HIV/AIDS 2000 – 2004

Factors that Facilitated or Constrained Development

Domestic Factors

12. Malawi enjoyed a relatively stable political environment during the first thirty years after independence under two systems of government: the one-party system of government (1964-1994) and the pluralistic multiparty system of government after the Presidential and Parliamentary General elections.

13. On the economic front, economic infrastructure form a key component in the enabling environment for sustainable development. However, the size of the Malawi market, the geographical dispersion and the landlockedness posed a particular challenge to meeting the needs of the private sector for high quality

infrastructure at the lowest possible cost. Telecommunications, energy, and logistics and transport are the areas of fundamental importance to private sector development. Faced with tight budgets, Government will need to explore more innovative ways of providing essential infrastructure services.

14. To ensure that the country minimises the areas constraining development, the Government undertook a number of policy reforms. The Government successfully intensified the smallholder growth strategy; introduced the Medium Term Expenditure Framework (MTEF); deepened the process of civil service reform; embarked on a privatisation program and established a sound institutional mechanism to manage the program; maintained its pro-poor stance in Government expenditure; and persisted with its emphasis on education. The government gave strong support to community led development initiatives and piloted public works programs as an alternative to untargeted hand-outs as a means of helping the very poor.

15. One of the major areas that constrained development was the weak financial sector. There was a sharp decline in the ratio of deposits to GDP and of credit to GDP at commercial banks. On the deposits side, financial savings were discouraged by high rates of inflation, which partly contributed to negative real interest rates. They were also constrained by low rates of growth of profits (and other incomes) and budget deficits. On the credit side, the demand for bank credit was adversely affected by an unfavourable economic environment of high budget deficits, large Government demands for bank credit, high rates of inflation, high nominal rates of interest and a depreciating currency, all of which must be contained. Private-sector demand for bank credit was also adversely affected by the poor investment environment.

16. Good governance is increasingly recognised as a prerequisite to economic growth and development. The introduction of multiparty democracy in 1994 brought in a constitution, which provided for people's participation in the formation of government, guarantees freedom of press, and ensures separation of powers. The constitution guarantees the protection of human rights for all citizens. Decentralization, a process involving transfer of responsibilities to district level adopted by Government will facilitate rapid development.

17. HIV/AIDS during the period took a terrible toll in Malawi although no reliable figures are available to substantiate the claim. Research revealed that incidence of HIV/AIDS among farmers and professionals was relatively high and the risky age group was 15-40 years, indicating the devastating effects of the epidemic on economic development. The HIV/AIDS epidemic was caused by continued high-risk sexual behaviour such as unprotected sex with multiple partners. There was a slow progress in changing the high-risk sexual behaviour.

18. Agriculture is the major contributor to economic growth in Malawi and it is a major source of employment in the country. The main sources of growth have been tobacco as a result of the specific heavy public investment in the form of research, extension, marketing services, and credit. Land scarcity during the decade became an issue because of the growing population. Nearly all cultivation

was rain-fed, making Malawi subject to periodic droughts and fluctuations in production levels

19. In addition, a number of factors held back increased productivity and diversification. These included Government pricing policies, world market policies, lack of interventions to create forward linkages with other industries in the value added chain, supply and demand constraints on the increased use of higher yielding varieties. The major constraints in the agricultural sector included the following:

- Inconsistencies between stated sectoral strategies and public expenditure
- Imbalances in capital and revenue expenditures
- Weak planning and implementation capacity
- Fragmentation and poor co-ordination of donor assistance
- Lack of forward linkages with other productive sectors;
- Dependence on rain-fed agriculture

20. Malawi's human development indicators trail below most regional countries. Improved access to health and education will be critical for long-term development in Malawi. In general, the major constraint facing the education sector was low access, particularly at secondary and tertiary levels

21. The environmental degradation played a major role in constraining development in the 1990s. Only 31 per cent of the total land area in Malawi was being utilized and suitable for cultivation, whilst 18 per cent of the cultivation was taking place on marginal or environmentally fragile land like steep slopes, riverbanks and valleys. The extension of cultivation to marginal areas, unsatisfactory land use practices, lack of appropriate conservation measures, deforestation and overgrazing led to a loss of agricultural land productivity, mainly through soil erosion and declining soil fertility. The rate of deforestation was estimated at 1.4 per cent per year due to dependence on agriculture, dependence on fuel-wood, high rate of population growth and excessive selling of wood to generate income. Deforestation resulted in depletion of surface water resources and in problems of siltation /sedimentation, reduced base flows and recurring drought conditions.

External Factors

22. There were also a number of external factors that facilitated or constrained development during the decade. Globally the increasing scarcity of fiscal resources was an important reason for the decline in net official development assistance during 1990s. Malawi also experienced reduced concentration of aid as evidenced by reduced concentration of ODA in GDP from 21 per cent in 1994/95 fiscal year to 11 per cent by 1996/97. In addition, donor flows were also erratic and were therefore part of the economic problem.

23. Nevertheless, aid helped to promote good economic policies by encouraging policy reforms and strengthening institutions. It was estimated that 80 per cent of government development expenditure was financed by external donors. Malawi also got balance of payments support throughout the reform

period which began in the late 1980s. However, these did not translate into improved living conditions for the ordinary citizen.

24. The outstanding debt for Malawi increased at a rapid rate from US\$ 1.23 billion in 1992 to US\$ 2.6 billion by 1999. As a proportion of GDP this represented an increase from 93.2 per cent in 1992 to 155.1 percent in 1998. Malawi is one of the most highly indebted countries in Africa. Following the Consultative Group meeting in May, 2000 and subsequent IMF/World Bank reviews, Malawi is likely to benefit from debt reduction through the HIPC Initiative. A decision point is was reached by December 2000 According to estimates the assistance under the HIPC Initiative could translate into an annual debt service reduction of around \$40 to \$50 million over the 2000 to 2020 period, equivalent to around 1.3 percent of GDP for the 2000-09 period and 0.7 percent of GDP for the 2010-20 period.

25. The summary of Malawi's performance substantiates many observers' analysis of Malawi's economy as being very fragile, narrow base and lacking in key social services and infrastructure. It is an economy that is vulnerable to various shocks. Malawi experiences shocks that could be categorised into three main areas. These are natural, economic and external shocks. These shocks had a negative impact on the ability of the country to attain sustainable economic growth.

26. The consequence of the shocks were strongly felt during the decade. Economic performance deteriorated rapidly during the first half of 1990s. In 1994, GDP contracted by more than 10 per cent. Drought caused the country's staple food, maize production levels to fall leading to a significant shortfall in government revenue and a large increase in expenditure for emergency food imports and related social services.

Program of Action 2000-2010

27. As Malawi looks at the Program for Action in the new decade, the challenge is for the country to reverse the present state of decline. There is enormous potential and great results can be achieved through proper utilization of the resources of water, land and people. The results will be dependant on the implementation of Vision 2020. The shared vision for Malawi as captured in the Vision 2020 document is as follows:

“By the year 2020, Malawi as a God-fearing nation will be secure, democratically mature, environmentally sustainable, self-reliant with equal opportunities for, and active participation by, all having social services, vibrant cultural and religious values and being technologically driven middle-income country”

28. Malawi should therefore rally around a common mission, which should have the following objective:

“To attain a balanced, broad-based and sustainable development through economic growth, development, efficient utilisation of the human capital,

development of economic infrastructure observance of good governance and protection of the environment and natural resources”.

29. This common mission entails that the Malawi economy must be fast-growing, competitive, innovative and knowledge-based. The major efforts in the plan period will be to eradicate hard-core poverty and transform the country into a middle-income country with a desired per capita income of at least US\$500 by the year 2010

30. To achieve a prosperous future, Malawi needs to concentrate on key themes and cornerstones

- Project a positive image of the country in such a manner that everyone in the country must have a stake in the economic success. The benefits will have to be fairly shared. There will be need for lasting partnerships in the drive to achieve common goals and social cohesion.
- Strengthen the culture of enterprise to unleash the potential of the private sector as wealth creators. Government's role in the industry would be restricted to encouraging self-reliance and exposure to the disciplines of the market.
- Re-orient the business and the society to be more outward looking in the wake of regional integration and globalisation initiatives. There will be need to learn from the best worldwide.
- Prepare all stakeholders for the applied knowledge-based economy of the future with better health and education; higher skills; commitment to research and development and innovation.
- Recognise that self-help and self-reliance are key to achieving success.
- Improve the quality of trained manpower and its utilisation.
- Improve the quality of economic infrastructure.
- Achieve macro-economic stability and growth.
- Ensure sound governance and shared responsibilities.

31. These themes will revolve around four major strategic issues which include:

- **Equality and Social Cohesion:** Total commitment by the public and private sectors to build an economy based on the principles of equality of opportunity and social inclusion.
- **Applied Knowledge-based:** There will be need for greater integration of economic activities and educational policy and more collaboration

between business and the education and training systems in delivering the skills and capabilities needed by business.

- **Enterprise and Outward-looking:** Enterprise development will involve raising the prestige of business as a career and providing role models to attract our best talent into the wealth-creating sectors.
- **Self-reliance and Self-help :** Self-reliance and self-help will guide by the principle of achieving more with the available resources. Malawi will have to take control of its own destiny through the creation of new mechanisms for partnership between the private and public sectors in pursuing our economic goals.

32. Finally, Malawi needs to institute pragmatic and flexible economic strategies, more especially by improving resource mobilisation, increasing efficiency in its utilisation to raise productivity and enhancing technology development with the major sectors of the economy. Sustained long-term development will be achieved through increased agricultural productivity, deepened and widened industrial base and a developed services sector. Partnership and consultation will underpin the successful implementation of the strategies because it will ensure consensus on the direction of the strategy and an acceptance by all involved in its delivery. The roles of the various stakeholders in the delivery will have to be clearly defined to avoid duplication and wasteful competition.

1.0 INTRODUCTION

(i) In the first 15 years after independence in 1964, Malawi's gross domestic product (GDP) grew at an average annual rate of nearly 6%. But the fruits of this growth were poorly distributed¹, and growth itself was narrowly based on estate owned agriculture, and large public and private conglomerates protected by pervasive barriers to entry. As a result, at the end of this period Malawi emerged with one of the worst sets of human welfare indicators in the World [See **Table 1.1**].

(ii) Malawi, in the late 1970s, suffered from a series of exogenous shocks that disrupted even the pattern of growth. These included high import costs due to disruptions in trade routes, oil price shocks, influx of refugees from Mozambique and droughts –In response to these disruptions, Malawi in 1981 started implementing policy reforms supported by the World Bank and International Monetary Fund (IMF) through successive adjustment credits, to stabilise and restructure the economy. The policy reforms were mainly aimed at stabilising the economy, liberalising international trade, investment licensing and financial markets. However, the reforms neglected important structural regulatory constraints and entry barriers in product and factor markets. The results were poor, and the growth rate of GDP during the 1981-1994 periods was 2.4% per annum, well below the annual population growth rate of 3%. Malawi's per capita income was on average declining at -1.0% per annum during the 1980s.

(iii) In line with the UNCTAD Conference on the LDCs held in September 1990, which adopted the Paris Declaration and Program of Action for Least Developed Countries, Malawi, during the 1990s continued undertaking adjustment programs aimed at consolidating reforms that started in the previous decade. The government development policy aimed at developing a market-oriented and export-led growth strategy. The challenge was to change the duality in the agriculture sector whereby the estate enclave fared better largely as a result of the exploitation of the smallholder sub-sector. It was hoped that, in the medium term, non-traditional traded exports in both the agro-based industries and manufacturing sectors would be encouraged and promoted.

(iv) In view of the negative per capita growth in the 1980s, the government's objective in the 1990s was to raise the rate of per capita income growth, to more than 0.6% per annum. This was to be achieved partly by restoring fiscal discipline consistent with the balance of payments target and reducing the annual rate of inflation from above 20% to below 10% in the 1990s. The performance and results of the 1990s were mixed and this is articulated in the next two chapters. Whereas in some years there was significant growth, its impact on poverty reduction and income distribution was minimal.

(v). The new decade brings significant challenges because of the significant social, political and economic changes that have taken place during the last decade. These changes have increased the demand on the country's scarce

¹ Malawi's Gini income coefficient of 0.63 makes its income distribution among the worst in the world.

resources. The country will need to attain consistently very high growth rates if there is to be a significant dent on poverty. The World Bank (1997) came up with two alternative GDP growth scenarios for the period 1997 to 2006, corresponding to a base case of 4 per cent annual growth rate and a high case of 6 per cent growth rate. A third scenario of a low 3% average annual growth rate is entirely possible in case there is a low rate of growth in the agricultural sector as was the case in the past. The base case corresponds to the "macro-economically sustainable growth rate", in other words, it is the maximum rate at which the economy can grow without overheating. The high case corresponds to the "poverty-reducing growth rate" or the minimum rate at which per capita GDP growth would permit reduction in poverty.

(vi) To meet these challenges, Malawi has developed its national shared vision, which articulates the people's aspirations by the year 2020. Vision 2020 and the other policy initiatives and analysis undertaken during the past years will be consolidated into a Poverty Reduction Strategy Program (PSRP). The PSRP will be the main short and medium term framework that will be used to attain the goals and objectives as stated in the Vision 2020.

2.0 OVERALL ECONOMIC PERFORMANCE IN 1990s

1. The Malawi economy is agriculture-based and it is almost entirely reliant on favourable climatic conditions for good agricultural production and therefore economic growth. Agriculture accounts for more than one-third of GDP and over 90% of export earnings. The sector employs nearly half of those in formal employment, and directly and indirectly supports an estimated 85% of the population. The country's staple crop is maize, while tobacco is by far Malawi's largest export crop, followed by tea, sugar and cotton. Tobacco is also Malawi's most important cash crop export earner, normally accounting for around 70% of agricultural export earnings, and about half of all exports.

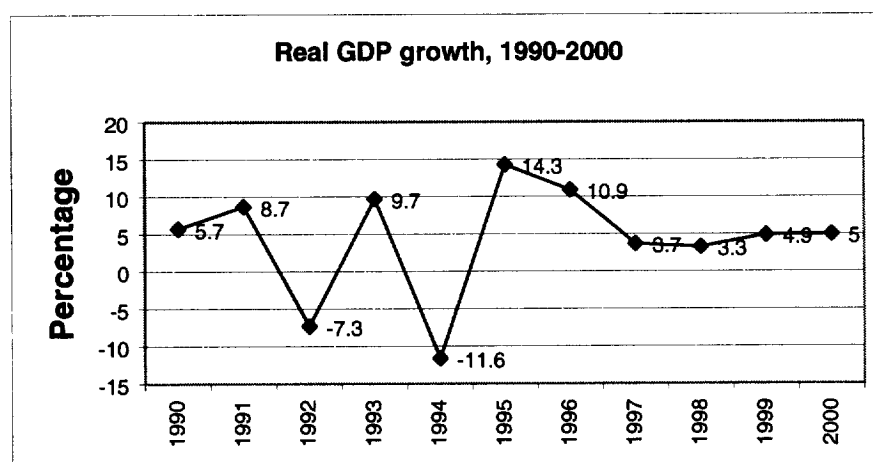
2. Malawi is grouped amongst the 10 least developed countries in the world, seventh from the bottom. The overriding problems include severe poverty, low export diversification, and slow growth, and heavy dependence on donor assistance. Despite concerted attempts at structural reform programs during the last decade, success was elusive due to internal and external factors, including inconsistent implementation of necessary and critical reforms. The general pattern was that periods of macroeconomic instability were followed by recovery periods. The major weakness was inability of the economic management to sustain macroeconomic stability at a level that generated confidence and credibility.

Macroeconomic Performance Overview, 1990- 1999

3. Developments on the political scene as well as climatic factors explain some of the macroeconomic developments during the period. The period was characterised by episodes of drought, deterioration in the terms of trade and macroeconomic management slippage attributed to political transition period from one party state to plural politics during the first half of 1990s. The performance is reflected in **Table 2.1**²

Review of GDP Growth

Fig 2.1



² See table in annex

4. The annual GDP growth rate for the period under review declined but on average the rate for the period was about 4 per cent per annum. This growth can be attributed to episodes of strong agricultural performance, combined with booming economic activity in the distribution sector following the implementation of the economic liberalization programme.

5. After an impressive 8.7 per cent growth in 1991, the economy registered a negative growth of 7.3 per cent in 1992, then posted a recovery growth of 9.7 percent in 1993 but declined again by 11.6 per cent in 1994 following serious industrial action, fiscal slippage caused by large drought related expenditures and suspension of aid flows due to concerns about governance. This period was characterized by large balance of payments and fiscal budget deficits, high inflation and economic stagnation.

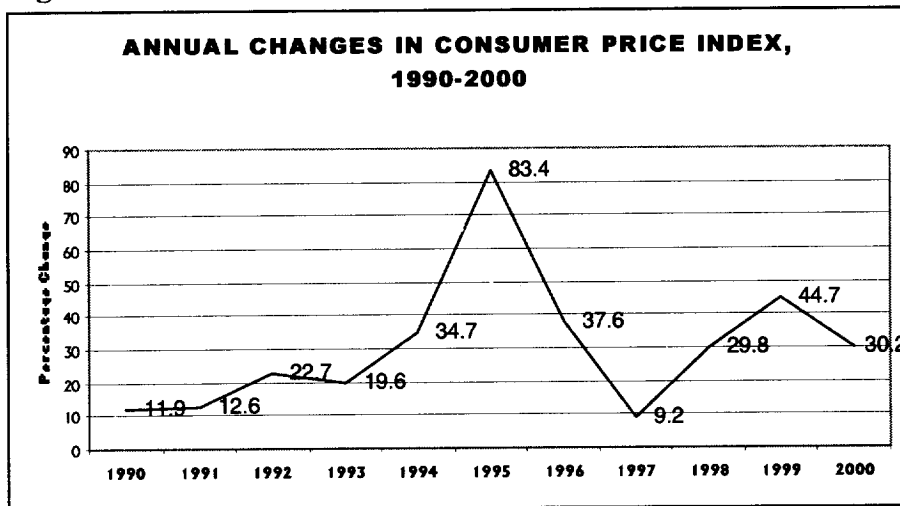
6. After the huge decline in 1994, there was a contrasting economic recovery in 1995. Real GDP increased by 14.3 per cent on account of favorable weather conditions that fostered tremendous recovery of small-scale agriculture (15.4 per cent growth). Continued favorable weather conditions sustained economic activity in 1996 and small-holder agriculture continued to enjoy strong growth (25.8 per cent). In addition to good weather, the effects of agricultural liberalization program, in which small-scale farmers were allowed to grow burley tobacco, boosted the small scale sub-sector production. Further to the expanded tobacco production, there were also increases in smallholder production of other crops like rice, pulses and other crops. In 1996, Government consolidated its macroeconomic programs. As a result, the overall fiscal deficit (excluding grants) declined from 16.2% of GDP in 1994 to 8.7% in 1996/97. Inflation declined from 83% in 1995 to under 9% at end 1996, while reserve cover increased to equivalent of 5.7 months of imports of goods and non factor services. At the same time, real GDP grew by 10.9 percent, led by high agricultural growth, which was aided by favorable rainfall in 1995-96 and the liberalization of production and marketing arrangements in the sector.

7. The economy recorded 3.7% growth in 1997. The growth rate then slowed to 3.3 percent in 1998, and 4.2% in 1999. Several factors explain the slow pace. Firstly, the smallholder sub-sector experienced drought in 1996/97 growing season, and the effect was compounded by high input cost, especially fertilizer following the removal of subsidies. In 1998, the economic slow down was a reflection of macroeconomic imbalances; there was a huge devaluation in 1998 which set in motion inflationary pressures and resulted in reduced real economic activity. Although macroeconomic indicators remained relatively stable in 1999, the characteristic of indicators in tenure (high inflation rates and interest rates) influenced the economic outcome for 1999.

Inflation

8. In general, the annual inflation rate as indicated by the Consumer price index (CPI) remained relatively high during the period. From 11.9 per cent in 1990, the inflation rate, mainly due to fiscal slippages and external shocks, went up to 34.7 per cent in 1994, and 83.4 per cent in 1995. Prudent fiscal policies introduced in 1995 tamed inflation to 37.6 per cent in 1996 and to 9.2 per cent in 1997. However, by the end of 1997, fiscal prudence slackened as the budget deficit widened and money supply growth increased. Consequently inflation rate also increased.

Fig 2.2



The depreciation of the Kwacha in August 1998 led to a cost push inflationary pressure resulting to annual average inflation rates of 29.8% and 44.7% in 1998 and 1999 respectively.

Nominal Exchange rate

9. Prior to 1994, the Kwacha was fixed to a basket of other currencies of Malawi's major trading partners. This arrangement was found to be inappropriate in the context of the economic liberalization programme and the heavy import dependency for the economy because the Kwacha was persistently under pressure and undermined the economy's competitiveness.

10. The Kwacha was floated in February 1994 in a bid to improve the economic situation. By the end of 1994, the Kwacha had depreciated by 96.7% against the US dollar. Following this huge depreciation, the Kwacha showed signs of stabilization for the most part of 1995 and 1996, with the average nominal official exchange rate reported at K15.3 to the US dollar. There was a slight depreciation during the last quarter of 1997, as a result the annual rate for 1997 left the kwacha at K16.4 per US dollar.

11. By the end of 1997, there were already symptoms of inflationary pressure which implied that the on-going exchange rate was overvalued. By August 1998, the Kwacha depreciated and the official rate went up to K31.1, and later to

K43.00 to the US dollar. Despite increased capital inflows on account of balance of payments support, the exchange rate pass-through continued to nourish inflation throughout 1999. By the end of December 1999, the nominal value of Malawi Kwacha against the US dollar was at K46.60. In terms of the real exchange rate, following the floatation of the Kwacha in February 1994, the real exchange rate was depreciated sharply in 1994, but when the Kwacha was pegged at K15.3 to the US dollar in 1995, it appreciated strongly until late 1997 when it gave way to the overwhelming pressure of foreign exchange reserves. The Reserve Bank of Malawi has an active real exchange rate management policy. It has been established that the real exchange rate is susceptible to terms of trade, increased openness to trade and timing of donor inflows.

Sectoral Growth Performance

Food and Agriculture

12. Despite a general declining trend in growth rate for the sector, the agricultural sector remained the main source of economic growth during the period under review. After a sharp decline in 1992 and 1994, the sector registered an impressive comeback in 1993 and 1995 with a 53.4% and 39.6% nominal growth, respectively. This was attributed mainly to relatively good climatic conditions during 1992/93 and 1994/95 crop seasons. The growth in the economy in 1997 and 1998 was a result of good agriculture performance. In 1997, growth was driven primarily by a good performance in the large-scale sector. In 1998, growth was strongly related to the recovery in the smallholder agricultural sub-sector. During the years of drought the economy experienced food shortages. However, during 1998/99, the economy had a maize surplus in excess of 500,000 tonnes partly as a result of a starter pack initiative, which saw government distributing free seeds and fertilizer to smallholder farmers.

13. During the period, the government rationalised the annual increases in smallholder producer prices; removed fertiliser subsidies; reduced the role of the state marketing board the Agricultural Development and Marketing Corporation (ADMARC), in favour of private competition in marketing of inputs and outputs; and smallholder farmers were allowed to grow burley tobacco. The supporting macroeconomic policies stressed the control of inflation so as to shift the rural-urban terms of trade in favour of agriculture and the role of exchange-rate liberalization to remove the implicit tax on agricultural exports.

14. The performance of the food sector, however, was generally unsatisfactory with no increase in yields of most food crops. This increased the risks of food insecurity and necessitated maize imports in some years using up scarce foreign exchange. The yields of the main cash crops grown by smallholder farmers did not increase either. For example, the average yield of fire-cured tobacco which, was 389 kg per hectare between 1970 and 1980, declined to 337 kg per hectare between 1981 and 1994. The corresponding average yields for sun-air cured tobacco were 364 kg and 287 kg per hectare in 1981 and 1984 respectively. The removal of restrictions on the cultivation of burley tobacco by smallholders led to a marked increase in production in the smallholder sub-sector. However, total

production of burley tobacco declined owing to a reduction in production on estates caused by higher input costs and rising insecurity in rural areas.

15. The growth of the smallholder agricultural sector during the period was generally erratic. This dismal performance could be attributed to adjustment policies as well as unfavourable weather conditions and the terms of trade. Unfortunately the adjustment policies prior to and during the 1990s seem to have addressed price constraint but not such non-price constraints as infrastructure and risk. Nor did they adequately address such problems as inadequate producer incentives, unfavourable internal terms of trade and inadequate credit and extension services. One of the major interventions that will be required in the sector will be the introduction of policies and programs that would increase productivity in the food sector. Improvements will also be required in rural infrastructure and feeder roads, (to allow private sector involvement in marketing inputs and outputs) extension services, and increase in credit and producer prices.

Industry

16. The manufacturing sector's performance in the 1990s was below expectations. The sector's growth rate was -0.6 percent in 1996 compared to 5.5% in 1995 and then by 1.0 % in 1997 and 0.5% in 1998. The sector registered a negative growth of -0.6 per cent in 1999. The heavily import dependent manufacturing sector was negatively affected by the depreciation of the Kwacha exchange rate resulting in under utilization owing to reduced importation of inputs and spare parts. Additionally, stiff competition brought about by the influx of cheap imports of manufactured goods, particularly textiles and clothes severely affected the domestic manufacturing companies.

17. The government undertook major reforms in the 1990s. For example, government eliminated the authority to grant exclusive product rights, revised the duty drawback system and reduced the scope of industrial licensing requirements. In addition, Malawi Investment Promotion Agency (MIPA) was established, the process for registration and incorporation of companies was simplified, the industrial licensing process was eliminated (except for a short list), and it instituted an Export Processing Zones (EPZs) regime.

18. Although these policy measures did not result into significant expansion in manufacturing, there was some notable diversification of exports. According to a World Bank study (World Bank 1997), about 16% of exports in 1996 were from manufacturing, compared to less than 8% in 1991. In addition, the study found that export-orientation of the manufacturing sector – the proportion of output that is exported – also increased significantly. Export oriented textiles and clothing manufacturing sub-sectors employed close to 12,000 labourers making it the largest employer in the Malawi manufacturing sector.

19. Despite traces of diversification, the industrial sector performed dismally. For example, between 1981 and 1996, manufacturing value-added increased at an average annual rate of 3.9 per cent, while prior to these reforms (1971-80), it grew at a much higher average annual rate of 13.6 per cent. As a result, the share of manufacturing in GDP remained stagnant at 14 percent since 1980. In addition,

its share in total formal sector employment also remained stagnant at about 14.0 per cent. Measured by the index of production, total manufactured output was low in 1999 compared to 1991, so was the index for the sub-sectors of export goods, intermediate goods and consumer goods (except food and beverages).

20. The unsatisfactory rate of growth of manufacturing industries was due to many factors. This included foreign competition, unreliable utilities, high cost of imported inputs induced by devaluation, foreign exchange shortages, unsatisfactory state of the internal road network, an unstable economic environment, decreasing rates of investment and inadequate delivery of credit to small- and medium-scale enterprises. Greater efficiency in import substitution was not achieved either. This was due to lack of competition as most industries were dominated by monopolies and oligopolies; excessive regulation of the economy; and price controls which were retained on some products after the authorities had started to dismantle price controls.

Utilities

21. In general, growth of the the utilities sector was resilient due to increased demand attributed to demographic factors. For example growth in demand for electricity resulted from increased activities in population growth, particularly new connections associated with rapid urbanisation. However, Malawi experienced major operational inefficiencies, both in electricity generation and distribution in 1990s, resulting in frequent blackouts. Silting was the main cause of failure in electricity generation and inadequate maintenance of the system caused failures in distribution. On the demand side, most enterprises faced high installation costs. This limited the access to electricity. Whereas private participation in the provision of electricity might increase efficiency, there is an urgent need to improve management of the existing supplier, ESCOM.

22. Urban water supplies in the 1990s were somewhat inadequate for industries that require vast amounts of water. Conscious of the adverse effects of these problems, government during the period decentralised the tapping and distribution of water by establishing commercially oriented regional water boards. It is too early to assess the impact of these boards, but it is hoped that eventually they will be able to meet the growing demand for water.

Social sector

Poverty Alleviation

23. It is estimated that 65.3% of the population in Malawi are below the poverty line. Since 1994, poverty alleviation was the central theme of the government development agenda. The government initiated several programs and projects under the Poverty Alleviation Program (PAP). The PAP is based on several-poverty related policies relating to sustainable livelihood; food security and nutrition; population issues; gender concerns, and actions for survival, protection and development of children. The most significant PAP activities recently implemented in Malawi include the Malawi Social Action Fund (Phase I and II), is described in chapter 3); Safety net programs covering the Starter Pack Initiative (SPI) and nutrition distribution programs; and; the establishment of the Poverty Alleviation Trust Fund. The Poverty Alleviation Trust Fund gave support to various institutions, which looked after disadvantaged groups in society.

24. The 1998 population census results showed that the population growth rate had declined to 1.9%. Nevertheless despite the reported slowdown in population at an estimated 10.36 million in 1999, the population is still large relative to available resources. Such a large population places other demands on Government to provide primary services in health and education. The introduction of free primary education in 1994 saw almost a doubling in enrolment rates. However over-time, the retention rate has been low. Nevertheless, there was an improvement in adult literacy rates. The prevalence of AIDS was and continues, to be a major development challenge since the age group 15-49 which is expected to be the most productive is the most vulnerable to AIDS in Malawi. It was estimated that 16.5% of this age group was affected by AIDS. An estimated 25% of the urban population, 21% of semi-urban dwellers and 11.2% of rural dweller are infected bringing the total number of those infected to approximately 1 million people. Over 300,000 Malawians have already died. Life expectancy of economic productive population dropped during the period and was at the end of the decade at 38 years. During this period 70% of hospital beds were occupied by people with HIV/AIDS and by 1998, 210,000 children under 15 years of age had lost their mothers to AIDS. Government, at the end of the decade, successfully developed a National Strategic Framework for HIV/AIDS 2000 – 2004 Implementation Plan and the Technical Co-operation Program. Government estimated that it would require US\$121.5 million to fund the various activities identified. During a Roundtable Conference on HIV/AIDS donors pledged close to US\$110 million.

Micro-Economic Situation

25. A SADC study (1997) on productivity found that regionally labour productivity increased by an average of 1.3% per year (between 1991-1995) for all SADC countries but it actually showed an annual decline (-1.75%) for Malawi. The widespread poverty is also reflected by high level of unequal income distribution. In 1998, the estimated Gini-income coefficient was 0.88, worsening from 0.64 estimated in 1994.. The preliminary results of the integrated household survey conducted in 1997 showed that 65.3% of the population lives below the

poverty line while 54.8% of the households leave below the poverty line. The prevalence of ultra-poverty at national level was estimated at 27.8 per cent of the population.

External Trade: Trends, Composition and Linkages

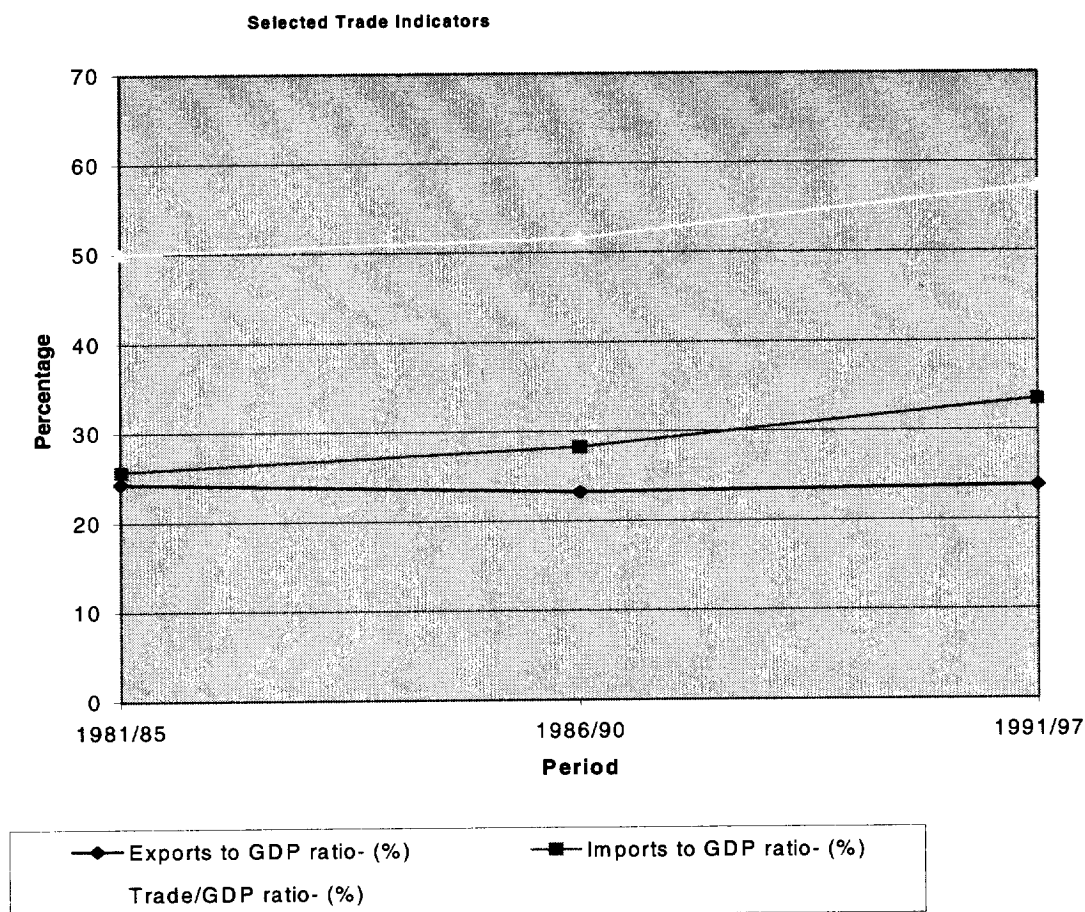
26. In the 1990s, there was an increased degree of economic co-operation, including regional integration. The trend of globalisation became more pronounced. Malawi's ability to integrate into the global economy can be assessed by looking at developments in international trade and its composition. From Fig 2.3, it is clear that the average shares of total trade to GDP in general, and of exports in particular did not change significantly in the 1990s. There was no marked difference between the 1980s and 1990s averages of the main trade aggregates. For instance, exports averaged between 23.0 and 24.0 per cent of GDP while imports ranged between 25 per cent and 33 per cent of GDP. The share of trade in GDP was, however, significant and comparable to similar economies, averaging about 53 per cent of GDP between 1981 and 1997.

27. Both exports and imports suffered a decline between 1991 and 1993 after having grown substantially in 1990/91. Fig 2.4 indicates that growth of both exports and imports was unstable in the later part of the 1990s and this was particularly true of exports and imports particularly, for Sub-Saharan Africa.

28. Malawi imports mainly industrial goods, that is, manufactured goods with a share of over 70% and exports mainly agriculture crops. The bulk of Malawi's exports (more than 85%) were agricultural items (see **Table 2.3**). The relative share of commodities in both exports and imports was, to a large extent, stable during the 80s and 90s. One could argue that the country was not successful in diversifying its export base. The only exception seems to be the relative increase of tobacco (which already accounts for over 50% of total exports) and a decrease in groundnuts in the share of exports in more recent years.

29. A similar picture emerges when further analysis is undertaken on a number of goods exported. As indicated in **Table 2.4**, both, the number of goods exported and the diversification index remained the same in 1994 as 1980, with a slight increase in 1995. And the concentration index increased in 1992 and 1994 compared to 1980. According to 1994 estimates, Malawi had one of the most highly concentrated export sectors among the SADC member countries.

Fig 2.3

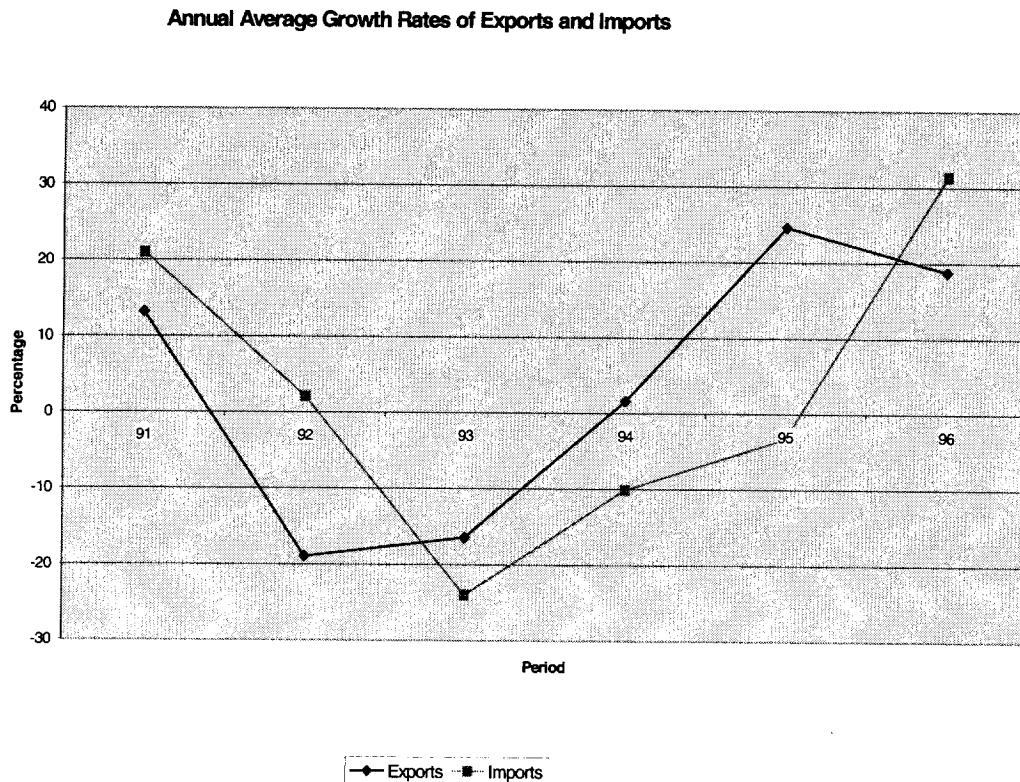


30. **Table 2.5** illustrates Malawi's terms of trade and the movement of price and quantity of exports and imports. Malawi's terms of trade deteriorated in the 1990s. The analysis suggest that there was no marked difference in Malawi's degree of integration during the 1990s compared to the previous decade. This was because the policy interventions were not decisively focusing on its competitive and comparative advantage, which would enable it to compete globally as intended by the liberalization programme. However, it is essential to remember that Malawi's structure of production, and quality standards may not have reached a stage of maturity for the economy to integrate at a fast pace. The Malawi economy is basically agricultural with no appreciable dynamic sector such as manufacturing, that could immediately gain from liberalized trade. Table 2.6 illustrates the structure of the manufacturing sector in Malawi. The Agro-processing industry alone contributes over 30% of the manufacturing output. The manufacturing sector value added was however low and for it to become dynamic the economy needed to be diversified towards higher value-added manufactured goods and tradeable services. It is also worth noting that the overall growth rate of the manufacturing sector decreased in the 1990s compared to the 1980s.

31. In general, the reform policies carried out during the period did not make any impact on the integration process of the Malawi economy. There are several reasons including slow implementation of policies, the long time lag required

before such policies can transform the economy, and rigid production structures incapable of competing in the global market.

Fig 2.4



Trends in Investment Flows

32. Investment flows can also be used as an indicator of globalisation. The investment flows during the 1990s both portfolio investment and foreign direct investment, were insignificant. The reasons range from the poor infrastructure of the country to inappropriate government policies among others. A World Bank Survey (1997) of private business cited poor infrastructure, crime and theft, inflation and corruption as major obstacles to private business. The same survey also cited tax regulation and policy instability among moderate obstacles. Although significant policy changes were undertaken in liberalizing the financial sector (privatisation of major corporations, for instance), the private sector still played a minor role. During the period, the share of the private sector in total investment on average increased, but it did not overtake public sector investment (see **Table 2.7**). A recent World Bank projection (**Table 2.8**) for the early years of the next century indicated that there will be a significant improvement in private investment, while public investment was expected to decline slightly. Consequently, the increase in total investment will still remain marginal unless the high-case scenario materializes.

33. The stock of foreign direct investment (FDI) in Malawi was small in magnitude but increased steadily. As a whole it seems to be comparable to the

average for African countries (see **Table 2.9**). From a low of \$100 million in 1980, the stock of FDI reached \$284 million by 1997 and it averaged around 10 per cent of GDP.

34. Malawi's competitive position was the lowest among SADC countries (**table 2.10**). Similarly, both the improvement and optimism indices and the opportunity to trade index also put Malawi among the least-favoured countries in the region.

35. The above assessment reflects the unfavourable economic environment for investment flows in the 1990s, at least relative to similar countries in the region. The problem such countries faced in attracting FDI goes beyond the existence (or absence) of pure economic returns. Perceptions and overall socio-political uncertainty played an important role in determining the direction of FDI flows. To put it differently, the premium required to compensate for the actual or perceived risks of investing in the economy was high.

36. According to the World Bank Development Finance Country Report (1997), portfolio equity flows to Malawi was nil for the last two decades. This was mainly due to the financial repression which characterized Malawi's financial sector before the introduction of reforms, and its slow development during the post-reform period. The equity market was in its infancy with only a few domestic companies that emerged to finance investment through equity capital. It is unlikely to attract any appreciable equity capital any time soon, despite its fast growth at a global level.

International Conferences and Implementation of Resolutions

37. In the 1990s, Malawi became a major player in different international and regional forums owing to the open society and the change in the political system. Some of the key forums include: IMF/World Bank Annual Meetings; Commonwealth Meetings; ADB Annual meetings; SADC meetings; COMESA meetings; OAU meetings; World Economic Forum; Southern Africa International Dialogue (SAID); and many more.

Environment and Natural Resources

38. Rapid population growth in the last decade posed challenges on the impact of economic growth and environmental management. Recognising the escalating natural resources depletion and environmental degradation, the Government adopted the National Environmental Action Plan (NEAP) in 1994 which identified several issues relating to environmental degradation: population growth, soil erosion, deforestation, water resource degradation and depletion, threat to fish resources, threat to biodiversity and human habitat degradation.

Gender Equality and Women's Empowerment

39. The Government of Malawi demonstrated its commitment to incorporate gender issues in the main stream of policy dialogue and planning by establishing a

ministry responsible for Gender, Women and Children's Affairs. During the decade, the weak gender policy was reflected in women's inability to have adequate access to basic social services, including access to education, increased Cases of sexual and domestic violence also increased. During the decade, women were under-represented in all spheres of political, professional and managerial positions. Malawi is a signatory to the convention on the elimination of all forms of discrimination against women (CEDAW).

3.0 ASSESSMENT OF FACTORS THAT HAVE FACILITATED OR CONSTRAINED DEVELOPMENT

Domestic Opportunities and Constraints

Peace and Social Stability

40. The beginning of the decade saw a wind of political change in the former Soviet Union and other East European countries. This brought to a close the years of East-West conflict which placed countries on either side of the two super powers. As the call for a more open political society descended on Africa, Malawi was not spared and this transformation, to a significant extent, affected the country's development efforts. The suspension of non-humanitarian aid in 1992 by the traditional donors triggered major political developments in Malawi which led to Malawi changing to a multiparty political system of government during a referendum. Two general elections have since been held.

41. Malawi enjoyed a relatively stable political environment during the previous thirty years after independence under two systems of government: the one-party system of government (1964-1994) and the pluralistic multiparty system of government after 1994.

42. The transformation of Malawi into a pluralistic multi-party system of government also necessitated the creation of institutions to ensure the separation of powers and the independence of the legislature, executive and judiciary. In addition, a number of institutions were established to promote healthy dialogue and diversity of opinions on topical issues affecting the people of Malawi. Some of the institutions created included the Law Commission, the Ombudsman, Human Rights Commission, and the Anti-Corruption Bureau etc. If nurtured properly, these institutional arrangements will be critical to sustain peace and stability in the country. However, Government realises that the creation of these institutions call s for additional resources to fund their operations.

Economic Infrastructure

43. Economic infrastructure forms a key component in the enabling environment for the private sector. The size of the Malawi market, the and the landlockedness pose a particular challenge to meeting the needs of the private sector for high quality infrastructure at the lowest possible cost. Telecommunications, energy, and logistics and transport are the areas of fundamental importance to private sector development.

44. After independence, emphasis on economic infrastructure centred initially on the creation of basic facilities and later on switched to the improvement of capacity utilization. Despite the previous heavy investments and strong focus on economic infrastructure, most of the facilities deteriorated and the services remained poor.

45. During the 1970s and 1980s period, the government continued to invest heavily in economic infrastructure which included airport, road network,

telecommunications, energy, and water projects. The government also introduced a number of reforms during the past decade aimed at enhancing the role of the private sector and strengthening Government's infrastructure maintenance program. Major initiatives included the establishment of the National Roads Authority (NRA), the Privatization Commission, the National Electricity Council (NECO), and the Malawi Communications Regulatory Authority (MACRA). These institutions were created to enhance competition in areas that were public sector dominated. In addition, the Malawi Railways was concessioned to a foreign concessionaire to improve the efficiency of the railway system, particularly the international operations to the port of Nacala.

46. Without modern telecommunications infrastructure, Malawi runs the risk of being left behind in the technology age. The sector's strategic importance arises from the increasing role played by value-added information and communications in economic activity and the unique ability of communications and information technologies to overcome difficulties of distance from and access to regional and world markets. In addition, the progressive impact of technological advances which are reducing the costs of providing information and communication services is crucial. In view of this, the Government split the public telecommunication corporation into a postal corporation and a telecommunication company. The telecommunication company is earmarking for privatization in the first half of the current decade.

47. The main source of energy in Malawi is electricity almost entirely generated from hydro electric power stations with a total installed capacity of 220.7 megawatts. An additional 128 MW will be added once the new plant, Kapichira is commissioned in two phases of 64 MW each in 2000 and 2001 respectively. According to estimates, the main source of Malawi's electricity, the Shire river, has a total hydro capacity of 582MW.

48. In the early part of the 1990s, demand for electricity was static. However, from mid 1990s, demand grew at 15MW per year owing to a liberalized economy. The reliability of supply to consumers deteriorated during the decade with faults per 100 consumers increasing from 30 to 40 between 1994 and 1997. Customer connection rate for new customers reached a high 5 months in 1997.

49. The water sector aims at the expansion of the networks to make potable water and sustainable sanitation services more available, for both rural and peri-urban areas, and to improving the efficiency and cost-recovery of the sector to make regional water boards financially sustainable. Coverage for both Blantyre and Lilongwe Water Boards is about 80%. Unaccounted for water is problem to all of Malawi's water boards and the current estimates ranges of UFW is 21 – 36%.

50. A common strength of Malawi's water boards is the level of metering. Most of the water boards' industrial, commercial, and residential accounts are metered.

51. The tariff structure provided for cross-subsidies from industries, business and more affluent households to poorer households. A major challenge facing the

sector will be how water tariffs should be set. One of the major causes for required increases in water rate during the period was level of arrears by Government and state-owned enterprises.

52. Some of the major constraints to efficient provision of economic infrastructure in Malawi included the following:

- Parastals did not develop professional cadre of managers and technicians and as such performed badly.
- Failure of policies to recognise financial viability and quality of services. In most cases under-collecting or under-pricing led to the deterioration of the services and scarcity.

53. Faced with tight budgets, Government will need to explore more innovative ways of providing essential infrastructure services. Some of the options to be looked into by Government include rehabilitation the facilities; increasing private sector involvement in areas which were hitherto the domain of the public sector; and improving cost recovery from public services

Policy Reforms

54 Since political independence in 1964, the Malawi Government has been concerned with addressing various development issues. During the 1960s and 1970s, the development approach to development planning was mixed. It comprised an approach oriented towards state intervention but at the same time allowing for private enterprise to thrive. However, such private enterprise had heavy political underpinnings especially in the ownership of estates. Emphasis was on the agriculture sector, that is, farming enterprise and agro-based industries. Further, within the agriculture sector, smallholder farmers were not allowed to engage in growing high value cash crops such as burley tobacco hence their incomes were generally low compared to large estate owners. However, the agriculture sector has since being liberalisation allowing smallholders to participate in the growing of high valued cash crops.

55. Structural Adjustment Programmes implemented since the early 1980's sought to maintain macroeconomic stability; restructure the public sector and restoring fiscal discipline; reform investment and trade policies; and the regulatory environment. The results were mixed - usually a cyclical trend of good performance was followed by a period of poor performance.

56. There was, however, some good progress made during the decade. The Government successfully intensified the smallholder growth strategy; introduced the Medium Term Expenditure Framework (MTEF); deepened the process of civil service reform; embarked on a privatisation program and established a sound institutional mechanism to manage the program; maintained its pro-poor stance in Government expenditure; and persisted with its emphasis on education. The government gave strong support to community led development initiatives and

piloted public works programs as an alternative to untargeted hand-outs as a means of helping the very poor.

57. New legislation was also passed during the decade on the environment, forestry and fisheries, with an important focus on empowering communities. In infrastructure, the government reformed management and financing of the road sector; and introduced reforms in the energy and telecommunications sectors.

58. The market orientation of the economy in agriculture, trade, industry and financial services did not generate sufficient response to sustain economic growth. During the decade, well intended reforms were at times delayed or not implemented at all because of various constraints. These included weak public expenditure discipline and prioritisation which led to excessive spending on non-priority items and under-funding core activities. Reforms were also slow in some cases because of weak capacity in public institutions due to high rates of attrition due to several factors including HIV/AIDS.

59. The economy relied heavily on borrowed resources to finance and support the foreign exchange liberalisation program. It was envisaged that the effectiveness of the policy reforms would depend on the positive response from the private sector, reflected in new private investments. However, private sector development and growth was constrained by the narrow base of local entrepreneurship; the poor condition of much of the plant and equipment; the unavailability of term financing; the poor infrastructure; the inefficient production and quality considerations.

60. Due to weak private sector response during the period, coupled with over dependence on traditional cash crops, Malawi faces the additional constraints of excessive reliance on foreign resource to finance imports and the budget deficit. More actions will be required to foster export drive for the reforms to be effective and sustainable. Four major policy areas will require further refinement and fine-tuning:

- A stronger approach to control public finances that will involve a process of tax reduction and reform to trigger enterprise, employment, and equitable development;
- A competition policy which promotes and supports innovative, successful, market-driven enterprises and which safeguards the interest of consumers;
- Achievement of higher levels of education and skills to form the basis of personal development and national competitive advantage; and
- Development of policies in science and technology to support innovation by the business community and within the public sector.

Conducive Environment for the Private Sector

61. A conducive environment for the private sector embraces a number of features including political stability, macroeconomic stability, friendliness of bureaucracy and policies, attitude of welcome, availability and cost of infrastructure, availability reputable financial institutions and other local support enterprises, and quality and availability of labour. Some of the areas have been covered under the different sub-sections in this chapter. Therefore, this section will dwell on the issues that have not yet been covered.

62. In the 1990s, emphasis was placed on several areas requiring reform to boost private sector performance. The major areas included policies that aimed at reduce fiscal deficits and eliminate domestic deficit financing; implementing a privatisation program; reforming in the financial sector regulatory framework; improving the infrastructure services through commercialisation and private sector participation; and introducing private participation in production and marketing of agricultural produce.

63. Liberalisation and stabilisation measures after 1993 under sectoral programmes aimed at reinforcing the market-oriented industrial development. There were some positive measures implemented under the broad-based structural adjustment programmes. The key reform programs included: price decontrol; elimination of foreign exchange rationing; elimination of authority to grant exclusive products rights; introduction of surtax credit system; repeal of the Industrial Development Act; reform of commercial parastatals; introduction of market-based instruments for monetary policy management; elimination of monopsonists; liberalisation of the agriculture sector; liberalisation of the financial system; publication of a Statement of Investment Policies and an Investors Guide and; establishment of Malawi Investment Promotion Agency.

64. Malawi's financial system operates in conformity to the international standards. The monetary authorities actively pursued more market-oriented monetary control and broadened the range of monetary instruments. Banking competition was increased through licensing of more entrants.

65. Financial liberalisation according to a recent study (UNCTAD 1999), generally did not lead to an increase in the competitiveness of Malawi's financial sector to spur private sector development. New loan products were largely introduced by recent entrants into the formal financial sector. These included factoring, insurance premium financing, discounting bills, and structural finance on the lending side. Diversification by older banks concentrated on increase in lending to such sectors as manufacturing, trading and households, which were not favoured before reforms. On the savings side, both new and old banks did not do much to introduce new savings instruments. In fact, some of the banks withdrew longer-term deposit instruments and raised minimum deposit balance requirements.

66. In terms of quantity of deposits and credit, overall, these did not increase in relation to changes in the level of economic activity in the country (**Table 3.1**).

At corporate banks and the only mortgage bank, these increased due to the offer of competitive deposit interest rates. However, this was offset by a sharp decline in the ratio of deposits to GDP and of credit to GDP at commercial banks. On the deposits side, financial savings were discouraged by high rates of inflation, which partly contributed to negative real interest rates. They were also constrained by low rates of growth of profits (and other incomes) and budget deficits. Reduction in the rate of inflation, restoration of high rates of economic growth and elimination of budget deficits would facilitate an increase in financial savings. On the credit side, the demand for bank credit was adversely affected by an unfavourable economic environment of high budget deficits, large Government demands for bank credit, high rates of inflation, high nominal rates of interest and a depreciating currency, all of which must be contained. Private-sector demand for bank credit was also adversely affected by unreliable power and water supplies, an unsatisfactory state of the internal road network, unreliable telecommunications system, a rising rate of crime and high transport costs, all of which will need more effective attention.

67. The relatively low level of private-sector demand for bank credit was, furthermore, blamed on the conditions that banks imposed on borrowers. The amount of security that banks demanded depended on their perception of risk. Where the level of risk was low, less was demanded by way of security, but where it was high, the amount of security demanded tended to be high as well. What could be objectionable was not the amount of security, but the type of security since borrowers may not have been able to offer certain types. In this regard, there will be a need for banks to exercise flexibility, to demand forms of security that will suit different borrowers and to devise other ways of security credit.

68. For commercial banks to spur private sector development, competition ought to be introduced in the market. However, none of the existing banks suffered under the weight of competition from new institutions. The entry of two small foreign-based firms into commercial banking did not provide strong competition to existing commercial banks which remained market leaders. Any future entry of bigger and aggressive foreign-based banking corporations will exert pressure on the existing banks to improve their efficiency.

69. Financial sector reforms did not pay much attention to the need to strengthen the micro-finance sector. There were developments during the period and the Government defined the country's micro-finance policy framework. This might assist in introducing new micro-finance lending institutions on the market. The only player was a state run institution. Other important missing links included export finance; the informal financial sector; and the primary capital market required to promote companies and issue new shares.

Domestic Resource Mobilisation

70. Domestic resource mobilisation was weak because of the overcrowding effect as a result of heavy public sector borrowing. Domestic Resource Mobilisation entails that household, and the public sector should generate enough savings for investment. Government savings are largely influenced by the fiscal

policy - which encourages revenue (taxation) and expenditure measure both of which impact on the overall net savings of government. There were slippages in adhering to fiscal and monetary targets. Between 1990 and 1999, the share of public credit in the net domestic credit averaged 50% when the target was about 20%. Also the share of government budget deficit before grants as proportion of GDP averaged about 9% in contrast to the target of 5%.

71. Malawi now faces the challenge of ensuring that the projected demand for investment is matched by an increase on the supply side mainly from the domestic resources. The major thrust of Government will be to institute measures that will lead to effective mobilisation of savings. First public savings would be raised by fiscal prudence and consolidation. Secondly, the banking system and the non-bank financial institutions would be strengthened to increase confidence in the financial sector, thus encouraging private savings. Thirdly, a stable macro-economic environment will be pursued to ensure positive real interest rates.

Governance and human rights

72. Good governance is increasingly recognised as a prerequisite to economic growth and development. The history of governance in Malawi was influenced largely by the system of Government introduced after independence in 1964. The leadership between 1964 and 1993 heavily authoritarian and not-transparent. The policy process between 1964 and 1993 exhibited both the strengths and weaknesses of extremely centralised decision making.

73. The introduction of multiparty democracy in 1994 brought in a constitution, which provides for people's participation in the formation of government, guarantees freedom of press, and ensures separation of powers. The constitution guarantees the protection of human rights for all citizens. The National Plan of Action in the field of human rights (1995) included the creation of an effective legal framework for the promotion and protection of human rights. Particular attention focused on rights of vulnerable groups: women, children, workers, and prisoners/detainees. The pluralistic society that emerged in the beginning of the decade fought to establish and maintain good governance and human rights. Other than changing the legal environment to enshrine this need, government created a number of institutions that would safeguard this new doctrine. However, the new doctrine created other concerns in the country. In the 1990s, insecurity became one of the most pressing concerns among the ordinary people as well as the business sector following increased armed robberies and other criminal activities.

74. Good governance during the period was also promoted through various means one of which is decentralisation. This was a process that involved the transfer of responsibilities to district level. Good governance also involved putting rules and procedures to make public expenditure transparent and efficient. In addition public information is central to good governance. Throughout the 1990s, the government instituted several policies making it hard to misuse public funds with impunity and guaranteeing press freedom to ensure that information was disseminated as widely as possible.

75. Following the adoption of a multi-party system of government, the state was still gearing its contribution to economic development as it matched its role with its institutional capability. Capability encompasses the administration or technical capacity of state officials as well as the deeper institutional mechanism that give politicians and civil servants the flexibility rules and restraints to enable them to act in the national interest.

76. Malawi has a long way to go because there are many forces influencing governance. The experience with governance since 1993 reveal fundamental weaknesses in the process of building the foundations of an effective public sector; instituting formal checks and balances and controlling corruption or corrupt practices; and promoting partnerships between the state and other stakeholders. The government, in the 1990s introduced a program to restructure the civil service so as to improve efficiency and control the growth of civil service wages and salaries. These goals will take time to be achieved. Efficiency/productivity, work ethic and commitment of the civil service declined during the period. Further, as salaries and wages did not keep pace with inflation, temptations might have become high for senior as well as junior civil servants to engage in private income-generating activities.

77. The shortfalls in macroeconomic management were due in part to insufficient technical expertise for policy formulation, as well as under-utilisation of the available expertise. Policy implementation during the period was inefficient, even in the case of some of the well-thought out policies. There was, however, an improvement in consultation between the economic policymaking organs and various interest groups in civil society.

78. The security situation in the country also needs to be improved. Using donor funding and local resources, the government increased the police force, the number of vehicles for patrolling and other facilities. However, these changes did not improve the security situation, as they were marginal and provision of private security services and establishment of neighbourhood watches, has mushroomed. Malawi needs to accord top priority to improving security, allocate more resources to the police and the judiciary, ease the economic hardship suffered by the people, and allow village and ward authorities to take responsibility for preventing crime.

79. Over the long-term, government must build formal checks and balances, backed by core state institutions such as an independent judiciary and separation of powers. These are essential ingredients for ensuring that no one else in the society is above the law, although, the rule of law is a necessary but not a sufficient condition for good governance. The challenge to Government will be to ensure that institutional arrangement put in place to foster partnerships with other stakeholders within and outside state machinery are effective and strong.

HIV/AIDS

80. HIV/AIDS during the period took a terrible toll in Malawi as the incidence of HIV was reported to be as high as 90,000 in the mid-1990s and this figure was expected to decrease to about 50,000 by 2010. Research revealed that incidence of

HIV/AIDS among farmers and professionals was relatively high and the risky age group was 15-49 years, indicating the devastating effects of the epidemic on economic development. The HIV/AIDS epidemic was caused by continued high-risk sexual behaviour such as unprotected sex with multiple partners. There was a slow progress in changing the high-risk sexual behaviour. Thus, active government and private sector participation will be crucial in the form of the provision of finance for the monitoring and control of the virus including the epidemiological surveillance, research on risky behaviour that spreads HIV and assessment of the costs and efficiency of the direct interventions. As no effective cure has been found, prevention will continue to be the prominent goal in HIV/AIDS policy in Malawi. The major responsibilities in the prevention of HIV/AIDS would involve the reduction of the negative impact of high-risk behaviour and the provision of information about the disease.

81. Prevention efforts will focus largely on changing the behaviour of people with the highest risk for contracting the virus and unknowingly passing it on to others. Considering that the disease is already widespread it will be necessary to fight for behavioural changes among the broader population to reduce infection rates. However, simply increasing awareness of HIV transmission will be insufficient. A number of related factors play a significant role in the spread of the infection. For instance, people use knowledge to assess the impact of risky behaviour and internalise it. People must understand the extent to which HIV infection could affect them personally, the extent to which people perceive their behaviour to be risky and the extent to which they have the power and skills with partners. Thus specific support will be directed toward programmes that could bring about behavioural change rather than knowledge alone. By 1999 the awareness level about AIDS was as high as 98 per cent but the real challenge still remained behavioural change.

82. Government will still have to devote resources towards the treatment of AIDS patients. Although the treatment of people with AIDS is primarily a private good as the benefit accrue largely to the person being treated - Government will likely incur certain costs relating to palliative care to relieve symptoms such as headache, pain, and diarrhoea; treatment of opportunistic infections such as tuberculosis and pneumonia, which can be fatal to people with weak immune system, and anti-retroviral measures which attack the virus directly). More importantly, preventative and awareness programs need also to move to the communities rather than being at implemented from the centre.

Agriculture and the Rural Sector

83. Agriculture has been the major contributor to economic growth in Malawi. It is a major source of employment in the country, with an estimated 80% of the labour force employed in the smallholder sub-sector and about 11% in the estate sub-sector. The main sources of growth have been tobacco as a result of the specific heavy public investment in the form of research, extension, marketing services, and credit.

84. Malawi's land area is estimated at 9.4 million hectares. It is estimated that about 5.7 million hectares are suitable for agriculture (4.55 million hectares under

customary tenure and 0.55 under the estate sector) and 4.6 million hectares are cultivated. Land scarcity became an issue because of the growing population. Nearly all cultivation was rain-fed, making Malawi subject to periodic droughts and fluctuations in production levels. The agro-ecological areas depict diverse tropical and sub-tropical climate, which offers the opportunity for food and commercial crops, orchard fruits and nuts, high-value horticultural and floricultural crops. Of the estimated 290,000 hectares of potentially irrigatable land, about 64,000 hectares were irrigated and the bulk of it was in the estate sub-sector. This indicates the clear potential for irrigation, particularly in the lower Shire and along the lakeshore.

85. The reforms which started in the 1980's were continued in the 1990's and focussed on the regulatory environment, producer price liberalisation and the exchange rate realignment. The reforms in exchange rate and trade policies reduced implicit taxation of agriculture and the discrimination of exports. There was increased entry by smallholders into areas that were previously restricted, such as burley tobacco production and private sector participation increased in the imports and distribution of agricultural inputs.

86. Despite all the positive attributes a number of factors held back increased productivity and diversification. These included Government pricing policies, world market policies, lack of interventions to create forward linkages with other industries in the value added chain, supply and demand constraints on the increased use of higher yielding varieties. The major constraints in the agricultural sector included the following:

- Inconsistencies between stated sectoral strategies and public expenditure;
- Imbalances in capital and revenue expenditures;
- Weak planning and implementation capacity;
- Fragmentation and poor co-ordination of donor assistance;
- Lack of forward linkages with other productive sectors and
- Dependence on rain-fed agriculture

87. Government will have to look at new ways of addressing the above constraints. In addition the agricultural sector was affected by the macroeconomic performance.

88. To facilitate the growth of the agricultural sector Government will adopt and support monetary and fiscal policies that will be neutral between sectors. Efforts, will also be taken to address problems at the farm level as a result of the dualism between the estate and traditional smallholder farmers.

89. The availability of new land was a major constraint for large-scale agricultural development. This will entail that expansion of the agriculture sector will have to increasingly rely on the development of intensive production. In order to achieve maximum utilisation of the land resource towards this end, Government will review its support to encourage farmers to switch to more resilient and remunerative crops such as vegetables, fruits, flowers. There will also be a need to emphasise productivity improvement through research and effective farm management in order to reduce losses and increase net yield.

90. The growth and viability of the agriculture sector will require greater commercial orientation in terms of the choice of the crops and the management style. Emphasis will be placed on land consolidation, rehabilitation, replanting, drainage and effective irrigation as well as adoption of technology by farmers. Malawi will have to intensify agriculture by specialising in the production of high value-added and market-oriented crops in which it has a competitive edge. Vertical diversification through the development of linkages with agro-based industries will also be promoted to ensure that growth in agriculture will trigger industrial development. In addition, Government will actively promote horizontal integration of crops with potential viable livestock and agro-forestry sub-sectors.

91. Government will also assess the country's dependence on maize as the staple food crop. In terms of land and other input requirements, the cost of production is high. Besides, the volume of output fluctuates with changes in weather. During drought, output can fall significantly, undermining food security in the process. A key policy question will be whether maize should continue to be promoted or whether consumer tastes should be changed in favour of alternative drought resistant staple food and less sensitive to the amount of precipitation.

Human Resources Development

92. Malawi's human development indicators trail below most countries the region. Improved access to health and education will be critical for long-term development in Malawi. On the whole, human development in Malawi can be described as unsustainable for a number of reasons. The first is that economic growth in the short run was achieved by reducing environmental capital. To the extent that the reduction in environmental capital tends to reduce the future rate of economic growth, long-term economic growth is not sustainable. This fact is not revealed in national income measures because such measures do not take into account environmental degradation which they should.

93. The second is that economic growth was undermining human capital. One aspect of this is that the rate of economic growth was not high enough to prevent the number of poor people from rising. Since poor people were not able to invest enough in the education and health of their families, the growth of human capital, upon which future economic growth depends, was seriously compromised. The third aspect is that in the face of high rates of inflation and declining productivity, low rates of economic growth failed to prevent real incomes of workers from falling. This led to a reduction in their standard of living and in their morale, ability and willingness to work. The fourth aspect is the fact that the fall in real earnings led to an exodus of high-level or skilled manpower from Malawi to other countries and within Malawi from the public sector to the private and NGO sectors.

Health Services

94. Malawi's health indicators are still amongst the worst in the world. Life expectancy at birth was at 44 years. Infant mortality rate and under five mortality rate were estimated at 133 per 1000 live births and 234 per 1,000 live births,

respectively. The constraints include both lack of financial resources and lack of critical health personnel. To redress the worsening health indicators, more resources were channeled to the Ministry of Health and Population whose share ranges between 6.7% and 10.5% of the revenue expenditure. However, the actual expenditures tended to be lower than the budgetary allocations and there were a mismatch between the priority activities and the actual allocation of funds. The priority sectors of preventative and promotive health services were allocated less than 20% of the health budget while the technical support services and secondary curative services accounted for nearly 51% of the health expenditure budget. There were also shortages in terms of health personnel. Malawi had a ratio of 6 nurses per 100,00 people and 2 doctors per 100,000. In addition to increasing the number of personnel involved in delivery of health services, there is also a need for increased scope in the efficiency of the spending in the health sector; the intra-sectoral re-allocation from tertiary services to primary services; and re-allocation from hospital overheads to goods and services. Towards the end of the decade the Ministry undertook reforms measures, which were in line with the overall decentralization policy, aimed at improving efficiency and increasing the number of health personnel.

Education

95. Increased investment in education could accelerate growth in several ways. For instance educated farmers have been found to achieve higher productivity levels than those who have not gone to school. Cost-benefit structures have shown that actual rates of return to investment in education are about 20% for primary, 17% for secondary, and 13% for higher education.

96. At primary level, only 50% of the school-going population or nearly 2 million children enrolled for primary education up to 1994. The repercussions of the low enrolment levels were low literacy levels (40%). Free primary education was introduced in 1994 and enrolment levels increased from nearly 2 million to 3.2 million children, representing almost 95% of the school-going children. The numerical gains in the enrolment levels adversely impacted the quality of education due to inadequate classrooms, shortage of qualified teachers, and insufficient instructional materials. Secondary and tertiary levels of education depicted similar trends in terms of the declining quality of education and internal inefficiencies.

97. In general, the major constraint facing the education sector was low access, particularly at secondary and tertiary levels. While the improvement of access to basic education in rural areas with emphasis on primary education and adult literacy will remain a major priority within the intra-sectoral resource allocations, other initiatives will have to be explored including the restructuring of fees at post primary level and constraining output in fields which are not strategic to the economy.

Environment

98. Malawi has a total land area of about 9.4 million hectares. Out of this total, 4.6 million hectares, representing 49 per cent, were under cultivation in

1992. However, at the unimproved level of land management among smallholder farmers then, only 31 per cent of the total land area was suitable for cultivation. Hence, 18 per cent of the cultivation was taking place on marginal or environmentally fragile land like steep slopes, riverbanks and valleys. This situation is believed to have worsened since then. The extension of cultivation to marginal areas, unsatisfactory land use practices, lack of appropriate conservation measures, deforestation and overgrazing led to a loss of agricultural land productivity, mainly through soil erosion and declining soil fertility.

99 About 37 per cent of the total land area (3.5 million hectares) is classified as forests. This is composed of 0.73 million hectares of forest reserves, 1.09 million hectares of national parks and wildlife reserves and 1.7 million hectares customary land forests. It was estimated that aggregate consumption of fuel-wood exceeded the level of sustainable yields by as much as 30 per cent. There was a continuous loss of forest resources, especially on customary land due to clearing of forests in excess of natural forest regeneration and afforestation activities. The rate of deforestation was estimated at 1.4 per cent per year due to dependence on agriculture, dependence on fuel-wood, high rate of population growth and excessive selling of wood to generate income. Deforestation resulted in depletion of surface water resources and in problems of siltation /sedimentation, reduced base flows and recurring drought conditions.

100 With respect to water resource management, Malawi faced three serious problems. The first was chemical contamination of stream water in urban areas due to improper disposal of domestic and industrial wastes; and pollution by agro-chemicals through water run-off due to absence of proper biological and physical conservation measures on farms in rural areas. The second was the poor bacteriological quality throughout the year of major rivers due to inadequate sanitation facilities and the presence of other sources of organic pollution. As a result of this, it was estimated that 50 per cent of all illnesses in Malawi were caused by water borne diseases. Thirdly, depletion of surface water resources caused by deforestation led to watershed loss, siltation/sedimentation, reduced base flows and recurring drought conditions. The natural resources of land, wildlife, water and fish provide a basis of sustainable development. Government prepared the National Environment Action Plan (NEAP) in 1994 to redress some of these problems associated with the over-exploitation of the natural resources. The NEAP identified the following as the key factors contributing to environmental degradation: high population growth, soil erosion, deforestation, human habitat degradation and water resource depletion, over - fishing.

101 Measures were instituted to establish individual and commercial woodlots to conserve the catchments, to discourage cultivation on steep slopes and along river banks. These measures were backed by measures to ensure environmental education and information through the mass media. In addition, environmental statutes were passed to protect the environment.

Research and Development

102. Although it was recognised that research and development are critical for sustained economic development, the Government did not accord the deserved

priority to the sector. Research and Development activities go a long way in solving some of the problems particularly in export diversification, manufacturing, and sustainable utilisation of environmental resources, enhancing industrial competitiveness and providing support to the SME sector. Problems in the past decade included inadequate funding, particularly for research and development activities outside agriculture. Even in agriculture the bulk of the funding was from donors, a situation which created unsustainable position as donors phased out. It was also found that the institutional framework to disseminate research findings to end-users was inadequate and not co-ordinate.

103. While acknowledging useful of basic research, one of the thrusts will be to emphasise applied research, development research, and innovation in areas that can contribute significantly to the country's development and competitiveness. All these initiatives will require resources in the form of budgetary allocations, matching grants, soft loans, preferential credit to accelerate inventive activities in the private and public sectors.

Science and Technology

104. In the formulation of Vision 2020, it was recognized that science and technology play an important role in raising new opportunities for enhancing firm's competitiveness and growth. Science and Technology provides product and service differentiation in the market place. There is a need for national budgets to incorporate adequate funding for technological innovation, including industrial research, technology, and diffusion. The role of the private sector in providing funding for these activities will also be crucial.

Mining and Mineral Development

105. The contribution of the mining sector was below 1% of GDP. The major mining activities during the decade included the production of coal, cement, and lime. Official figures estimated that employment in the sector reached 4,000 tones by 1999 while exports mainly coal and gemstones, reached US \$ 1 million. The country's potential in gold, bauxite, diamonds, copper, and petroleum and platinum group metals has to be explored.

Gender Concerns

106. Gender issues during the period increasingly gained attraction in the design and implementation of programmes in Malawi. Adult literacy rate was at 42 per cent. But only 32 percent of the women were literate compared to 52 per cent of the male counterparts. Yet women were involved in most of their household functions such as farm work, childcare, food preparation, provision of water and firewood. As a first step the Malawi Constitution has provided for the protection of women's rights. However, there are many other areas that will require transformation to promote gender equity and equality.

Co-ordination of Non-Governmental Organisations

107. There was an increase in the role of Non-Governmental Organisations in the process of socio-economic development in Malawi during the decade. The number of domestic and international donor organisations increased during the period there was an obvious conflict between government and some NGOs in terms of strategies used in implementing poverty alleviation programs. Lack of government policy on the role of non-governmental organisations could explain some of the conflicts that arose. There was also an obvious lack of effective co-ordination between the two sectors. NGOs will be key partners in the next decade as government implements development programs including the provision of social safety nets

External Opportunities and Constraints

Official Development Assistance (ODA)

108. Globally the increasing scarcity of fiscal resources has been an important reason for the decline in net official development assistance during the 1990s. Malawi also experienced reduced share of aid as evidenced by reduced concentration of ODA in GDP. During the 1994/95 fiscal year ODA to GDP ratio was at 21 per cent but it had almost halved to 11 per cent by 1996/97.

109. Most of the ODA in Malawi was earmarked for budgetary support in the form of balance of payments support and project or development assistance.

The Impact of Conditionality on Development

110. During the 1990s, Government, with financial support from bilateral and multilateral donors, continued to implement structural adjustment programs with a view to increase the rate of growth of GDP, attain export diversification and to improve the performance of the civil service and the parastatal. Sector access to adjustment credit was always subject to specific policy or administrative reform across the various sectors. In most instances, because of non-performance of government in implementing policy reforms, donors tended to withhold the release of funds. The implication of this throughout the 1990s was felt mostly on the macroeconomic side. As donor pledges would already have been incorporated in government budget, the withholding of donor funds forced government to borrow on the domestic market or print money altogether. These measures were inflationary during most years and also crowded out private sector. In certain cases, government was forced to implement policy measures with the long-term negative consequence on the economy. For example, the introduction of intermediate buyers in the tobacco industry has had major impact on production and quality of the crop.

Aid Effectiveness

111. The effectiveness of aid depends on how well it is utilized. It is also influenced by such factors as the quality of economic management as measured by inflation, the budget deficit, and trade regime, effectiveness of the legal system and competence of the bureaucracy and extent of corruption within the public

sector. There are several factors that explain the effectiveness of aid during the period.

112. Difficulties in expenditure management and the need to control expenditure led to the introduction of the cash budget system in 1995. However, the cash budget, while initially crafted as a short-term stabilization measure, was maintained at the expense of undermining the effectiveness of the medium term expenditure framework and the associated donor support.

113. In addition, donor flows were also erratic and therefore became part of the economic problem. Donor support to Malawi was suspended in 1992 with a view to influence the transition from a one-party system of government into democratic and multiparty dispensation. The immediate effect was that several development programs were grounded to a halt. Even after successful transition in 1994, aid flows did not increase significantly, despite the fact that there was opening up to non-traditional donors. In some instances, traditional donors channelled their support to NGOs to by-pass the problem of fundability of funds and high-level corruption.

114. Nevertheless, aid helped to promote good economic policies by encouraging policy reforms and strengthening institutions. However, these did not translate into improved living conditions for the ordinary citizen.

115. The expected outcome was that private foreign investment would official development assistance. For Malawi, take an increasing share to offset the drop in private investment inflows into the country were insignificant, probably reflecting the erratic nature of macroeconomic stability compounded by small domestic markets.

Aid Co-ordination

116. Malawi is a Consultative Group (CG) country. The last CG meeting in the 1990s was held in December 1998 in Lilongwe where a total of US\$432 million was pledged. The latest CG meeting was held in Lilongwe in May 2000. A total of US1 billion was pledged towards Malawi's economic programs. The policy dialogue at the meeting helped to shape the macroeconomic policy framework and created a better understanding of the assistance needs of Malawi. Poverty alleviation remains the government's development priority and various donors subscribed to the poverty alleviation program. Donors within Malawi have taken the initiative in co-ordinating their efforts.

117. In a bid to improve the link of aid flows to development priorities, the government established a debt and aid management section within the Ministry of Finance to monitor external assistance flows and provided an interface with donors for purposes of aid co-ordination and management.

Aid Dependency

118. It was estimated that 80 per cent of government development expenditure was financed by external donors. Malawi also got balance of payments support

throughout the reform period which began in late 1980s. However, level of current account deficit remained high despite showing a declining trend. It was 18.4 percent in 1992, 15 per cent in 1994 and 12 per cent in 1997 and the gap was always met by donor assistance.

External Debt Burden and Degree of Indebtedness

119 The outstanding debt for Malawi increased at a rapid rate from US\$ 1.23 billion in 1992 to US\$ 2.6 billion by 1999. As a proportion of GDP this represented an increase from 93.2 per cent in 1992 to 155.1 percent in 1998. (see table 3.2)

120. Malawi is one of the most highly indebted countries in Africa. Since 1994, its outstanding long-term debt exceeded its GNP. The percentage of debt service payments to export earnings was also significant. This situation suggests the following implications. First, Malawi was borrowing not only for investment but also for other expenditures since investment only accounts for a small proportion of GNP. Second, with such huge debt service payments, Malawi's ability to increase its expenditure on investment in infrastructure for instance, to become globally competitive was limited. Third, such a huge debt burden discouraged flows of foreign direct investment via what is referred to as the debt-overhang. All these factors suggest that Malawi's ability to achieve sustainable and equitable growth and substantially reduce poverty will be adversely affected until the debt burden issue is resolved following the Consultative Group meeting in May 2000 and subsequent IMF/World Bank Board meetings, Malawi is benefiting from debt reduction through the HIPC Initiative. A decision point was reached by December 2000. According to estimates the assistance under the HIPC Initiative will translate into an annual debt service reduction of around \$40 to \$50 million over the 2000 to 2020 period, equivalent to around 1.3 percent of GDP for the 2000-09 period and 0.7 percent of GDP for the 2010-20 period.³ By comparison, the combined spending on health and education amounted to 6.3 percent of GDP in 1998/99. A significant percentage increase in the resources devoted to health and education – of as much as 20 percent above current levels – could thus be realised if the amount of assistance under the HIPC Initiative were fully used to augment health and education expenditures.

Market Access for Goods and Services

121. Malawi exports continued to be dominated by agricultural products despite the government efforts in promoting export diversification, away from agriculture. Tobacco, sugar, and tea remained the major export commodities during 1990s, accounting for 80 per cent in 1997. Small amounts of coffee, around 4 million kilograms per year, were exported to the United Kingdom and the European Economic Community (EEC)⁴. Sugar was mainly exported under the quota system to the European markets and the United States of America while the bulk of Malawian tea went to the London market. Since 1994, there was a noticeable increase in non-traditional agriculture exports particularly cut flower, paprika and animal products. From 1997 exports of textiles and garments

³ Interim assistance is estimated at approximately \$7 million in 2000 and \$29 million in 2001.

⁴ Malawi is a member of the International Coffee Organization. Previously its quota used to be 40,000 60kg bag or 2.4 million kilograms.

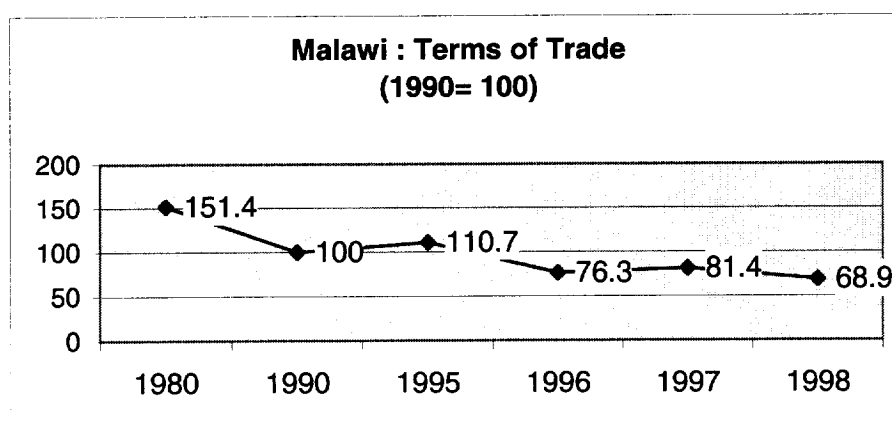
increased substantially, mainly to regional markets including South Africa. Malawi enjoys preferential access to South Africa markets and has sugar export quotas to United States of America, and the European market. The opportunity for Malawi rests in taking advantage of the African Growth and Opportunities Act (AGOA) for the USA market.

Terms of Trade

122. During the last decade, Malawi's terms of trade deteriorated significantly for a number of reasons. Firstly, the economy continued to rely on primary commodity exports (tea, coffee, sugar and tobacco), which faced weak demand. Secondly the global slow down triggered by the Asian crisis also contributed to the deterioration of terms of trade. According to the country economic report for 1999, the commodity terms of trade prevailing during the 1990s remained below the level attained in the 1980s.

123. Malawi is a small economy and, therefore, a price-taker on the world market. With growing anti-smoking campaigns and generally deteriorating terms of trade facing primary agricultural produce, Malawi performance in international trade will largely be influenced by the success of diversification into manufactured exports.

124. In recent years, Malawi had to re-negotiate trade agreements with South Africa and Zimbabwe, the two important regional trading partners. In both cases the main problem was the application of non-tariff barriers on Malawis exports.



Source: African Development Report 1999

Fig3.1

125. While the textile industry provided Malawi with a comparative and competitive advantage, the main problem was access to international markets in Europe and North America due to transport costs and restrictive rules in those markets. Although there was good international demand for Malawi tobacco, in general, tobacco is becoming a victim of anti-smoking campaigns. With respect to tea, the prices at the London market have been declining and there is a need to find alternative markets. Malawi may have to look for new markets for the

traditional export crops while developing new export products such as paprika, cut flowers, manufacturers and internationally tradable services.

Foreign Direct Investment

126. Foreign Direct Inflows were relatively low, accounting for 0.8 per cent of gross fixed capital formation in 1992 and 4.9 in 1993. However, since 1994 the proportion has been above 5 per cent and increasing. It was reported at 8 per cent in 1997.

127. The main problem was that both domestic savings and investment to GDP ratios were low, below 10 and 15 per cent respectively and fell short of the desired level for sustained economic growth. Even in a period of good performance such as from 1988 to 1991 the domestic savings rate of 10 per cent was inadequate to finance the levels of investment necessary for sustained growth. The economy had to look up to foreign savings in the form of ODA or foreign direct investment to augment domestic savings.

128. The stock of FDI in Malawi was relatively low. It was reported at US \$215 million in 1990 and at \$286 million by 1997. Efforts to attract more foreign direct investment were undermined by such factors as a general negative attitude towards Africa as an investment destination; land-locked position for Malawi, and poor infrastructure as well as a small domestic market.

129. The Asian financial crisis affected the foreign direct investment from the region to Malawi as several Asian companies withdrew their investment plans.

Regional and International Cooperation

130. Malawi continued to be a member of the Southern Africa Development Community (SADC), Organization of African Unity (OAU), United Nations, Commonwealth, World Bank and International Monetary Fund. It was also a member of the Lome Convention, General Agreement on Tariff and Trade (GATT) and later the World Trade organization (WTO); the Common Market for Eastern and Southern Africa (COMESA), the International Labour Organization etc.

131. There are several opportunities for Malawi in joining the various groups. Given Malawi's position as a small economy, and land-locked position, cooperation in the area of trade, transport, energy and infrastructure development can help alleviate some of the development constraints. Through the membership of groups for developing countries like the ACP, Malawi was able to negotiate for a common position on issues of globalisation.

132. During the 1990s the SADC group increased the pace for regional integration. Recognizing that road transport and communications were instrumental in removing operational constraints and facilitating the cross border movement of people and goods, member-states of the Southern Africa Development Community embarked on the implementation of development corridors and Malawi falls in the domain of Nacala and Beira corridors. The

importance of economic integration derives mainly from the opportunities it provides to pool resources for investment; enlarging markets for domestic products; and industrialises efficiently by exploiting scales economies and opportunities for cross-border vertical integration and production-sharing. Malawi has a small domestic market but through regional cooperation, and the resulting enlarged markets and easy access to inputs, Malawi can attract foreign direct investment and improve the living standards of the people.

133. SADC has to lobby for a re-orientation towards a production focused approach, marked by increased efforts to undertake regionally based projects and joint exploitation of natural resources.

134. For Malawi to maximize the benefits of regional economic cooperation, it must take part not only in trade liberalization but also lay greater emphasis on joint production and infrastructure investment schemes. In this regard, the Growth Triangle Initiative and the Nacala Development Corridor offer opportunities in the medium term.

Vulnerability to Shocks

135. The Malawi economy is agriculture-based and almost entirely reliant on favourable climatic conditions for good agricultural production and therefore economic growth. Agriculture usually accounts for more than one-third of GDP and over 90% of export earnings. The sector employs nearly half of those in formal employment, and directly and indirectly supports an estimated 85% of the population. The country's staple crop is maize, and tobacco is Malawi's largest export, followed by tea, sugar and cotton. Tobacco is Malawi's most important cash crop and export earner, normally accounting for around 70% of agricultural export earnings, and about half of all exports.

136. Malawi's economic performance in the 1990s, as outlined in chapter 2, varied widely. Years of steady average real growth were followed by sharp falls in growth mainly on account of drought. Apart from drought, the economy suffered from political upheaval unleashed by the demise of the one-party regime. Another key factor in the decline in economic performance was the freezing of all non-humanitarian aid to Malawi by Western donors in May 1992. Moreover, in the months before the elections in May 1994, the government embarked on a wild spending spree, including large wage increases for civil servants, which exacerbated already severe revenue shortages. Even after adopting a multi-party system of Government, growth continued to depend on the performance of the agriculture sector, which continued to be influenced by weather and government intervention through its sponsored distribution of free packs of seed and fertilizer to rural small-scale farmers.

137. The summary of Malawi's performance substantiates many observers' analysis of Malawi's economy. It has been defined by most analysts as being very fragile, narrowly based and lacking in key social services and infrastructure. Malawi has faced two central economic problems—the need to reduce the budget deficit and cut the level of absolute poverty—throughout the decade. Although the major objectives of the structural reform had largely been achieved in the earlier

years of the decade, key elements of structural reforms remained to be implemented, especially those that would trigger a supply response in the economy and avert or minimise vulnerability to shocks.⁵

138. After more than 10 years of structural adjustment programs, the structure of the economy was still dominated by production, processing and distribution of a limited number of agricultural crops⁶ and agricultural production remained dependant on erratic climatic conditions. Poverty during the period was both widespread and a growing phenomenon in the country. The Human Development Index (1999) ranked Malawi at 161 out of 174 countries. In terms of national income, Malawi was amongst the world's 10 poorest at US\$ 200 per capita. Some two-thirds of the population lived below the poverty line, defined as *the inability to fulfil one's nutritional requirements and to meet essential non-food needs equivalent to US\$ 40 per annum.*⁷ Poverty was most prevalent and severe in rural areas with some 95 % of the poverty gap (the shortfall below the poverty line) is found in rural areas.⁸ The highly prevalent poverty and heavy dependence on rain-fed agriculture made the rural population highly vulnerable to the effects of any adverse climatic and environmental factors. In normal times, over 50% of the rural households experienced chronic food insecurity which became pronounced in the pre-harvest period; attributable to small landholding areas, low production levels and low purchasing power among other factors.¹

139. The inability of Malawi to achieve structural adjustment objectives (aimed at stabilising the economy and achieve sustainable growth) could be attributed to many factors. The factors signify the vulnerability of the economy to shocks and the lack of structures that can cushion the economy against the effect of such shocks.

Nature of Shocks

140. Malawi's shocks could be categorised into three main areas. These were natural, economic and external shocks. These shocks had a negative impact on the ability of the country to attain sustainable economic growth. The following summarises the nature of the shocks and the resulting impact.

Natural Shocks

141. The most common disasters especially in the 1990s occurred as a result of floods and drought, both of which caused frequent food insecurity at both national and local level. Droughts affected up to 6 million people in Malawi⁹. It is estimated that 15% of the rural population lived on the fringes of highly flood risk areas, especially in the south of the country. In addition, approximately 35% of the population lived in the rain shadow zones and/or areas with unreliable rainfall distribution patterns. About 60% of smallholders experienced transient food

⁵ These reforms were mainly in agriculture, transport, social and financial sectors.

⁶ Mainly tobacco, tea, sugar, cotton and maize

⁷ Situation Analysis of Poverty in Malawi - 1993

⁸ Malawi Human Resources and Poverty Profile - World Bank 1996

⁹ Kalembe, draft report, p. 19]

insecurity in normal years as a result. Disasters therefore resulted in severe losses of livelihood systems among the affected population with women and children being the most vulnerable group.

142. The major Southern Africa drought of 1992/93 and 1994/5 seasons severely affected the majority of the population in Malawi and required food aid intervention. Even in the absence of pronounced droughts, intermittent long dry spells within the rainfall season were a common occurrence in many parts of the country. Such dry spells were reported to cause between 20 – 30% loss of total production yield per hectare. The El-Nino threat in 1997/98 had major devastating effects as had been anticipated. However, some parts of the country due to the continuous rains and flooding experienced loss of crops through wash-away and rotting of root crops. Government/Donor Review Mission¹⁰ found out that a total of over 4,600 hectares of food crops were destroyed.

143. In the 1990s, flooding in most districts of Malawi was as a result in large part from excessive run-off caused by environmentally poor land use systems on marginal lands, hills and catchment areas. Poor land use was particularly common in Southern Region where very high population densities forced people to encroach marginal lands. High level of deforestation was another causal factor. It was reported that the country's forests were disappearing at a rate of 2.3 percent per annum,^{11/} a situation attributed largely to land clearing for subsistence agriculture, and wood energy production to meet the needs of the country's rising population. The forest cover along Malawi's major rivers was estimated to stand at less than 2%. The 1990's also saw the complete liberalisation of the tobacco production. This added a total of 200,000 new tobacco farmers and this brought further pressure on deforestation as farmers cleared more land and used trees for curing and building structures.

External Shocks

External Political Conflict

144. The decade also started at a time Malawi was still coming to terms with the effect of the war in Mozambique. Over a million refugees were in Malawi and this created enormous pressure on land, the consequence of which Malawi continues to face to date. The deforestation that occurred led to the continued loss of topsoil which is being washed down at an estimated rate of 29 metric tons per hectare per year.¹²

145. The war in Mozambique throughout the first half of the 1990s, continued to disrupt Malawi external routes. As a landlocked country dependent on overland movement of exports and imports, Malawi's transport network and its connections to neighbouring countries are of the utmost economic importance. The shortest, cheapest, trade routes are to the Mozambican ports of Nacala and Beira. Until 1982, around 95% of Malawi's trade passed through those two ports, but throughout the 1980s and early 1990s the Mozambican civil war severely

¹⁰ Malawi Government: Mid-Year Economic Review 1998-99

^{11/} State of the Environment Report - Environment Affairs Department 1998

¹² World Bank 1992

disrupted these external trade routes, forcing most export and import traffic to be routed through distant ports in South Africa and Tanzania. The CIF margin, at 40% is one of the highest in the world.

Withdrawal of Donor Assistance

146. The first years of the decade saw an outbreak of political and labour unrest in the country. The deterioration of governance and rule of law during the period led to donor countries suspending non-humanitarian balance of payment support. Malawi is highly dependent on donor assistance, therefore vulnerable to any withdrawal, reduction or even delay in disbursement. Over 80% of the government development budget was being funded by donors. According to a latest estimate, for every MK6 the government uses MK1 is borrowed or received as grant money.

Economic Shocks

147. Malawi's export sector was highly vulnerable for several reasons. Key to these was the dominance of tobacco accounting for more than 50 per cent of total exports in the export basket. In addition to being highly concentrated, Malawi's share of exports in total world trade was very small as its share of world exports was only 0.01 percent in 1994. Even tobacco was only 5.6 per cent of the world trade. This suggests that Malawi could not influence world prices even in commodities that dominate its export sector. This makes the Malawi export sector even more vulnerable to terms of trade shocks.

Consequence of the Shocks

148. Economic performance deteriorated rapidly during the first half of 1990s owing to the effect of these shocks. In 1994, GDP contracted by more than 10 per cent. Between 1992-94, the terms of trade losses and the droughts especially cumulatively caused an income loss equivalent to 25 per cent of annual GDP.

149. Drought caused the country's staple food, maize production levels to fall to just 1.35 million tons in 1996/97, but output recovered to 1.76 million tons in 1997/98. In 1992 and 1994, the drought led to maize production levels falling to just over 0.6 million and 0.8 million tons respectively and also leading to a significant shortfall in government revenue and a large increase in expenditure emergency food imports and related social services.

150. In aggregate terms, Malawi was on average losing 160 million tons of soil per year and the cost associated with soil erosion was estimated at MK1,115 million per year. This corresponded to 8.1 % of the country's GDP in 1994.

151. Malawi had difficulty retaining adequate foreign exchange levels in the early part of the decade because of the adverse effects of drought and the freezing of non-humanitarian aid, gross official reserves fell substantially during the 1992-94 period to an average of less than one month of imports. Careful management by the central bank helped build reserves up gradually from just \$43 million at the end of 1994 to \$226 million by the end of 1996, according to the IMF, the

equivalent of more than four months' of import cover. However, reserves deteriorated to \$162 million by the end of 1997 and dropped below \$150 million in early 1998, setting the stage for the depreciation of the Kwacha later that year. The reserves were slowly recovering, and reached \$254 million by the end of 1999 representing 5 months of import cover.

152. The series of shocks also contributed to the exchange rate instability. Following the floatation of the Malawi currency in 1994, the Kwacha depreciated substantially as the exchange rate re-aligned to market forces. From the beginning of 1995, however, the Kwacha achieved a remarkable degree of stability and remained relatively constant until mid 1997. In the second half of 1997 the Kwacha began a slow slide, reaching MK26:\$1 by August 1998. Then, over a four-day period in late August, the Kwacha plummeted a further 37% to hit MK42.7:\$1. Following the resumption of IMF assistance and a rebuilding of reserves, the currency stabilized in the final quarter of 1998 in the MK43-45:\$1 range.

153. Disruption of transport routes through Mozambique doubled CIF costs of imports. Transport costs thus increased by \$50 million to \$75 million per year, with insurance and freight costs rising from around 20% of the import bill in the early 1980s to 40% by the late 1980s and only falling to 35% in the mid-1990s.

154. The reduced donor assistance led to a surge in fiscal deficit reaching to nearly 18.3% of GDP in 1993 fiscal year. The fiscal deficit was financed by a large increase in bank credit to government. Matched with concurrent substantial increase in credit to private sector and a tight aggregate supply situation, there was pressure on prices and external reserves leading to a decline in import cover from 3 months to only one month.

Opportunities in the new decade

155. Malawi's vulnerability to these shocks does bring an opportunity for innovative ideas, which could cushion the country from future shocks. A good case in point is the opportunity to increase growth in the agriculture sector through irrigation. One third of Malawi is water and for the period Malawi has been independent Malawi has to do more to put water resources to good and effective use.

156. Secondly, most of Malawi's arable land is used inefficiently and for maize production. There is an opportunity especially with irrigation to transfer use of land from maize production to other high-value export crops, whilst increasing productivity of maize production. This would reduce the number of farmers involved in maize production as well as the land dedicated for maize production whilst maintaining if not increasing the yield.

157. Thirdly, Malawi has learnt that if fiscal deficit gets out of hand, an economic vicious circle ensues. Through this experience, the country can now devise an early warning system that would guide government to ensure that the deficit does not become unmanageable.

4.0 EXAMPLES OF SUCCESSFUL BEST PRACTICES

MALAWI SOCIAL ACTION FUND (MASAF)

One of the major success stories of Malawi's development programmes in the 1990s is the Malawi Social Action Fund (MASAF). The programme was established in 1995 as a key poverty alleviation instrument designed to address community social needs. MASAF is a social Fund designed to finance self-help community projects and transfer cash through safety net activities. It is community oriented and demand-driven and thus depends primarily on the people's commitment for its success.

In 1995, the government obtained a loan from the World Bank equivalent to USD56 million to be used for the implementation of the MASAF project. The operations of the Project were successful and demand for funding was overwhelmingly high. As a result, in 1998, Government had to obtain a second loan from the World Bank equivalent to USD 56 million to implement the second phase of MASAF (MASAF II). MASAF II was designed to build on the success of MASAF I in reinforcing the spirit of self-help and continuing to deal with the country's pervasive poverty.

The following were the specific objectives of MASAF:

- providing additional resources and ensuring sustainable use of services targeted at the poor, vulnerable and marginalised social groups;
- promoting a new approach to development by direct involvement of communities in project preparation and management, while encouraging government agencies, NGOs and private institutions to assist a community's poverty alleviation efforts;
- transferring cash incomes through employment in labour intensive public works as a social safety net in targeted areas;
- supporting capacity building efforts involving all stakeholders in the different operational components of the Project through the provision of training, technical assistance and funding of qualitative studies to improve project delivery process.

MASAF Project is based on a number of principles:

- **Community Participation:** Communities are actively involved in decision making at all stages of the project cycle, which include project identification and preparation, implementation, monitoring and evaluation, and maintenance of completed projects;
- **Independent community project management:** a Project Management Committee (PMC), selected by the community is responsible for all decisions made on project matters.
- **Accountability and Transparency:** project management processes are designed to promote transparency and accountability.

158. In the last decade, Malawi's human capacity was used extensively in designing new policy measures and programs. However, there are a number of programs and activities that the Government and the private sector implemented that could be replicated in other countries as they have proved to be effective in as far as poverty reduction and sustainable human development is concerned. The two examples illustrated below in text boxes represent practices that will enhance the country's future self-reliance as well as increased agricultural productivity.

- **Partnership:** MASAF collaborates with relevant sectoral ministries , NGOs and other funding agencies with the aim of improving the standard of living of poor communities.

MASAF project is implemented by an institutional and management structure deliberately designed to promote effective participation of beneficiaries in project management to ensure capacity building and sustainable development.

An autonomous Management Unit was established and it reports to a Board comprising representation from Traditional leadership, NGOs, University, Government ministries and independent members from private sector with specific expertise.

MASAF has four components.

1. **Community Sub-Projects:** MASAF provides 80% -95% of the total costs of project and the community contributes 5%-20% for projects aimed at creating community assets e.g. schools, health facilities etc.
2. **Sponsored Sub-Project (SSP):** The SSP was designed to provide financial grants and technical resources for programs targeted at marginalised groups.
3. **Public Works Program (PWP):** Public Works Component is a safety net scheme targeting poor households and communities by supporting programs of labour intensive construction activities. The works generate significant employment at a minimum wage to provide self targeting for those who have no alternative income earning opportunities.
4. **Capacity Enhancement and Studies (CES):** This component is aimed at enhancing capacity at the MASAF, national, district and community levels. It finances training of national, regional and district agencies in MASAF procedures and systems. It also finances project related studies.

MASAF has been a major success not only in achieving its stated objectives but also in enhancing ownership and sustainability of the created assets by the communities. Communities from the on-set play a key role in the identification and implementation of activities.

As at October 1999 MASAF had funded 1,655 projects at a total cost of K1.6 billion (US\$ 35 million 2000). 1,220 projects were funded under the community sub-projects at a total cost of K648 million (US\$14.4 million). A total of K393 million was used for 435 projects under the Public Works Program whilst the Community contribution on all the funded Community Sub-Projects totalled K130 million.

Among the achievements of the Community Sub-Project a total of over 1,200 classrooms; over 1,400 teachers houses and over 1,500 bore-holes were constructed during the period. Over 7,000 community based committee members benefited from training. As a MASAF policy, 40% of those trained are women

The CSP has also contributed to the creation of new bridges, Health units, postal agencies, water kiosks etc.

The Public Works Program has generated significant employment to most of the rural population with no alternative income earning opportunity

A total of 165,000 jobs were created as a result of the Public Works Program during the period with women contributing about 31% of the total workforce.

A number of community assets were either rehabilitated or new ones constructed. These included community dams and road-network. 86% of the projects were in road-network whilst 11% of the projects were in afforestation, which is a response to a major depletion of trees throughout the country. The remaining 3% were projects in water conservation, mostly in the construction of community dams. The community dams will contribute greatly to small-scale irrigation especially for winter crops.

5.0 PROGRAMME OF ACTION, 2000-2010

159. The overall growth of the Malawi economy has averaged 4% since 1990, only marginally above the average population growth of about 3% per annum during the same period. Malawi's deepening crisis emanates from erratic agricultural growth, a decline in industrial output, poor export performance, increasing debt and deteriorating social indicators.

160. Another factor that have impacted per capita growth is the low return on investment. Malawi's business operating costs are normally 50% to 100% above those in South East Asia mainly due to heavy public sector involvement in the provision of economic infrastructure and these services are managed inefficiently.

161. The challenge now is for Malawi to reverse the present state of decline. The potential is there and great results can be achieved through proper utilisation of the resources of water, land and people.

Shared Vision

162. The shared vision for Malawi as captured in the Vision 2020 document is as follows:

“By the year 2020, Malawi as a God-fearing nation will be secure, democratically mature, environmentally sustainable, self-reliant with equal opportunities for, and active participation by, all having social services, vibrant cultural and religious values and being technologically driven middle-income country”

Common Mission

“To attain a balanced, broad-based and sustainable development through economic growth, development, efficient utilisation of the human capital, development of economic infrastructure, observance of good governance and protection of the environment and natural resources”.

163. This common mission entails that the Malawi economy must be fast-growing, competitive, innovative and knowledge-based. The major efforts in the plan period will be to eradicate hard-core poverty and transform the country into a middle-income country with a desired per capita income of at least US\$500 by the year 2010.

Strategic Issues

164. A number of strategic issues have been determined after examining closely the strengths, weaknesses and opportunities. The identification of the strategic issues will form the basis of the courses of action.

....

.The economic environment.....

- With the onset of globalisation, the economic environment is getting tougher and more challenging. Thus, Malawi has to survive in a highly competitive world.
- The global economy is more open than ever before. Investment capital is flowing to the most profitable destinations throughout the world. In a similar manner, there is increased competition among countries – some of them have a low cost-base – which can produce sophisticated goods and services. Their economies of scale give them a major advantage over smaller nations such as Malawi.
- The regional integration initiatives are taking root. This will enable some of the countries that are strong in some sectors to displace the existing inefficient producers of goods and services in Malawi.
- Some of the neighbouring countries have registered formidable successes in the 1990's and are strong competitors for foreign direct investment.
- Financial inflows and support from the multilateral institutions have been erratic in the 1990's due to the numerous conditionalities attached to funds disbursements.

..... when Malawi makes good of the strengths.....

- Malawi has a substantially good record of industrial relations.
- Malawi has a strong past record of educational attainment, which is critical for a knowledge-based economy.
- Malawi has a youthful population, which will remain young and has the potential to adapt to better and faster technological changes and new skills needs.
- Malawi has less social regulation on businesses.
- Malawi has enjoyed peace and stability since independence in 1964.

.....Get rid of the weaknesses.....

- Many industries are in activities that have poor growth prospects. As a result, there has been increased de-industrialisation. The balance needs to shift to high-growth and high value-added sectors.
- Education standards have deteriorated by international standards and technical education is not providing the level of skills relevant to the industries that have potential for growth.

- Firms spend too little on research and development such that they are less likely to innovate than the competitors.
- The economic infrastructure is inefficient.
- The macroeconomic environment is unstable and unpredictable.
- Human capital development is weak and inappropriately utilised.

...Malawi's future prosperity and the key strategic objectives...

165. A background of peace and stability is crucial in setting the pace for national prosperity and will provide the best platform for growth until 2010 and beyond. Therefore, the key strategic objectives for Malawi will include the following:

- To be a fast-growing, competitive, innovative and knowledge-based taking advantage of the numerous opportunities.
- To achieve ambitious and challenging targets in education, health, economic infrastructure for social and economic progress measured against regional and international benchmarks.
- To change the mind-set and attitudes of Malawians to believe in themselves. {To emerge as a success in the region.}
- To achieve a higher standard of living with a skilled, creative and well remunerated workforce in modern high-value and innovative businesses.
- To improve entrepreneurs skills and develop indigenous businesses and attract high quality inward investment.

....To achieve a prosperous future, Malawi needs to concentrate on key themes and cornerstones.....

- Project a positive image of the country in such a manner that everyone in the country must have a stake in the economic success. The benefits will have to be fairly shared. There will be need for lasting partnerships in the drive to achieve common goals and social cohesion.
- Strengthen the culture of enterprise to unleash the potential of the private sector as wealth creators. Government's role in the industry would be restricted to encouraging self-reliance and exposure to the disciplines of the market.
- Re-orient business and the society to be more outward looking in the wake of regional integration and globalisation initiatives. There will be need to learn from the best worldwide.

- Prepare all stakeholders for the applied knowledge-based economy of the future with better health and education; higher skills; commitment to research and development and innovation.
- Recognise that self-help and self-reliance are key to achieving success.
- Improve the quality of trained manpower and its utilisation.
- Improve the quality of economic infrastructure.
- Achieve macro-economic stability and growth.
- Ensure sound governance and shared responsibilities.

...Action will be taken on them.....

166. A number of studies have been undertaken on major issues but little action has been taken. There will be not quick fix solutions to Malawi's social and economic problems. Instead there will be need to design solutions that will lead to a total structural transformation of the Malawi economy in a sustainable manner. There will be commitment to achieve the shared vision as long as the stakeholders feel they will enjoy the benefits of equity and social cohesion and more private sector involvement in the generation of wealth.

Equality and Social Cohesion

167. Total commitment by the public and private sectors to build an economy based on the principles of equality of opportunity and social inclusion have been incorporated in the development agenda through the Vision 2020. More opportunities will be offered to under-represented groups including women and people with disabilities for them to play their equitable share in the development of the economy.

168. This will require a significant re-orientation of the existing institutions to ensure an efficient delivery system that is backed by a high-powered research capability, to agree on formulation and implementation of economic development policy.

Applied Knowledge-based

169. There will be need for greater integration of economic activities and educational policy and more collaboration between business and the education and training systems in delivering the skills and capabilities needed by business. Some of the measures will entail tackling weaknesses in vocational and technical education by giving the education sector a clearer focus and by creating technician qualifications; raising the prestige of technical education vis-à-vis the academic route; ensuring that students have a better appreciation of the attractions and potential of a career in industry by involving experienced business people in an enhanced careers guidance system and by giving trainee teachers direct experience of industry.

170. Measures will be taken to ensure that Malawi must upgrade the telecommunications infrastructure and build enhanced capacity in information and communication technologies to match with the demand of e-commerce.

Enterprise and Outward-looking

171. Enterprise development will involve raising the prestige of business as a career and providing role models to attract our best talent into the wealth-creating sectors. In addition, there will be need for additional support measures in the form of re-balancing the incentives to existing industries to focus on export and innovation-oriented companies with high value-added output; encouraging the use of private equity finance generally; creating Venture Funds to provide capital to smaller firms; mobilising informal investors; and increasing the rewards of success in industry.

172. Action will be taken to ensure that the share of international transportation enables fast, cost effective and efficient links with regional and overseas markets

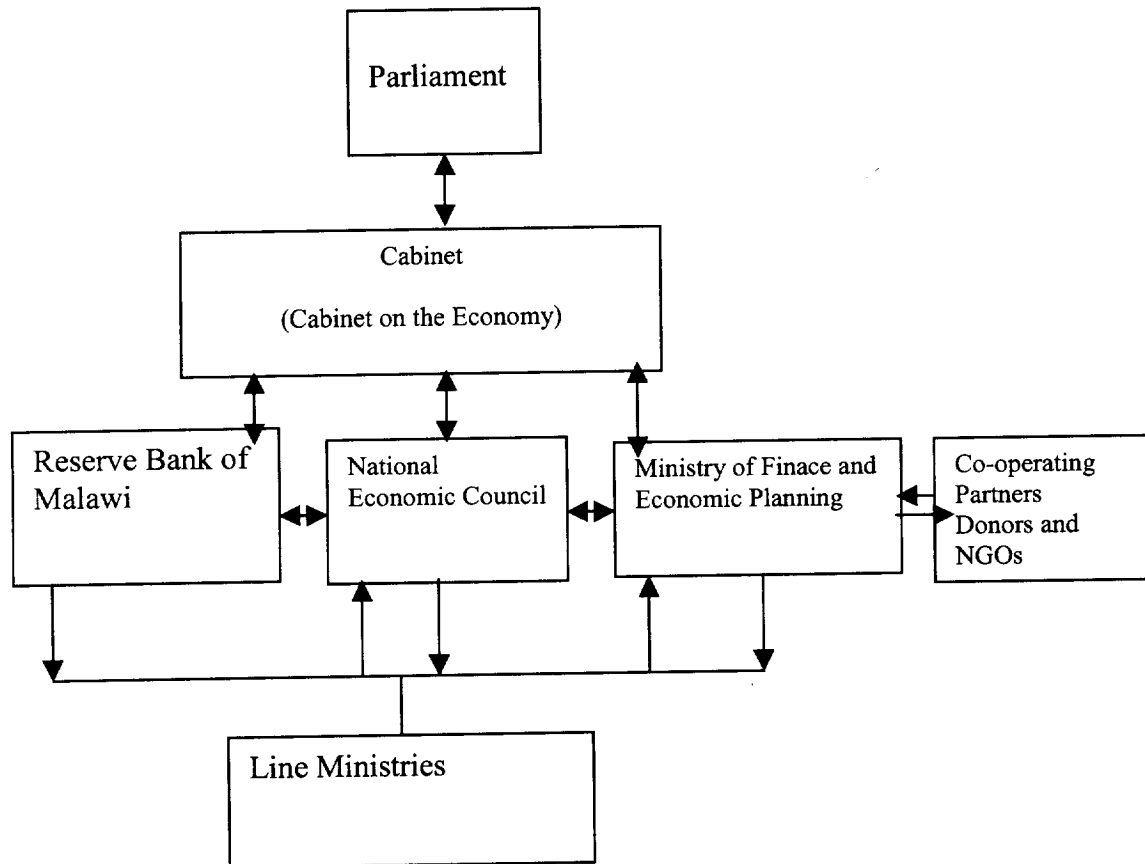
Self-reliance and Self-help

173. Self-reliance and self-help will be guided by the principle of achieving more with the available resources. Malawi will have to take control of its own destiny through the creation of new mechanisms for partnership between the private and public sectors in pursuing the country's economic goals.

...Implementation.....

174. Malawi needs to institute pragmatic and flexible economic strategies, more especially by improving resource mobilisation, increasing efficiency in its utilisation to raise productivity and enhancing technology development with the major sectors of the economy. Sustained long-term development will be achieved through increased agricultural productivity, deepened and widened industrial base and a developed services sector. Partnership and consultation will underpin the successful implementation of the strategies because it will ensure consensus on the direction of the strategy and an acceptance by all involved in its delivery. The roles of the various stakeholders in the delivery will have to be clearly defined to avoid duplication and wasteful competition. The public-private sector consultation, therefore will be redefined and strengthened to provide strong and smart partnership among the various stakeholders.

FIGURE 5.1: FRAMEWORK FOR THE FORMULATION AND IMPLEMENTATION OF DEVELOPMENT AGENDA



Plan Thrusts and Targets¹³

	Benchmark	Current	Target (2010)	Desired (2010)
Macroeconomic Targets				
<i>GDP annual growth per annum</i>	6.0%	2.6%	8.5%	10.0%
<i>GDP per capita</i>	US\$500	US\$200	US\$450	US\$500
<i>Investment / GDP</i>	35%	13%	25%	35%
<i>Inflation</i>	5%	30%	5%	5%
Social Targets				
i. Health				
<i>Health expenditure per capita per annum</i>	US\$12	US\$2	US\$12	US\$7
<i>Infant mortality</i>				
<i>Child mortality per thousand births</i>	69	133	90	90
<i>Under five mortality per thousand live births</i>	104	225	150	150
<i>HIV prevalence</i>		13%	10%	1%
<i>Doctors per 100,000 people</i>	108	2	5	50
<i>Nurses per 100,000</i>	175	6	12	100
<i>Maternal mortality per 100,000 live births</i>	321	620	500	500
<i>Life expectancy at birth</i>	63 years	42 years	45 years	52
ii. Education				
<i>Net primary enrolment</i>		95%	99%	100%
<i>Tertiary science enrolment as a % tertiary</i>		18%	25%	30%
Economic Infrastructure				
<i>Telephone cost per line</i>	US\$ 1,000	US\$ 4,900	US\$ 1,500	US\$ 1500
<i>Telephone lines per 1000 people</i>	100	4	49	54
<i>Number of Working lines</i>		40,000	150,000	400,000
<i>Average recorded waiting time in years</i>	.7	10	3.5	.3
<i>Electricity penetration</i>		% 4	% 10	% 25

¹³ NOTES TO THE THRUST TABLE

1. The estimates on the macroeconomic targets are based on the aspirations of Malawians as contained in the Vision 2020 document.
2. Health targets are based on the 1999-2004 Health Sector Plan.
3. The net primary enrolment is estimated to reach 100% because of the programme for free primary education.
4. Telephone costs per line will have to be reduced to internationally acceptable standards. In addition the telephone penetration levels will have to increase to keep pace with the demands on an information rich society. This will require substantial re-organisation and restructuring of the Malawi Telecommunications Limited to make it more efficient and customer driven.
5. Access to electricity has to considerably improve from the current levels of 4% of the population. This will require massive capital injection into the generation capacity, transmission and distribution networks.

Social Services

175. The quality of the basic social services has declined in Malawi. Therefore, it is important to ensure that more resources are allocated to basic social services.

Health

176. Programmes in the health sector are aimed at achieving a standard of health that will enable Malawians to enjoy a high quality of life. It implies a longer life expectancy, decreasing rate of infant mortality and diminishing incidence of infectious diseases. The thrust of the health programmes will centre on equitable distribution of efficient health services and facilities in the urban and rural areas as well as effective collaboration health and non-health programmes.

177. Life expectancy at birth in Malawi was estimated at just 44 years in 1998. Child mortality stands at 234 per 1000 live births. AIDS and other illnesses such as malaria are expected to exacerbate the situation. Health outcomes depend on at least six factors: incomes, education, information, health services, water supply and sanitation. Studies of household data show that both education and specific information about the causes of illness significantly reduce child mortality. Using international data, it has been shown that child mortality responds to the effects of technical progress in preventive and curative care over time, and to female education and income growth within the economy.

178. Improving the health of the population is a priority objective of the Government of Malawi. The Health Sector Strategy sets targets of reducing child mortality from 133 to 90 per thousand, maternal mortality from 620 to 500 per 100,000 live births, and to reduce HIV prevalence by 25%.

Education and Skills

179. Education increases incomes and economic growth, and it offers an intrinsic benefit in itself. The policy of free education introduced has increased enrolment enormously from 1.9 million in 1994 to 3.2 million in 1999. During the next ten years, the main focus in primary education will no longer be increasing quantity, but maintaining quantity while enhancing quality. It is generally agreed that the quality of education in Malawi has declined seriously between the mid-1980s and the late 1990s, and the increased enrolment is now straining the system. The heavily burdened primary schooling system cannot meet the immediate demands for classrooms, teachers, and teaching/learning materials. Educational policy thus faces two central challenges of how to keep the increased number of children in school and how to improve and maintain quality given the expansion of the system.

180. The education and training of the workforce is recognised as one of the most significant factors in developing a successful economy. The education system should maximise its value to society by producing a workforce that is appropriately skilled and adapted to meet the emerging needs of the economy. It should be capable of providing opportunities to update current skills and to acquire new ones as the changing economic environment requires.

181. Education and training programmes will be expanded and improved, not only to equip individuals with appropriate knowledge but also produce responsible citizens. The thrust of the programmes will be to improve the quality of education and training as well as to achieve a more efficient delivery system so as to enable the low-income groups to have greater access to education and training.

Primary

182. Government now faces the challenge of encouraging children to remain in school, and to acquire relevant skills for adult life. Primary education will be the government's main priority considering that this particular sub-sector has the highest social returns. At the primary level, the major focus will be:

- To achieve universal primary school enrollment rate (including poor households);
- To improve quality by increasing budget allocation for child learning and teaching materials;
- To enhance and strengthen teacher training programs;
- To reduce drop-out rates and raise completion rates; and
- To raise the cognitive skills of primary school graduates.

Secondary and Higher Education

183. For secondary and higher education, one of the most important issues is for Government and industry to develop strategic guidance for those aspects of education and training on which economic growth will depend. Government is clear on the position of the Malawi economy in future. The specific sectors which show signs of growth world-wide are automation, information technology, electronics, biotechnology, research and development, manufacturing, tourism, fashion design, among others. Such a strategic product portfolio is necessary to focus the direction of education and training in the area of specific activity related skills and knowledge. International comparisons seem to suggest that economic growth (whether driven by domestic investment or foreign investment) has been catalysed by such a strategic focus. The existing structures and responsibilities have neither delivered a strategic economic vision translated into education and training nor have they been effective in coping with immediate skills constraints. Until the two issues - the strategic vision and its supporting operationalisation - are effectively addressed, Malawi is unlikely to be competitive. Therefore, Government will play a strategic role to encourage higher education to respond more positively than in the past to economically valued skills needs.

Vocational Training

184. Vocational education has not been given much attention and yet it has a major impact on the competitiveness of labour. There is need to embark on an extensive vocational training program to increase its impact on national development.

Career Information

185. There is great concern about the quality and fragmentation of career guidance in Malawi. This is mainly attributed to societal prejudice, inadequacy of vocational qualifications, and others that form the backdrop to career guidance. Many young people drift through education into unknown career territories influenced in an intuitive way by peers, parents, teachers and media.

Major Actions

- Develop a clear strategic focus for business development based on Malawi's strategic strengths or potential. This in turn must influence education and training policy, funding and delivery mechanisms in the relevant areas. The educational issues of relevance and flexibility must be addressed by this policy.
- Establish collaboration clusters of schools, businesses and colleges to deliver locally relevant but nationally guided education and training outcomes, facilitated by an enabling organization. Funding for clusters must be adequate to fulfil their functions.
- Develop an attractive and valued vocational education.
- Transform schools and universities approach to education to embrace broader curricula of greater intrinsic value. The approach to curriculum development would involve all the relevant stakeholders to ensure effective operationalisation of policy decisions.
- Transform the current system of careers to enable properly informed decision making on the part of students, parents, teachers, employers and Government.

Infrastructure

186. Infrastructure is of particular importance to Malawi. This includes telecommunication, transport and logistics, energy and physical environment. The major programmes will include rehabilitation of main roads, development of rural access and feeder roads, modernisation of the railroads, upgrading and increasing the capacity of airports, as well as improving and expanding of telecommunication services. The infusion of the public investment resources will also offer significant opportunities to private sector involvement in the construction, maintenance and management of infrastructural facilities.

187. The decline in emphasis on traditional transport infrastructure is being matched by an increased reliance on telecommunications. Most economies are seeing a rise in the share of services in economic activities. There is also an increasing awareness that many services (e.g. call centres, financial services) are not as tradable as traditional manufacturing due to technological developments. However, it is expected that growth in world trade is likely to be dominated by such trade in the future. Therefore, a highly developed communications infrastructure will be essential to fully reap the benefits.

188. Traditional economic development strategies placed great emphasis on providing strong transport infrastructure linkages as part of a package to attract inward investment. Well developed communications linkages to other regions are a necessity for indigenous firms if they are to compete successfully in a global market and to participate fully in the wider networks which promote research and development and innovation.

189. The economic infrastructure – especially transport, communications, energy and water networks – will be a major factor in shaping the development of the Malawi economy by 2010. With the regional and world economy in a process of continuous change, any credible strategy concerning future infrastructure development should seek to reflect, and preferably pre-empt, the changing needs of industry. Major steps have been taken to involve the private sector in the provision of infrastructural services.

Roads

190. Historically, one of Malawi's perceived economic weaknesses has been that it is landlocked, implying that it will be more difficult for manufactured products to compete in world market. However, the share of manufacturing in most modern economies has shown a tendency to decline in recent years. Within the manufacturing activity, there is an increasing shift away from more traditional areas toward sectors where the value of output will be determined by the extent that it incorporates the highest standards in design and technology and how it reacts to the increasing specialisation according to customer needs.

191. Global changes may reduce the importance of overland transport. Despite these anticipated global changes, overland transportation by rail and road will still play a pivotal role in the competitiveness of Malawi's goods and services. The maintenance and development of a top quality road network is, therefore, essential in order to provide for the speedy transportation of goods and persons both internally and to/from the seaports. Although the extent of the current network is, by and large, insufficient to meet the present and likely future need, the emphasis will be placed on improving the quality of the network.

Rail

192. The rail network in Malawi is not extensive, with many parts of the country having no rail service. The existing railway line network benefited from considerable investment in the 1970's. The importance of the rail lies in the linking of Malawi to the seaports of Nacala and Beira leading to a reduction of international transport costs which are currently estimated at almost 40% of the landed costs of imported goods. The Central and East African Railways has taken over the operations of Malawi Railways (1994) and it is expected that involvement of the private sector would provide an efficient alternative for the movement of traffic. There is need to strengthen regulatory mechanisms to protect consumers and ensure effective complementarities between the rail and other modes of transport.

Telecommunications

193. The telecommunications sector has undergone astounding transformation in the 1990's. Two operators have entered the GSM mobile phone network and several Internet service providers have been registered. Plans are quite advanced to privatise the public switching telephone network, Malawi Telecommunications Limited.

194. It is widely recognised throughout the world that excellent telecommunications is a key infrastructure requirement of any economy. Huge amounts are being spent on telecommunications infrastructure developments across the globe. But the existence of physical infrastructure is only one side of the story. The services offered as a result of the infrastructure, the geographical coverage, pricing, the ability of the consumer to use the services and the availability of a suitably trained workforce are all-important factors for a developing electronic economy.

195. In view of Malawi's geographical position, the need for state of the art telecommunication infrastructure is even greater. With the on-going liberalisation and privatisation in the telecommunications sector, the benefits of more private sector involvement are beginning to be felt.

Energy

196. Competitive economies need energy policies that ensure that adequate and secure supplies of energy are available at affordable prices to all sections of society. Energy is essential to the quality of life and to provide the power needed to produce the goods and services needed by society. Energy must also be provided on a basis, which is sustainable and does not damage the environment.

197. Therefore, Government will put in place an energy policy that will ensure that the industry operates and develops in a way, which furthers national interest.

Government has indicated its willingness to engage in and make decisions about fuel diversity and cross-border potential of energy markets in the region.

198. In theory, privatisation empowers the private sector to make investment decisions. In practice, a number of key investments can only be possible because of the participation of the state. These are strategic decisions, which can only be made by Government and given effect by some form of public-private partnerships.

199. The vision for ten years, hence, should be of an energy industry that is successful - that is, one that is meeting the expectations of customers, shareholders and Government. It is evident that harmonisation of interests and aspirations implies a radical departure from the way in which the energy industry is structured at present. Within a restructured industry the Energy industry must be restructured with a view to reduce energy costs without expropriating shareholder value. In addition, competition or regulation must lead to cost reductions as reflected in prices.

Major Actions

200. Stakeholders will need to focus on the following key areas:

- ❑ A clearly enunciated energy policy on the part of Government, shaped within a broad economic, environmental and social policy perspective, which sets the direction and provides the framework within which these things can happen.
- ❑ A system of regulation which secures maximum competition in the interests of consumers.
- ❑ A stable framework for private investment that would lower costs.
- ❑ Public investment, where this is needed, to enable projects of strategic significance to proceed must be applied for transparent purposes and in a way that safeguards against distortion of competition.
- ❑ Promulgation of an appropriate legislation for concessioning public enterprises.

201. Developments at regional level - COMESA and SADC - will have implications for local infrastructure policies. The initiatives to introduce the free trade area in COMESA and preferential trade area in SADC will require facilities to cope with an increasing volume of transport of both goods and people. It will be essential that the economic infrastructure does not impose any further cost penalty on local firms while the telecommunications sector helps facilitate a shift to higher value-added products.

202. In summary, Government has to explore more ways of providing essential infrastructure services. Some of the options to be looked into by Government include rehabilitation of the facilities; increasing private sector involvement in

areas which were hitherto the domain of the public sector; and improving cost recovery from public services.

Economic Sectors and Industrial Activities

Agriculture

203. In the 1990's, the sector contributed more than 70% to exports, nearly two fifths of GDP and over 90 per cent of total employment. The anticipated rapid growth in the manufacturing and services sectors and the increasing importance of the agro-processing industries will require complementary growth in agriculture for reliable and sufficient supply of inputs and raw materials from the agricultural sector. The growth of the agricultural sector will be driven by a more commercial approach that emphasises efficient utilisation of resources through more private initiatives. While the public sector will continue to provide such facilities, the contribution of the private sector will be enhanced.

204. The basis for placing Agriculture as a priority sector follows conclusions reached after studying the role and impact of the sector during the past decade. These include the following:

- Agriculture plays a central role in economic development;
- Economic policies that are not biased against primary production are important;
- Public and private investment in infrastructure, technical development and credit, which are essential for modernising production and improving competitiveness are needed; and
- The role of private enterprise in the sector's performance, in the provision of services and in co-ordination with the rest of the economy is increasing.

205. Given these conclusions, the country will strive to attain a number of goals in the agriculture sector including the following key ones:

- Bring down real food prices;
- Forge important economic linkages in chains of production, both backwards¹⁴ and forward¹⁵;
- Diversify agriculture production through increased production of Cassava, rice, Pigeon peas, beans and Soya.
- Increase employment and income; and
- Ease pressures on land use through productivity increase.

¹⁴ industries producing seeds fertilizers and machinery

¹⁵ processing marketing and transport

206. Priority will be given to the re-orientation of the smallholder sub-sector towards greater commercialisation and international competitiveness. The commercial approach to agriculture will require greater supply of trained personnel and management as well as organizational support. The realisation of growth in agriculture will depend on the availability of adequate supporting infrastructural facilities. The inadequacy of essential farm infrastructure such as access roads to rural areas, power supply, drainage and irrigation, storage, grading and marketing network facilities, will discourage farmers from producing food items with marketable surplus.

Major Actions

- Actively promote horticultural and floriculture exports.
- Establish a research and advisory service to support agriculture diversification and irrigation development.
- Increase support for agriculture credit.
- Accelerate the switch from subsistence to commercial production for a large number of smallholders.
- Promote agro-based industries that are closely located near the sources of raw materials.
- Promoting a more efficient and sustainable use of land by introducing measures to reduce soil erosion.
- Promoting the management of forest and wildlife resources by involving the local populations and increasing their returns in a sustainable manner;
- Promoting a more equitable and efficient land allocation by improving the land and tenure registration process.

Program Design

207. The economic and technological changes of the last decade highlight the growing interdependence of different areas of economic activity, consequently, investment projects must be based on an integrated view of agricultural issues in relation to the rest of the economy. There will, therefore, be a need for sectoral studies to serve as a basis for designing strategies for action.

Manufacturing

208. Several policy recommendations were implemented during the 1990's to enhance private investment and to develop a more focussed policy implementation. There were no specific sectors earmarked for active promotion, the result of which is that it has been difficult to measure the effectiveness of the policy measures on private investment.

Generating Momentum for Growth

209. The Manufacturing sector is targeted to grow at 5% per annum during the plan period. As a result of the anticipated expansion, the sector is expected to contribute almost 25% of GDP by 2010. Government will put in place measures to accelerate industrial restructuring, technological upgrading, human resource development and industrial linkages that will ensure greater level of domestic value-added to contribute to growth. Other measures to promote manufacturing investment will include the provision of a conducive environment and the improvement of infrastructural facilities.

210. The thrust during the next ten years will aim at promoting new sources of growth so as to strengthen and diversify the industrial base. New approaches will be adopted to target and focus on the development of export-oriented, high value-added, high technology industries with greater assistance and support from domestic research and development. Thus industrial policy will aim at catalysing capital intensive and technologically advanced industries producing better quality and competitive products that are integrated with the regional and international markets. The following sectors and sub-sectors are earmarked for active promotion:

<i>Resource-based</i>	Mining, agriculture & agribusiness, wood and wood products, hospitality
<i>Labour-intensive</i>	Apparel and textiles,
<i>High value-added</i>	Electronics and electrical, fashion design, medical accessories and pharmaceuticals, information technology
<i>Services</i>	Financial services

Investment

211. It is estimated that the amount of investment required to achieve the targeted growth rate for the sector will be about US\$1.8 billion. Of this, 45% will be foreign direct investment and the balance from domestic investment.

Competitiveness of Products

212. The expansion of manufacturing products and exports will be facilitated through improvement of the marketing and information networks and penetration into new markets. In addition, inefficient industries will be rationalised, restructured and modernised. Selected industrial sub-sectors will be restructured and modernised to improve capacity utilisation, level of technology, cost competitiveness and productivity.

Development of Small-scale Industries

213. The development of small-scale industries will be key to a more dynamic and competitive industrial sector because of their supportive and complementary roles. Emphasis in the plan period will be placed on improving the capabilities of the small-scale industries to supply the required production inputs of the larger enterprises and also penetrate the export markets.

Major Actions

- Identify resources for industrial restructuring.
- Identify resources for industrial estate development to ensure the development of specialised industrial estates, especially for small and medium scale industries and high technology industries.
- Allocate adequate resources for the development of cottage industries.
- Allocate adequate resources for training and consultancy services to promote entrepreneurship development and enhancement of the skills of the workforce, especially in vocational and technical training.
- Establish a productivity centre;
- Strengthen infrastructure necessary for manufacturing sector;
- Formulate and implement the Micro-finance policy to increase accessibility to credit, savings opportunities, and financial services to low income people;

Tourism

214. The share of tourism to GDP has not been clearly quantified. Earnings from tourism recorded strongest growth in the 1990's. Most of the tourists to Malawi come from neighbouring countries and the region. Expenditure per person is quite low standing at nearly K1,700. This is an indication of either the quality of tourists or the poor data capture on tourist expenditures.

Tourism is expected to achieve the following targets:

- Raise tourism revenue to GDP;

- Create jobs;
- Diversify tourism sources; and
- Develop Malawi as an attractive location for tourists.

215. By 2010, Malawi's Tourism should be positioned in high-growth, upper-ends of the tourism market targeting segments of the markets which are highly mobile and less prone to changes in the global economy. The future emphasis of tourism in Malawi should be based on the following guiding principles.

- Increase in revenues and yield rather than tourist numbers;
- Upward pressure on quality of product and services; and
- Securing a better spread of demand throughout the year.

216. In summary, the main thrust to achieve tourism goals must be based on developing scale, environment management, product positioning and segmentation and image promotion. Allocation of resources should be channeled to preservation of national/historical heritage, tourist accommodation, environmental and cleanliness/beautification programmes, cultural product development, facilities and infrastructure.

217. Tourism not only creates multiplier effects and linkages in the economy, but also fosters national integration and unity. In promoting tourism, the religious and cultural values of the country will be fully respected and protected. Close collaboration between the private sector and public sector will continue to be fostered in the formulation and implementation of tourism development programmes.

Conclusion

218 The Success of the Program of Action will depend on the impact of both endogenous and exogenous factors outlined in the report. On the endogenous factors, observance of good governance has a number of trickle down effects especially its impact on fiscal discipline, which would stabilise the Macroeconomic situation. Secondly, generation of domestic revenue will be crucial to be able to support the poverty reduction strategy.

219. Thirdly, the majority of the people live in the rural areas and to reduce poverty, the people will depend on continuous increased productivity of their natural resources. Reduction of environmental degradation will therefore be a crucial challenge in achieving success of this Program of Action. The ability of Government to design programs that will assist in preserving natural resources will greatly assist increased productivity of the rural assets.

220. Fourthly, on the external side, the ability of government to negotiate for more grant financing than loan financing will be crucial. Malawi has many challenges and as such success will depend on setting and getting the priorities right. The formulation of the Poverty Reduction Strategy Program which intends to prioritise development needs will provide an opportunity for government to refocus the country's future direction.

Box 2. Malawi: Macroeconomic and Balance of Payments Assumptions**GDP Growth**

- Real GDP is projected to grow by an average of 5.5 percent in the 2000-2002 period, 10 percent in the 2003-09 period and 8.5 percent in the 2010-2020 period.

Exports and Imports

- Volumes for traditional exports are projected to grow at an average rate of about 3 percent throughout the projection period; non-traditional exports are projected to grow at a rate of 6 percent per annum in the 2003-09 period and 4 percent per annum in the 2010-20.
- Import volumes are projected to grow at a rate of 5.0 percent per annum in the 2000-09 period and 3.7 percent in the 2010-20 period.
- The terms of trade are projected to improve at an average annual rate of around 0.7 percent per annum between 2000 and 2005, but are projected to deteriorate by an average of -0.4 percent per annum beginning in 2010.
- Official transfers are expected to average 5 percent of GDP in the 2003-09 period, and 4.5 percent of GDP in the 2010-20 period.

Capital account

- Around 90 percent of new borrowing is expected to be made on IDA terms which have a grant element of around 75 percent. The remaining 10 percent of concessional borrowing is projected to be from bilateral creditors carrying a grant element of 35 percent.
- Foreign direct investment is expected to average about \$30 million in the 2000-09 period, and \$50 million in the 2010-20 period.

NOTES

¹ The Human Development Index ranked Malawi at 161 out of 174 countries. In terms of national income, Malawi is amongst the world's 10 poorest at US\$ 180 per capita. Some two-thirds of the population live below the poverty line, defined as *the inability to fulfil ones nutritional requirements and to meet essential non-food needs equivalent to US\$ 40 per annum.*^{1/} Poverty is most prevalent and severe in rural areas with some 95 % of the poverty gap (the shortfall below the poverty line) is found in rural areas.^{1/} The highly prevalent poverty and heavy dependence on rain-fed agriculture makes the rural population highly vulnerable to the effects of any adverse climatic and environmental factors. In normal times, over 50% of the rural households experience chronic food insecurity which becomes pronounced in the pre-harvest period; attributable to small landholding areas, low production levels and low purchasing power among other factors.

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ANNEX I

TABLES

WORKING SET OF CORE INDICATORS

Table 1.1 Malawi – Core Indicators

<i>Poverty Incidence</i>		Sub-Saharan Africa	Low Human Development*
Population below income poverty line, less a dollar a day	42.1%		32.2 ¹⁶
Proportion in absolute Poverty	62.0%		
Inequality: Poorest Fifths share in National Consumption	-		
Child malnutrition (prevalence of underweight), 1990-1997	30.0%		39 ¹⁷
<i>Universal Primary Education</i>			
Net enrollment in Primary education (1996)	68.0%		
Completion of 5th Grade of primary Education			
Males (1980)	48.0%		
Females (1980)	40.0%		
Female adult literacy rate (1997)	43.4%		38.3%
Male adult literacy rate (1997)	72.8%		63.0%
<i>Infant and Child Mortality</i>			
Infant mortality rate (per 1,000) live births (1997)	170		65**
Under five mortality rate (per 1,000 live births)	292		95**
<i>Maternal Mortality</i>			
Maternal Mortality ratios (per 100,000 live births)	620		
Births attended by skilled Health Personnel			
<i>Reproductive Health</i>			
Contraceptive Prevalence rate (women aged 15-49), 1990-98	22%		
HIV prevalence in 15 to 24 year-old women			
Population with Access to sanitation (1990-1997)	97%		
Population with Access to safe water	53%		
Urban	97%		
Rural	52%		
Intensity of fresh water use			
<i>Environmental Sustainable and Regeneration</i>			
Biodiversity: Land area protected			
Energy Efficiency: GDP per unit of energy use			
Carbon dioxide emissions(1996) cubic metres	0.7 mn		

¹⁶ Refers to the population below poverty income line all developing countries

¹⁷ UNICEF 1998b

Seats in parliament held by women (% of total)	5.7		
Female administrators and manager (% of total)	4.8		
Female professional and technical workers (% of total)	34.7		
<i>General Indicators</i>			
GNP per capita (1998)	US \$ 200		\$233
Savings as a per cent of GDP (1998)	3.3		
Services as per cent of exports of goods and services	12.8		
Debt Servicing as per cent of exports of goods and services	24.0		
FDI inflows as per cent of GFCF (1996)	5.6		
Adult illiteracy rate age +15 (1997)	42.3		
Males	27.0		
Females	57.0		
Total fertility rate			
Life expectancy (years) at birth (1997)	39.3		
Males	38.9		56.7
Females	39.6		
Aid as per cent of GNP (1997)	11.1%		
Investment as per cent of GDP (1998)	12.2%		
Trade as per cent of GDP (1999)	69.6%		
Seats in parliament held by women (% of total)	5.7%		
Female administrators and managers (% of total)	4.8%		
Female professional and technical workers (% of total)	34.7%		

Source: Human Development Report, 1999;

* 1995

** 1996

Table 2.3 Commodity Composition of Exports and Imports (Annual Average) (%)

COMMODITY/ YEAR	1981/85	1986/90	1991/97
Exports (by commodity)	50.1	62.7	68.6
Tobacco	19.9	12.3	8.9
Tea	1.8	1.2	0.2
Groundnuts	0.9	0.8	1.7
Cotton	12.6	8.9	6.5
Sugar	14.7	13.6	14.2
Other exports			
Imports (by end use)	13.0	11.1	N/A
Consumer goods	12.0	15.8	N/A
Equipment	10.6	12.7	N/A
Transport	5.9	5.5	N/A
Construction	40.7	39.5	N/A
Industry	17.5	14	N/A
Final and Intermediate	0.3	1.3	N/A
Miscellaneous			

Source: Reserve Bank of Malawi, *Financial and Economic Review* (1998).

Table 2.4 Malawi: Export Concentration and Diversification Indices

Indicator	1980	1992	1994	1995
No. of Commodities Exported	47	35	47	56
Diversification index	0.926	0.923	0.921	0.899
Concentration index	0.490	0.704	0.696	0.680

Source: UNCTAD: *Handbook of International Trade and Development Statistics, 1994, 1995.*

Table 2.5 Malawi – Terms of Trade Index

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Imports										
Volume	104.0	118.2	118.2	93.4	100	85.9	114.4	143.3	134.3	
Unit value	474.8	503.3	654.3	695.1	100	181.4	179.2	192.6	285.5	
Domestic exports										
Volume	103.9	109.0	103.9	122.2	100	101.7	117.5	131.0	130.9	
Unit value	433.5	490.3	550.4	492.6	100	214.3	221.6	249.8	369.4	
	<i>changes</i>									
Commodity Terms of Trade	9.1	5.7	-16.6	-11.2	7.6	1.7	12.1	4.8	-9.5	-4.2
Income Terms of Trade	37.6	12.0	-17.4	14.4	2.0	28.9	14.3	13.9	-4.0	-10.0

Table 2.6 Malawi – Structure of the Manufacturing Sector – sub-sectoral growths

<i>Sub-Sector</i>	<i>1990</i>	<i>1994</i>	<i>1995</i>	<i>1996</i>	<i>1997</i>	<i>1998</i>
Agro-processing	48.5	35.0	36.7	35.1	35.9	30.2
Textile, Clothing, leather	8.8	6.8	5.1	4.8	6.3	7.1
Wood products, publishing	8.4	14.2	15.9	16.2	18.2	19.2
Chemicals, plastics, rubber	19.1	23.6	23.66	23.4	23.0	23.2
Non-metallic mineral products	5.6	4.1	3.5	3.0	2.4	3.2
Metal Products, machinery	6.9	13.6	12.8	14.5	10.8	13.8
Other manufacturers	2.7	2.8	2.5	3.1	3.3	3.3
Total	100	100	100	100	100	100
Annual average growth Rate	5.2		1.5			

Source: National Economic Council/ National Statistical Office

Table 2.7 Malawi – Private and Public Investment (% of GDP)

Year	Private	Public	Total
1990	8.5	8.0	16.5
1991	8.8	8.1	16.9
1992	6.7	9.4	16.1
1993	2.6	7.6	10.0
1994	11.6	15.1	26.7
1995	5.6	9.4	15.0
1996	5.8	5.1	10.9
1997	5.2	6.2	11.4
1998	6.6	4.4	11.0
1999	6.6	4.6	11.2

Source: National Economic Council, Economic Report (various years)

Table 2.8 Malawi: Projections in Public and Private Investment

Year	Private Investment		Public Investment	
	Moderate	High	Moderate	High
2001	14.11	15.3	5.9	6.8
2006	14.3	17.2	5.9	6.8
1997-2006	13.8	15.4	5.8	6.8

Source: World Bank, Accelerating Malawi's Growth: Long-term Prospects and Transitional Problems, September, 1997

Table 2.9 Malawi – Inward Foreign Direct Investment Stock

Year	\$ Million	% Of GDP	% of GDP –Sub Saharan Africa
1990	215	11.6	13.5
1996	267	18.2	21.8
1997	284	11.4	...

Source: UNCTAD, World Investment Report, 1998

Table 2.10 Malawi- Competitiveness Index

	Competitiveness	Improvement	Optimism (1997-1999)	Trading Opportunity
Malawi	-0.43	10.39	12.6	4.33
Mauritius	0.87	13.0	11.27	6.02
Botswana	0.54	9.6	8.99	4.57
Namibia	0.43	10.02	6.99	5.19
South Africa	0.34	9.22	3.61	5.38
Zambia	-0.09	13.35	15.06	4.13
Tanzania	-0.24	20.03	20.55	4.8
Mozambique	-0.32	19.44	23.13	3.85
Zimbabwe	-0.4	18.37	9.55	4.8
Maximum Score	1.0	30.0	30.0	7.0

The African Competitiveness Report, 1998

Table 3.1 Malawi - Banking Sector Indicators

	1990	1991	1992	1993	1994	1995	1996
Liquid assets /deposits (Liquidity ratio)	44.5	31.8	39.4	48.8	52.7	62.3	70.6
Loans/Deposits	67.6	72	81.8	53	55.2	39	31.2
Treasury bill holdings/deposits	3.2	2.7	7.4	16.1	14.8	34.1	41.3
Bank Spread	8.9	7.5	5.5	7.8	6	10.1	19
Real deposit rate	0.2	-0.1	-6.2	2.2	-9.7	-46.1	-10
credit to private sector/ GDP	10.2	10.9	13.3	8.8	10.8	5.6	4.2

Reserve Bank, Finance and Economic Review (1998)

Table 3.2 – Malawi Public External and Debt Service

	1992	1993	1994	1995	1996	1997	1998	1999	2000
Debt Outstanding (Mn \$)	1,230	1,337	1,397.3	1,379.5	1,507.9	1,608.3	1,688.4	1,741.8	1,792.25
Total Debt Service (Mn \$)	73.3	59.9	63.7	61.4	62.6	68	82.4	88	90
Principal (Mn \$)	48.9	34.8	38.5	37.7	38.6	41.1	50	52.3	50.8
Interest (mn \$)	25.9	25.1	25.2	23.8	24.1	26.1	32.4	35.8	39.2
			<i>Ratios</i>						
Debt outstanding /GDP	93.2	91.1	154.5	161.7	155.6	158.1	155.1	150.7	146
Total debt service/ XGS	24.7	24.5	24.1	22.1	21.7	21.7	24	23.3	21.5
Principal	16.5	14.2	14.6	13.5	13.3	12.9	14.5	13.8	12.1
Interest	8.7	10.3	9.6	8.5	8.4	8.6	9.4	7.5	9.4

Source: Ministry of Finance

Table 3.3 Malawi – Government Finances (MK Million)

Government Finances	FY90	FY91	FY92	FY93	FY94	FY95	FY96	FY97	FY98
Total revenue & Grants	1,155.9	1,389.9	1,615.2	1,853.3	4,096.7	6,422.9	7,756.2	10,554.0	12,907.4
Current Revenue	1,043.2	1,181.9	1,383.4	1,569.3	2,194.6	4,436.7	6,047.7	8,461.6	8,993.3
Domestic trade tax	347.2	391.1	427.1	523.6	523.6	1,439.8	1,964.3	2,671.1	2,903.4
International trade tax	162.8	211.5	252.4	253.8	792.0	1,121.1	1,364.0	1,976.4	1,526.0
Total Expenditure	1,371.8	1,534.1	2,103.1	3,263.9	4,286.0	7,868.0	8,736.9	13,213.0	15,727.9
Current expenditure	1,060.2	1,219.3	1,635.4	2,234.7	3,745.1	6,228.9	6,999.2	10,357.0	9,468.5
grants and subsidies	91.4	100.0	153.6	227.5	240.3	645.1	1,708.5	2,092.4	567.5
wages and salary	237.9	289.5	415.6	654.4	865.9	1,955.9	1,771.4	3,618.7	3,854.3
Interest	177.8	165.8	254.1	251.6	400.0	1,653.6	1,881.7	2,080.8	1,798.0
Development expenditure	311.6	314.8	467.7	1,029.2	540.9	1,639.1	1,737.7	1,808.1	6,259.4
of which social and community services	70.4	98.6	164.5	126.0	146.0	883.3	499.0	4567.1	2,457.3
gross fixed capital formation	206.5	208.6	254.4	701.1	300.3	997.7	1,246.2	1,224.5	3,916.0
Overall balance									
excluding grants	-328.7	-352.2	-719.7	-	-	-	-	-4751.4	-5,295.6
including grants	-216.0	-144.2	-487.9	1,694.7	2,091.4	3,431.3	2,689.2	-980.7	-1,044.6
						1,445.1			
<i>As percentage of GDP</i>									
excluding grants	-6.5	-5.7	-10.0	-18.3	-18.7	-13.4	-7.3	-8.3	-8.1
including grants	-4.3	-2.4	-6.8	-15.2	-1.7	-5.7	-2.7	-4.6	-1.6

Economic Reports various years

Table 3.1 Malawi- Vulnerability to Shocks

<i>Indicator</i>	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Composition of GDP										
Agriculture/GDP	40.1	10.1	33.8	45.7	34.7	38.2	36.5	33.7	32.7	34.5
Smallholder production/GDP	24.1	25.5	17.3	28.9	21.7	26.7	33.7	24.6	25.1	27.3
Industry GDP	25.8	24.7	27.5	22.5	25.6	24.4	19.1	17.4	17.0	16.5
Manufacturing/GDP	17.4	16.5	18.5	14.6	16.7	16.1	12.6	14.1	13.3	12.9
Services/GDP	23.3	25.8	29	23.2	29.7	26.7	35.2	39.4	40.6	41.7
Official External Capital Flows										
Percent of Deficit Financed through external grants	39.8	47.6	20.6	29.8	38.8	52.7	55.9	44.0	80.3	81.5
Grants as % of total Revenue (incl. Grants)	9.8	15.0	14.4	15.3	40.4	30.9	22.2	19.8	38.5	37.8
Grants/GDP	5.4	6.0	5.5	5.7	21.5	16.7	4.6	3.6	6.5	9.5
Percent of Deficit financed through external borrowing	67.5	56.5	35.9	67.6	30.3	18.2	47.1			
Composition of exports										
Total merchandize exports/GDP of which	22.8	21.8	21.4	16	29	28	19.8	20.3	30.2	28.4
Tobacco exports/GDP	16	16.5	15.8	11.1	20	17.5	12.4	13.0	18.5	17.0
Tea exports/GDP	2.7	1.7	1.6	1.8	2.3	1.8	1.2	1.6	2.2	2.7
Sugar exports/GDP	1.6	1.3	1.5	0.8	2	1.8	1.5	1.2	1.6	1.4
Tobacco exports/total merchandize	70.1	75.6	74	69.1	68.8	62.5	62.6	63.1	65.9	63.4

Fig 2.5

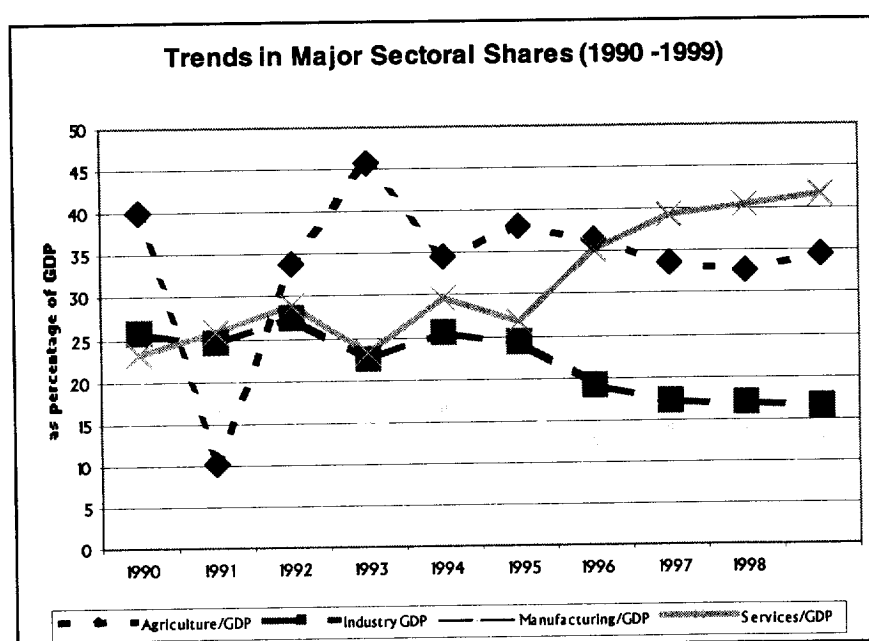


Table 3a. Trends in Social Expenditures

	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99
Education Expenditure						
Share in Total Expenditure	8.9	10.5	17.9	16.2	18.4	14.1
Share in Recurrent Expenditure	9.9	9.4	16.0	18.2	18.3	15.6
Share in Development Expenditure	6.6	18.0	26.4	8.4	18.6	10.6
As Percent of GDP	3.3	3.2	5.4	4.0	5.5	3.3
Per capita (in US dollars)	6.2	4.5	9.1	9.0	11.8	5.4
Health Expenditure						
Share in Total	5.4	6.3	11.4	7.8	7.5	12.8
Share in Recurrent Expenditure	6.0	6.5	9.7	8.8	7.5	8.8
Share in Development Expenditure	4.1	4.8	18.9	3.6	7.2	22.4
As Percent of GDP	2.0	1.9	3.4	1.9	2.2	3.0
Per capita (in US dollars)	3.8	2.7	5.8	4.3	4.8	4.8
<i>Memo items:</i>						
Interest Expenditure (percent of GDP)	1.9	3.1	4.3	4.1	2.1	2.1
Domestic	1.2	2.0	2.2	1.1	1.1	1.7
External						

Source: *Recurrent Actual Estimates* and *Development Actual Estimates*, various years. Actual figures for 1993/94-1997/98, estimated figures for 1998/1999.

Table 3b. Selected Educational and Health Indicators

	1980-85	1993-98
Education		
Primary school enrollment rate, total (percent of age group)	43	76
Primary school enrollment rate, male (percent of age group)	46	76
Primary school enrollment rate, female (percent of age group)	41	76
Health		
Safe water (percent of population with access)	32	45
Immunization, measles (percent of children under 12 months)	49	87
Immunization, DPT (percent of children under 12 months)	52	95
Child malnutrition (percent under 5 years)	24	30
Life expectancy at birth, total (years)	45	42
Mortality rate, infant (per thousand live births)	163	134
Mortality rate, under 5 (per thousand live births)	265	229

Source: 2000 World Development Indicators CD-ROM, World Bank

Table 3: Exceptional Financing Requirements (\$ Million)

	1999	2000	2001	2002	2003	2000-03
Requirements	-284	-285	-345	-328	-342	-338
Current account deficit (minus interest)	-282	-257	-237	-265	-286	-263
Interest payments	-26	-30	-30	-30	-30	-30
Amortization	-39	-57	-58	-58	-63	-60
Change in international reserves *	63	59	-20	25	37	14
Total financing available	284	285	345	328	342	338
Regular financing**	284	285	260	238	237	245
Grants	157	141	106	111	121	113
Loans	127	144	154	127	116	132
BOP support	16	31	38	19	14	24
Projects	111	113	116	108	102	109
Exceptional financing (gap)	0	0	85	90	105	93
Memo item						
Financing gap after HIPC relief	62	46	61	56
GDP growth (% per annum)	4.0	3.2	3.0	4.0	4.0	3.7

* Includes projected average net FDI and other capital movements

** Includes planned project and BOP support

SECTOR	MINISTRY/ DEPARTMENT	PROGRAMME	GENERAL PUBLIC SERVICES	SOCIAL & COMMUNITY SERVICES	ECONOMIC INFRASTRUCTURE	PRODUCTIVE SECTORS	DISASTER RELIEF & PREP.
GENERAL PUBLIC SERVICES							
SOCIAL AND COMMUNITY SERVICES							
PRODUCTIVE SECTORS							
ECONOMIC SERVICES & INFRASTRUCTURE							
DISASTER RELIEF AND PREPAREDNESS							
SECTORAL SCORES FOR INTER- LINKAGES			2	3	1	3	2
