



Malawi Government

ANNUAL DEBT AND AID REPORT

(JULY 2008 - JUNE 2009)

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ACCRONYMS AND ABBREVIATIONS

AAA	Accra Agenda for Action
ADF	African Development Fund
AfDB	African Development Bank
AMP	Aid Management Platform
BADEA	Arab Bank for Economic Development in Africa
DACU	Development Assistance Coordination Unit
DAD	Debt and Aid Management Division
DAS	Development Assistance Strategy
DfID	Department for International Development
DOD	Disbursed Outstanding Debt Stock
ESF	Exogenous Shock Facility
EIB	European Investment Bank
EU	European Union
FAO	Food and Agriculture Organisation
FY	Financial Year
GBS	General Budget Support
GDP	Gross Domestic Product
GoM	Government of Malawi
GTZ	Deutsche Gesellschaft für Technische Zusammenarbeit
ICT	Information, Communication and Technology
IDA	International Development Agency
IFAD	International Fund for Agriculture Development
IMF	International Monetary Fund
JICA	Japanese International Cooperation Agency
KfW	Kreditanstalt für Wiederaufbau
M&E	Monitoring and Evaluation
MGDS	Malawi Growth and Development Strategy
MoF	Ministry of Finance
NAC	National Aids Commission
NDF	Nordic Development Fund
OPEC Fund	Organisation of Petroleum Exporting Countries Fund
PAF	Performance Assessment Framework
P&I	Planning and Information
PBA	Programme Based Approach
PIU	Project Implementation Unit
PRGF	Poverty Reduction Growth Facility
RBM	Reserve Bank of Malawi
SBS	Sector Budget Support
SDR	Special Drawing Rights
SWAp	Sector Wide Approach
SWG	Sector Working Group
UN	United Nations
UNDP	United Nations Development Programme
UNFPA	United Nations Population Fund
UNICEF	United Nations Children's Fund
USAID	United States Agency for International Development
WFP	World Food Programme
WHO	World Health Organisation

PREFACE

This is the third edition of annual Debt and Aid Reports published by the Debt and Aid Management Division (DAD) of the Ministry of Finance. Like the previous publications, this report aims at providing and analysing data on the volume, distribution and effectiveness of the foreign aid that Malawi received in the 2008/09 financial year. It also provides and analyses the latest information on the public external and domestic debt portfolios. The review focuses on the trends of Malawi's external and domestic debt stock and the composition of debt by creditors, currency and borrower category.

The report is structured as follows: The first chapter is the Aid Portfolio Review. The data used in this review was obtained from the Aid Management Platform (AMP) database which is maintained in the Debt and Aid Management Division. Chapters 2 and 3 provide an overview of the domestic and external debt portfolios, respectively, as at 30th June 2009. The data used to analyse the external debt portfolio was obtained from the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) domiciled in DAD. The domestic debt data was obtained from the Reserve Bank of Malawi.

The Ministry of Finance wishes to thank all the development partners who have contributed to the ongoing process of improving aid and debt data collection in Malawi and in the production of this report.

This report was prepared by Tiyamika Kanthambi, Verity Outram, Tayani Banda, Alfred Kutengule and Stan Nkhata of DAD. Mr. Aaron Batten also contributed to the report, particularly in the final stage. All enquiries related to this report should be directed to the Director of Debt and Aid Management

CHAPTER 1: AID PORTFOLIO REVIEW

1.1 Data Collection and Reporting

The data used to analyse the foreign aid portfolio is provided to DAD by Malawi's development partners. Partners are required to return monthly data templates to DAD, including all aid disbursements made in the previous month in addition to a variety of project/programme information and projections of future disbursements.

In the 2008/2009 Financial Year (FY), there was a revived effort by DAD to improve the data collection mechanisms following deterioration in both the timeliness and quality of submissions from donor agencies in 2007/2008FY. As outlined in the 2007/2008FY Debt and Aid Annual Report, the lack of data submissions from a number of development partners, in particular the United Nations (UN) agencies, had caused increasing difficulties for DAD in conducting regular analysis of aid flows in addition to hindering the provision of accurate, timely aid data for the budgeting process and for government-wide dissemination. Furthermore, monthly submissions by donors are required to accurately monitor the International Monetary Fund (IMF) supported Exogenous Shock Facility (ESF) programme. Incomplete data constrains the Government's ability to monitor the ESF targets effectively and contributes to the need for frequent adjustments to the programme targets.

Part of the process of improving data collection has been to establish Data Focal Agents (DFAs) within each of the donor organisations who provide Malawi with foreign aid. To date, 14 official DFAs have been confirmed. This includes one DFA for the German Development Cooperation (GDC) to cover aid inflows from both Gesellschaft fur Technische Zusammenarbeit (GTZ) and Kreditanstalt fur Wiederaufbau (KfW) under the German Development Cooperation (GDC) and a single DFA who coordinates with all the UN agencies. The individual UN agencies have also come forward with 6 DFAs with whom the coordinating DFA liaises. By establishing one DFA per donor, there is increased accountability and clarity surrounding aid data management. On the Government side, DAD has also designated one person responsible for all data-related matters. It was agreed that each year there will be two training sessions for all DFAs so as to further improve communication and knowledge sharing with the development partners and improve the accuracy of the aid data that is reported by donors.

**Data Focal Agents
have been identified
for each development
partner.**

In the 2007/2008 annual report, donors were ranked in terms of their timeliness in responding to aid data requests by the Ministry of Finance. This report does not include such rankings due to the ongoing processes of improving data systems within DAD and on the donors' side. However, it will be reintroduced in the next report after the data management system is well established.

A number of donors failed to provide complete data in the period July 2008 – June 2009 despite several requests. These include:

- United Nations Development Program (UNDP) provided data only in the month of June that included disbursements for July 2008 – April 2009.
- The European Union (EU) did not respond to data requests for the first half of 2009 due to changes in their internal financial management systems but did provide all the disbursement figures at the end of 2008/09FY.
- UNICEF did not respond to any requests for the entire 2008/09FY and are therefore not included in this aid portfolio review.
- Other UN agencies had difficulties in providing data prior to the DFA training but have since had a good response rate.

The Ministry of Finance commends Norway, Ireland, USAID, GDC, the World Bank, Japan, Department for International Development (DfID) and African Development Bank (AfDB) for submitting disbursements data to the Ministry every month of the past financial year.

In addition to analysing the timeliness of aid data submission, the completeness of information provided is important to the Government's budgeting process. Given that donor funding has historically accounted for 80% of the development budget, having accurate and complete projections is vital for the effective allocation of resources. Some donors were unable to provide annual projections for 2009/10FY, whilst others were only able to provide projections for July-December 2009, citing incompatible financial years with that of the Government.

As outlined in the Annual Report for 2007/2008FY, the Aid Management Platform (AMP) has now been launched and is in full operation within DAD. AMP is a web-based aid database that is used for tracking the financial flows in donor funded programmes as well as the physical implementation progress. It also has a facility for generating customized reports on aid flows depending on the needs and requirements of the user.

AMP has led to improvements in data sharing within the Ministry of Finance. It is expected that the system will be expanded so that parties outside the Ministry will have access to all aid information about Malawi via the AMP website. In the next 12 months, a number of donors will pilot entering data into AMP themselves in order to reduce transaction costs and further improve the accuracy of the data being collected.

1.2 Distribution of Aid Disbursements

1.2.1 Aid by Development Partner

In the 2008/09FY, foreign aid disbursements to Malawi amounted to K112.9 billion, an increase of K335.1 million over the disbursements in 2007/08FY. Table 1.1 overleaf presents total disbursements of aid in the previous three financial years by development partner in addition to projected disbursements for 2009/10FY.

Almost all donors increased the volume of their disbursements in 2008/09FY. However, the increase in total disbursements also represents the greater coverage of donors that are reported on such as the Global Fund to Fight HIV/AIDS, Malaria and Tuberculosis, Iceland International Development Agency (ICEIDA), and UNAIDS. Furthermore, Malawi has attracted new donors like Ireland, and the Flemish

International Cooperation Agency (FICA) which commenced disbursements in 2007/08FY and 2008/09FY. The Global Fund is now the third largest donor in terms of disbursements, with K15.6 billion of their funds directed to the Health Sector Wide Approach (SWAp) and the National AIDS Commission (NAC).

Total disbursements increased by K225 million on the year to K107.3 billion

Nine of the donors that are reported on in this report increased disbursements, in many cases significantly, in the 2008/09FY compared to 2007/08FY. AfDB more than doubled disbursements on the year as a result of the increase in General Budget Support (GBS).

Four donors had lower disbursements than in the previous year: DfID, Norway, UNDP and UNFPA. The decrease in disbursements from DfID is a due to the reduction in support towards the Health SWAp. In addition, there was a one-off \$10 million disbursement towards the National Consensus in 2007/08FY.

The apparent decrease in Norwegian disbursements is not due to Norwegian aid reductions but rather the withdrawal of Swedish aid which was being channelled through Norway. The Swedish International Development Agency (SIDA), who have had a cooperative agreement to channel funds to Malawi via Norway since 2001, have been gradually withdrawing aid since 2007. Swedish aid accounted for an average of 90-100 million Norwegian Kroner (NOK) a year (approximately MK1.9 - MK2.1 billion), falling to NOK 75 million in 2008 and reducing to NOK 25 million in 2009.

The World Bank and GTZ kept disbursements at roughly the same level as in the 2007/08FY. UNICEF was unable to provide data to DAD on disbursements for the entire period while UNDP only provided data until April 2009. As a result, given their significant volumes of aid disbursements in previous years, total aid will have in fact been higher than the reported amounts.

Table 1.1: Total Disbursements by Donor, 2006-2010

	Actual Disbursement 2006/07FY		Actual Disbursement 2007/08FY		Actual Disbursement 2008/09FY		Projections 2009/10FY	
	USD	Kwacha	USD	Kwacha	USD	Kwacha	USD	Kwacha
AfDB	24,594,108	3,405,447,952	26,075,644	3,650,454,733	71,850,195	10,050,069,329	47,425,616	6,629,693,267
CIDA	6,098,795	846,243,098	9,256,861	1,296,105,908	10,859,976	1,519,246,214	9,765,952	1,365,196,070
DfID	143,423,554	19,897,631,534	145,492,367	20,358,194,269	112,716,639	15,767,185,727	157,897,340	22,072,690,180
EU	57,205,173	7,931,542,941	70,727,387	9,897,997,343	138,817,040	19,416,963,498	90,181,924	12,606,657,441
FICA	0	0	2,787,586	392,261,319	3,063,731	428,575,769	436,681	61,044,279
FAO	1,957,960	271,472,720	1,098,402	153,868,634	4,189,730	586,045,393	-	-
GDC	14,950,034	2,072,834,127	15,581,281	2,181,005,510	21,273,495	2,975,432,398	32,646,570	4,563,709,717
GTZ	8,433,158	1,169,264,108	12,610,359	1,765,505,738	12,615,856	1,764,670,262	9,578,814	1,339,035,808
KFW	6,516,876	903,570,019	2,970,922	415,499,772	8,657,639	1,210,762,136	23,067,756	3,224,673,909
Global Fund	0	0	0	0	111,770,649	15,633,575,603	88,579,335	12,382,629,251
ICEIDA	3,120,014	432,593,867	4,957,935	694,086,894	3,199,162	447,465,623	2,488,252	347,836,231
IFAD	0	0	8,000,000	1,118,331,200	122,766	17,174,841	-	-
Ireland	0	0	4,854,226	678,579,048	9,488,284	1,327,265,979	17,565,468	2,455,501,410
JICA	10,262,728	1,422,935,448	14,627,943	2,047,354,791	28,959,028	4,049,919,871	8,152,424	1,139,638,787
Kuwait Fund	0	0	21,319	2,976,548	478,906	66,993,537	-	-
Norway	42,750,933	5,927,852,913	69,715,351	9,753,262,698	61,148,695	8,552,500,379	57,534,212	8,042,788,063
OPEC Fund	0	0	0	0	143,000	20,005,539	-	-
UNFPA	0	0	9,329,204	1,304,268,760	903,849	126,414,667	1,300,000	181,728,820
UNICEF	11,103,929	1,539,568,639	27,926,293	3,919,900,267	-	-	-	-
UNDP	9,554,465	1,324,734,216	8,322,188	1,165,963,302	6,596,042	922,535,789	-	-
UNAIDS	0	0	0	0	333,689	46,681,553	-	-
USAID	43,555,036	6,043,338,927	57,045,445	7,977,697,409	76,714,380	10,731,189,852	84,520,840	5,120,685,633
World Bank	44,680,314	6,194,961,280	66,397,059	9,295,647,037	75,808,466	10,600,932,478	95,046,000	13,286,613,404
WFP	303,337	42,057,918	8,587,375	1,200,286,650	45,282,166	6,334,018,473	45,570,805	6,370,406,630
WHO	0	0	988,786	138,445,917	2,281,425	319,106,778	-	-
Total	428,510,413	59,426,049,707	567,373,932	79,407,693,746	807,274,809	112,914,731,689	771,757,990	101,190,528,899

Dash (-) indicates that donor has failed to provide sufficient information.

Source: Aid Management Platform, DAD, Ministry of Finance

It is projected that disbursements for 2009/10FY will amount to K101.2 billion. However, as the many gaps in the table show, this does not necessarily indicate that aid will decline. It is a result of some development partners not being able to provide forecasts to the Ministry of Finance. The issue of supplying data on annual and quarterly aid projections is addressed later in the report.

1.2.2 Bilateral Aid Disbursements

The relative share of aid from bilateral development partners has decreased from 59% in 2007/08 to 41% in 2008/09. This is a result of the significant disbursements from the Global Fund (a multilateral organisation) and also increased disbursements from the other multilateral donors like EU, WFP and AfDB.

1.2.3 Aid Concentration among Major Donors

The year has also seen the concentration of aid from the top donors decline, as displayed in Table 1.2. In 2007/08FY the top five highest disbursing donors accounted for 76% of total aid whereas in 2008/09FY this fell to 67%.

Table 1.2: Top ten Donors by Disbursement

RANK	2007/08		2008/09	
	Donor	% of Total	Donor	% of Total
1	DfID	26.8%	EU	18.1%
2	EU	13.0%	DfID	14.7%
3	Norway	12.9%	Global Fund	14.6%
4	World Bank	12.3%	USAID	10.0%
5	USAID	10.5%	AfDB	9.4%
6	UNICEF	5.2%	World Bank	8.8%
7	AfDB	4.8%	Norway	6.9%
8	Japan	2.7%	WFP	5.9%
9	GTZ	2.3%	Japan	3.8%
10	UNFPA	1.7%	GTZ	1.6%

Source: Aid Management Platform, DAD, Ministry of Finance

1.2.4 Disbursements by Type of Assistance

The majority of aid to Malawi comes in the form of grants, which accounted for 92% of disbursements in 2008/09FY (Table 1.3). A small number of concessional loans were received from AfDB, Kuwait fund, OPEC, BADEA and the World Bank.

Table 1.3: Disbursements by Type of Assistance, 2008/09 in Malawi Kwacha

Type of Assistance	Total Disbursement 2008/09
Grant	99,200,320,362
Loan	7,499,826,583
Technical Assistance	596,205,934
Total	107,296,352,878

Source: Aid Management Platform, DAD, Ministry of Finance

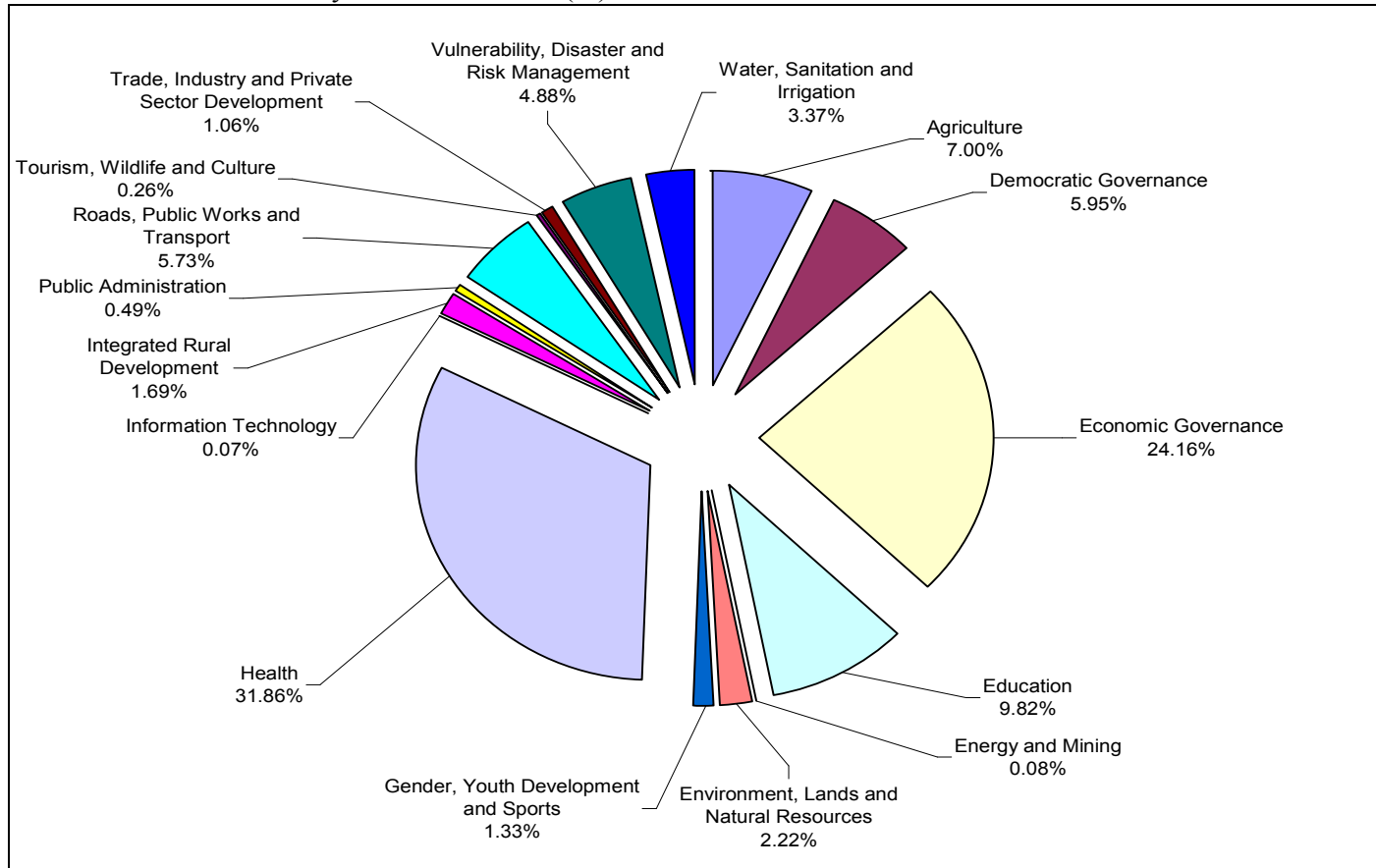
1.2.5 Disbursement by Economic Sector

Chart 1.1 below displays the distribution of disbursements by economic sector based on the new sector classification that was launched by the Government in November 2008. The new list of sectors is as follows: Agriculture; Integrated Rural Development; Environment; Lands and Natural Resources; Tourism, Wildlife and Culture; Water, Sanitation and Irrigation; Trade, Industry and Private Sector Development; Vulnerability, Disaster and Risk Management; Health; Education; Gender, Youth Development and Sports; Roads, Public Works and Transport; Information, Communication and Technology (ICT) and Research & Development (R&D); Energy and Mining; Economic Governance; Democratic Governance; and Public Administration.

The health sector received the highest proportion of disbursements in 2008/09FY

The highest aid receiving sectors were, as in previous years, Health, Economic Governance, Education and agriculture. These five sectors together accounted for 76% of all aid disbursements. With the elections held within the 2008/09FY, there was a relative increase in the volume of aid disbursed to the Economic Governance sector with an increase of 11% on the year. Further analysis of the distribution of disbursements by donor and sector can be found in the aid effectiveness section of this report.

Chart 1.1: Disbursements by Economic Sector (%)



Source: Aid Management Platform, DAD, Ministry of Finance

For further insight into the distribution of aid by donor and sector, DAD has produced the first edition of the Malawi Aid Atlas, available on request. The 2008/2009FY Aid Atlas will be available by the end of 2009.

1.3 Aid Effectiveness

This section analyses the aid flows to Malawi in the context of the principles of the Paris Declaration on Aid Effectiveness (2005) and the Accra Agenda for Action (2008). The effectiveness of aid is analysed according to the different modalities of aid delivery as well as the predictability of the aid received.

1.3.1 Disbursements by Aid Modality

Table 1.4 presents total aid disbursements to Malawi according to aid modality by donor. There are three main classifications of aid modality: GBS, direct project support and pooled funding/sector support which includes funding to Food Security, the Health SWAp, NAC and to support the Fertiliser Subsidy. The Definitions of each modality are as follows:

- GBS (grants or loans) is financial assistance that a donor provides directly to the Government budget to meet its financing gap.
- Direct Project Support is donor funding in the form of grants or external loans for specific activities like capital projects or infrastructure development.
- Grants for the National Aid Commission (NAC) and the Health SWAp are donor resources aimed at supporting the implementation of the HIV/AIDS and Health sector strategies.
- Food Security and Subsidy Grants are resources provided by donors to support the purchase of maize for the Strategic Grain Reserve and also to support the implementation of the Government's fertilizer input subsidy programme.

a) General Budget Support

GBS and Sector Support are the preferred modalities of aid delivery by the Government. In recent years, there have been efforts by Government and donors to increase the proportion of aid delivered through these channels. GBS and Sector Support altogether accounted for 43% of total disbursements in 2008/09FY of which GBS accounted for 21% while the remainder was Sector Support (Table 1.4). In fact, the proportion of GBS has increased compared to 18% in the previous year, reflecting donor confidence in the Government's ability to manage public finances and prioritise development spending.

**GBS and Sector Support
accounted for 43% of
disbursements in 2008/09FY, a
10% increase on 2007/08FY**

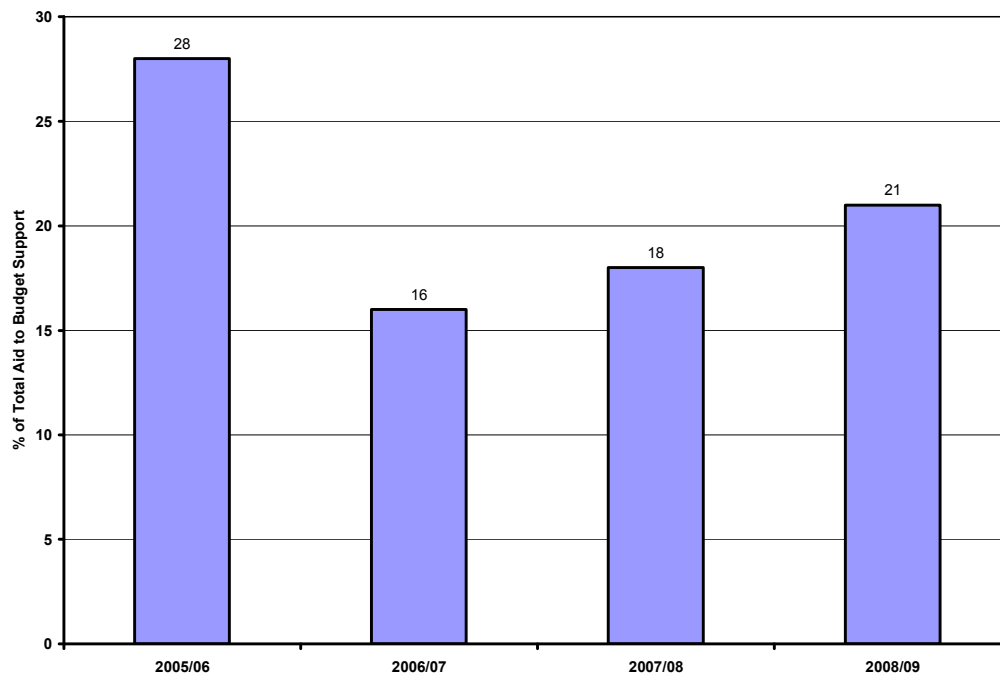
Table 1.4: Disbursements by Aid Modality and Donor in 2008/09FY

	US Dollars	Kwacha	Proportion of Total
Budget Support	164,007,710	22,939,710,846	20.9%
AfDB	37,817,562	5,290,607,242	
DfID	40,468,766	5,661,523,743	
EU	45,317,659	6,338,957,141	
Norway	10,403,722	1,454,880,720	
World Bank	30,000,000	4,193,742,000	
Direct Project Support	428,251,685	59,901,346,642	54.5%
AfDB	27,734,515	3,878,537,284	
CIDA	10,810,565	1,512,334,487	
DfID	37,451,916	5,238,826,606	
EU	86,272,798	12,067,201,494	
FICA	3,063,731	428,575,769	
FAO	4,189,730	586,045,393	
GDC (GTZ + KFW)	1,977,438	2,039,499,059	
ICEIDA	3,199,162	447,465,623	
IFAD	122,766	17,174,841	
Ireland	7,018,205	981,704,303	
JICA	28,959,028	4,049,919,871	
Kuwait Fund	478,906	66,993,537	
Norway	30,291,434	4,237,116,200	
OPEC Fund	143,000	20,005,539	
UNFPA	903,849	126,414,667	
UNDP	6,596,042	922,535,789	
UNAIDS	38,123	5,333,317	
USAID	76,714,380	10,731,189,852	
World Bank	42,119,264	5,891,347,759	
WFP	45,282,166	6,334,018,473	
WHO	2,281,425	319,106,778	
Food Security Support	7,226,583	1,010,804,863	0.9%
EU	7,226,583	1,010,804,863	
Sector Support - Health SWAP	86,745,908	12,132,914,730	11.0%
AfDB	6,298,118	880,924,802	
DfID	20,706,091	2,896,166,437	
Global Fund	33,869,706	4,737,941,753	
GDC	6,692,816	935,933,339	
Norway	16,179,177	2,262,524,099	
World Bank	3,000,000	419,424,300	
Sector Support - National AIDS Commission	88,458,906	12,372,293,844	11.3%
CIDA	49,411	6,911,727	
DfID	7,359,750	1,029,235,020	
Global Fund	77,900,943	10,895,633,851	
Norway	2,164,034	302,746,592	
UNAIDS	295,566	41,348,236	
World Bank	689,202	96,418,418	
Subsidy Support	11,310,522	1,582,228,366	1.4%
DfID	6,730,115	941,433,921	
Ireland	2,470,079	345,561,676	
Norway	2,110,328	295,232,769	
Total	786,001,314	109,939,299,291	100.0%

Source: Aid Management Platform, DAD, Ministry of Finance

Graph 1.1 below displays the trend in the proportion of aid in the form of GBS in the past four financial years. Although there was a peak in 2005/06FY, this was due to large disbursements made by DfID and EU to alleviate the effects of the food crisis that affected Malawi in that year.

Graph 1.1: Percentage of Budget Support in Total Aid Disbursements by FY



Source: Aid Management Platform, DAD, Ministry of Finance

In the 2007/08FY Annual Debt and Aid Report, DAD had projected that GBS would account for 26% of total disbursements in the 2008/09FY. However, due to the significant increases in disbursements using the other modalities of aid, this projection did not materialise. In actual terms though, GBS has increased by over K10 billion compared to the amount that was delivered in the preceding year. Despite the evident improvement in the volume of aid delivered as GBS and Sector Support, the proportions are low in comparison to the other countries in the Africa region.

b) Other Programme Based Approaches

Programme based approaches of aid delivery are preferable to Direct Project Support because they allow the Government to efficiently allocate resources, build Government systems and to reduce transaction costs associated with numerous stand alone projects. In recent years, there has been a marked increase in the delivery of aid delivered via Sector Support. To date, the majority of Sector Support has gone to the

Health sector which includes both the Health SWAp and the strategic response to HIV/AIDS via NAC. Sector Support currently accounts for 22% of total disbursements, an increase of 6% on the previous financial year. In part, this is due to the Global Fund's large disbursements to the Health SWAp and NAC, in addition to increased disbursements from other donors. The inclusion of disbursements from the Global Fund in this year's analysis has led to a marked increase in support towards NAC from MK2 billion in 2007/08FY to over MK12 billion in 2008/09FY.

Sector Support and GBS accounted for 43% of disbursements from reporting donors in 2008/09FY compared to 34% in 2007/08FY. Although a proportion of this may be due to the improvement in reporting by donors, the increase is nevertheless significant.

1.3.2 Predictability of Aid Flows

One of the central aspects of the Paris Declaration and the Accra Agenda for Action is the need to increase the predictability of aid flows in order to allow for enhanced planning and budgetary execution by developing country governments. By signing the Paris Declaration, donors committed to "provide reliable indicative commitments of aid over a multi-year framework and disburse aid in a timely and predictable fashion according to agreed schedules"¹ in order to strengthen the public financial management systems in recipient countries. This commitment was re-affirmed in the Accra Agenda for Action, stating that "donors will provide developing countries with regular and timely information on their rolling three to five-year forward expenditure and/or implementation plans, with at least indicative resource allocations that developing countries can integrate in their medium-term planning and macroeconomic frameworks. Donors will address any constraints to providing such information."²

DAD requests all donors to provide projections on all projects and programme aid for the current financial year (by quarter) in addition to projections for the following two financial years. At present, some donors continue to provide inaccurate or incomplete projections to DAD, in particular for Direct Project Support. The Ministry of Finance considers aid to be predictable if the actual disbursement is within plus or minus 10% of the reported projected disbursement. Graphs 1.2, 1.3 and 1.4 overleaf present the variance of the volumes of the aid actually disbursed in relation to the projections provided by donors on an annual basis.

a) Predictability of Direct Project Support

This analysis is based on those donors that reported both their projections and their actual disbursements on Direct Project Support for 2008/09FY. USAID, Canada, ICEDA, WFP and the World Bank disbursed closely in line with their projections as displayed in Graph 1.2. However, there remain significant variations between projected disbursements and the actual volumes of aid received for most development partners. Six donors had a variance greater than -10% i.e. having far lower disbursements than projected (Graph 1.2). Four donors

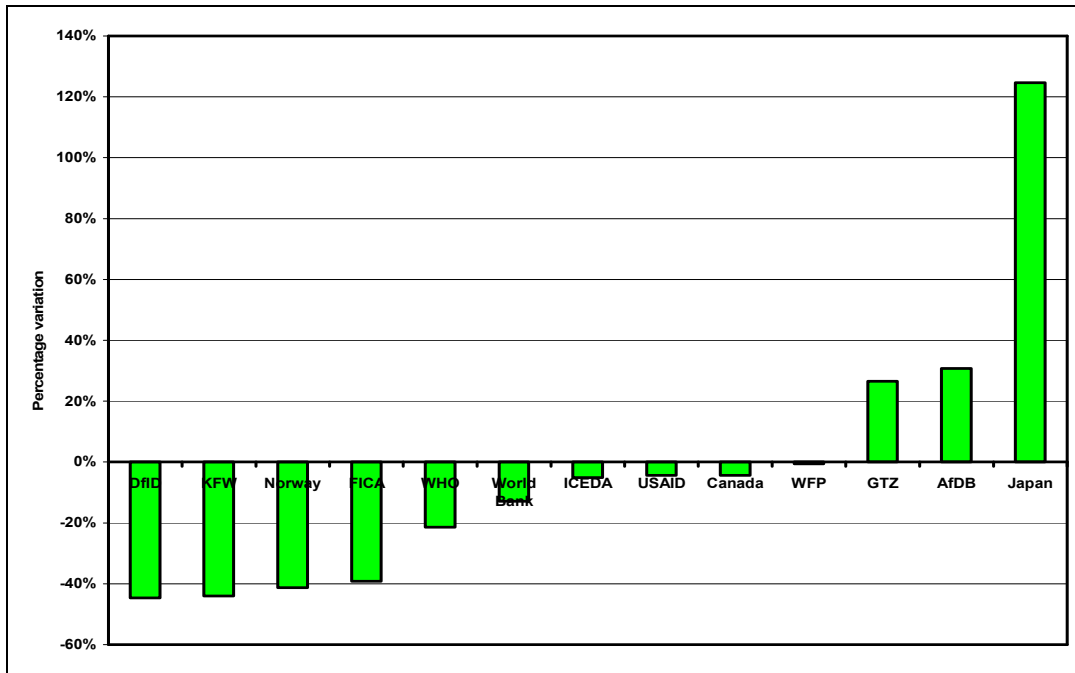
Projections are still not reflective of actual disbursements in 2008/09FY especially for project support

¹ Point 26 of the Paris Declaration (2005)

² Accra Agenda for Action (2008)

had a variance of less than 10% (+/-) and a further three disbursed more than 10% over the original estimates. The greatest outliers were DfID, KFW, Norway and JICA. JICA in particular disbursed 125% more than they had originally projected, largely reflecting inaccurate projections that are provided at the beginning of the year rather than the donor providing more aid.

Graph 1.2: Predictability of Direct Project Aid in 2008/09FY



Source: Aid Management Platform, DAD, Ministry of Finance

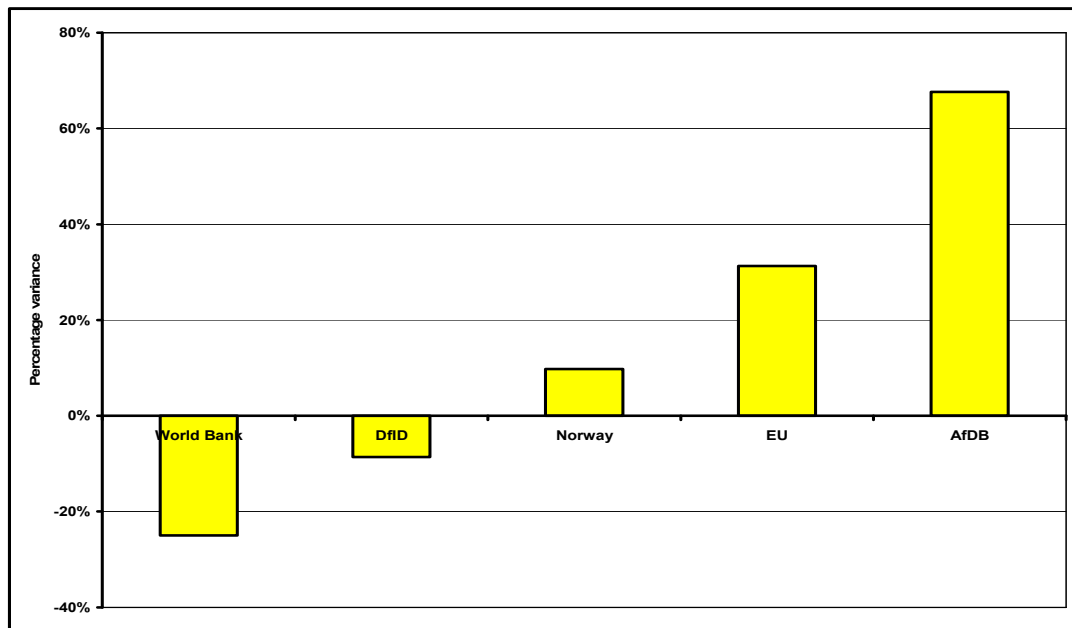
b) Predictability of General Budget Support

Although generally seen as a more predictable form of aid, GBS had large variations in projected versus actual disbursements for some donors. Whereas the variation between projected and actual direct project support tends to be a result of difficulty in forecasting, the variation of projected and actual disbursements of GBS is mostly a result of conditionality which leads to reduced or delayed disbursements.

Graph 1.3 shows the predictability of GBS by donor. DfID's disbursement was very close to planned amounts, as was Norway's. AfDB had significant positive disbursement as a result of an un-forecast disbursement of a Poverty Reduction Support grant. The positive variance of EU budget support is a result of a late disbursement from the 2007/08FY that was only made in the year under review. For the World Bank, the variance between actual and projected disbursements was largely due to the Bank's decision to disburse US\$30 million instead of the planned US\$40 million for the year. The Bank justified its decision on the basis that the Government did not abide by some of the principles of the partnership agreement with donors under the Common Approach to Budget Support (CABS) group.

Like in the previous three years, GBS from DfID and Norway was relatively more predictable in 2008/09FY

Graph 1.3: Predictability of Budget Support in 2008/09FY

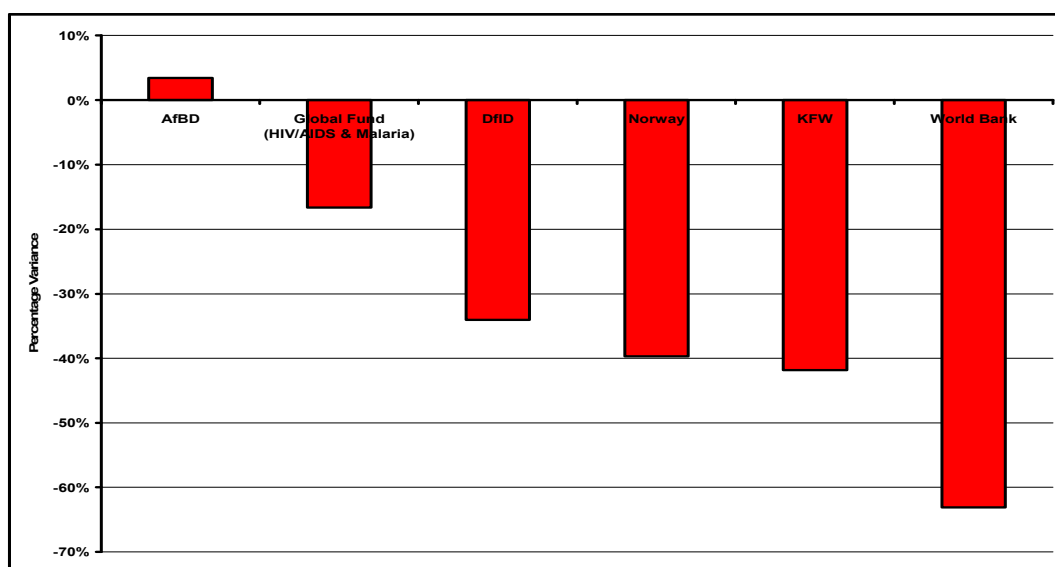


Source: Aid Management Platform, DAD, Ministry of Finance

c) Predictability of Sector Support

Sector Support is also considered as a more predictable form of aid delivery than Direct Project Support. However, there were significant variations in projected versus actual disbursements from most development partners. Apart from AfDB, all the development partners disbursed outside of (+-)10% of the projected disbursements (Graph 1.4).

Graph 1.4: Predictability of Programme Aid in 2008/09FY



Source: Aid Management Platform, DAD, Ministry of Finance

Although efforts continue to be made to address the issue of inaccurate/incomplete projections, further work and a re-commitment by donors is required to improve the situation. Donors cite poor planning processes, differing financial years and unknown project implementation speeds as central reasons for not providing this data.

**Donors must re-commit
to providing
comprehensive and
accurate projections**

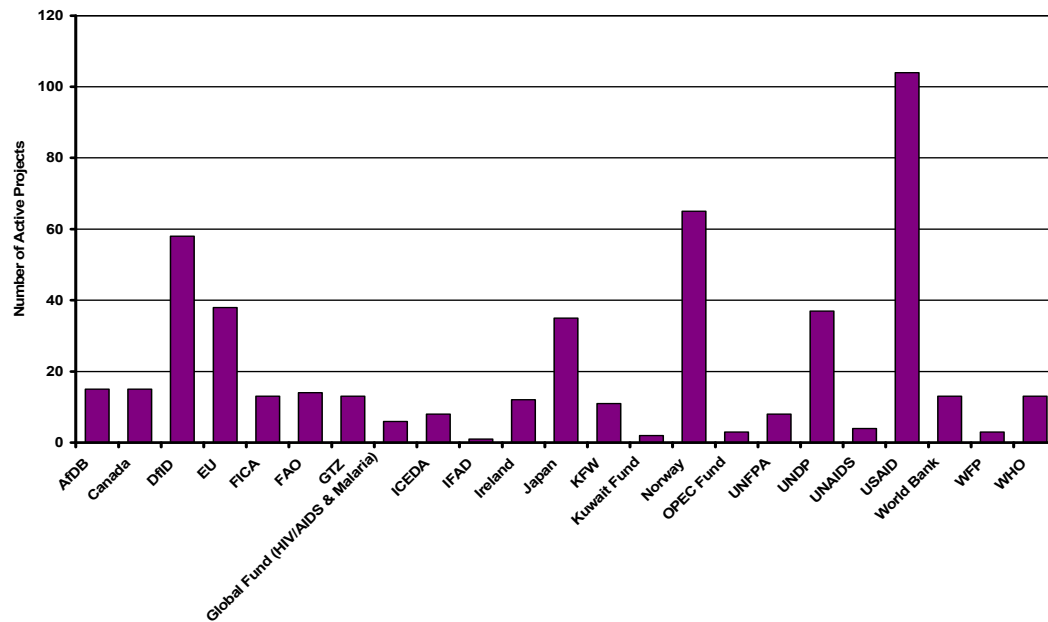
1.3.3 Fragmentation of Aid

Both the Paris Declaration and the Accra Agenda for Action emphasise the need to reduce aid fragmentation as a way to improve both the effectiveness and efficiency of foreign aid. The Malawi Aid Atlas for 2007/08FY highlights the high level of fragmentation of aid, measured by the number of donors per sector, the number of sectors within which each donor is active and the total number of active projects each donor is responsible for.

This section provides a summary of the 2008/09FY findings on the current state of aid fragmentation, which will be further analysed in the 2008/09FY Aid Atlas to be published at the end of 2009. This is part of a greater area of work of the Donor Division of Labour, looking into optimal methods to harmonise and align foreign aid to maximise its efficiency within each sector according to the comparative advantage of donors and in view of national and sector development strategies prioritised by the Government of Malawi.

Although the optimal number of projects and sectors per donor will vary according to the size of the donor budget and the expertise of the donor, Government feels that donors are currently not fully recognising their comparative advantages or working together to fully realise the potential gains of streamlining their activities. Graph 1.5 overleaf presents the number of active projects by donor. USAID continues to have the greatest number of projects (104) followed by Norway (65) and DfID (58).

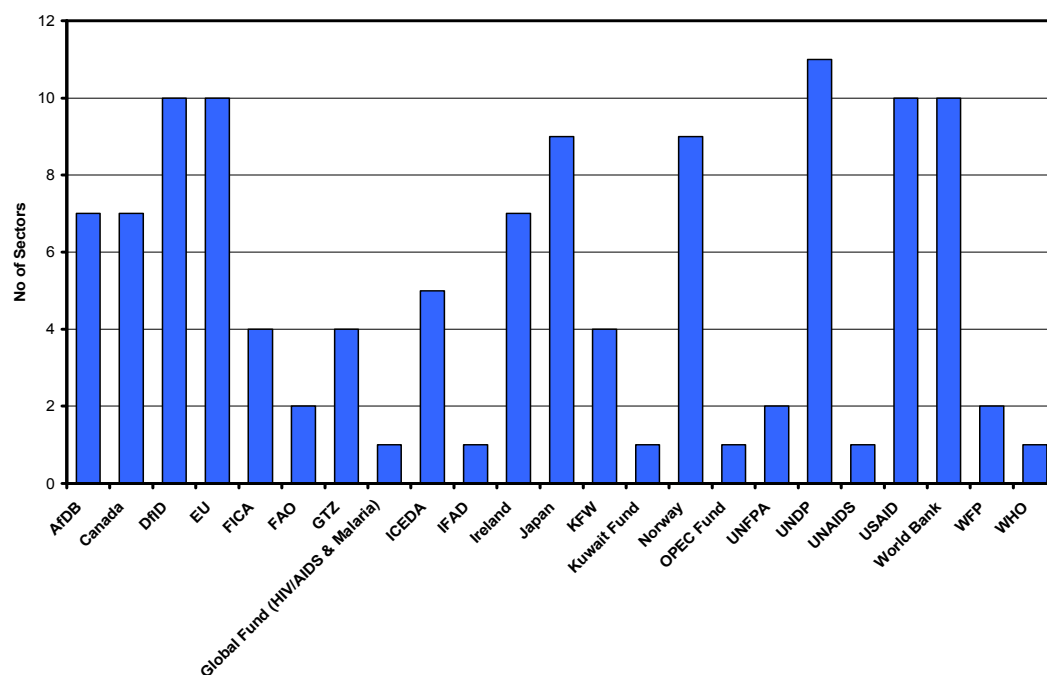
Graph 1.5: Number of Active Projects by Donor, 2008/09FY



Source: Aid Management Platform, DAD, Ministry of Finance

Graph 1.6 shows the number of sectors that each donor is active within. In 2008/09FY, seven donors had projects in at least nine of the sixteen sectors. As displayed in Table 1.5, five sectors had more than ten active donors each, with the health sector having twenty active donors. The Information Technology sector had only one active donor, UNDP. Neither of these extremes is optimal.

Graph 1.6: Number of Sectors each Donor was Active, 2008/09FY



Source: Aid Management Platform, DAD, Ministry of Finance

Table 1.5: Summary of Data on Aid Fragmentation, 2008/09FY

Sector	Number of Projects /Programme	Number of Donors	Disbursement to Sector 2008/09 (Kwacha)	Average No. of Projects per donor	Average Disbursement per Project /Programme	% of Total Aid Disbursed to Sector
Agriculture	66	12	7,867,038,608.99	6	119,197,555	7.3%
Democratic Governance	48	8	6,363,947,510.49	6	132,582,240	5.9%
Economic Governance	60	12	25,822,071,875.53	5	430,367,865	24.1%
Education	49	14	10,492,907,575.71	4	214,140,971	9.8%
Energy and Mining	2	2	88,746,359.83	1	44,373,180	0.1%
Environment, Lands and Natural Resources	18	8	2,371,793,005.58	2	131,766,278	2.2%
Gender, Youth Development and Sports	17	7	1,423,842,641.71	2	83,755,450	1.3%
Health	135	20	34,099,302,541.32	7	252,587,426	31.8%
Information Technology	1	1	76,671,768.19	1	76,671,768	0.1%
Integrated Rural Development	9	6	1,810,710,272.58	2	201,190,030	1.7%
Public Administration	3	3	526,802,727.07	1	175,600,909	0.5%
Roads, Public Works and Transport	20	6	6,128,281,740.10	3	306,414,087	5.7%
Tourism, Wildlife and Culture	7	3	281,589,952.97	2	40,227,136	0.3%
Trade, Industry and Private Sector Development	14	5	1,131,152,971.53	3	80,796,641	1.1%
Vulnerability, Disaster and Risk Management	17	6	5,210,099,659.68	3	306,476,451	4.9%
Water, Sanitation and Irrigation	23	11	3,601,393,666.87	2	156,582,333	3.4%
TOTAL	489		107,296,352,878.15			100.0%

Source: Aid Management Platform, DAD, Ministry of Finance

1.4 Aid Dependency Indicators

This section provides basic indicators of Malawi's aid dependency, relating the annual disbursements to economic variables, including Gross Domestic Product (GDP), Government Expenditure and imports. As in the 2007/08 Annual Report, these indicators are based on those used by the World Bank in the World Development Indicators (WDI) Report.

Table 1.6: Aid Development Indicators, 2004-09

Indicator	2004/05	2005/06	2006/07	2007/08	2008/09
Aid/Nominal GDP (%)	11	16	14	17	19
Aid/Real GDP (%)	13	16	16	21	26
Aid/Total Government Expenditure (%)	22	22	29	29	43
Aid/Total Imports (%)	34	34	34	44	58

Source: Aid Management Platform, DAD, Ministry of Finance

Table 1.6 illustrates that aid dependency according to all indicators has increased, reflecting increased donor confidence on the Government to manage aid effectively. The ratio of aid to GDP has been increasing since 2004 and is estimated at 19% in 2008/09FY. However, as Malawi develops economically, the need for Aid will decline. The aim of development policies is to create an economically viable country with domestic resources sufficient to delivery the goods and services required by its population

Aid dependency, according to all indicators, have been increasing since 2004.

CHAPTER 2: EXTERNAL DEBT PORTFOLIO REVIEW

2.1 Evolution of External debt stock

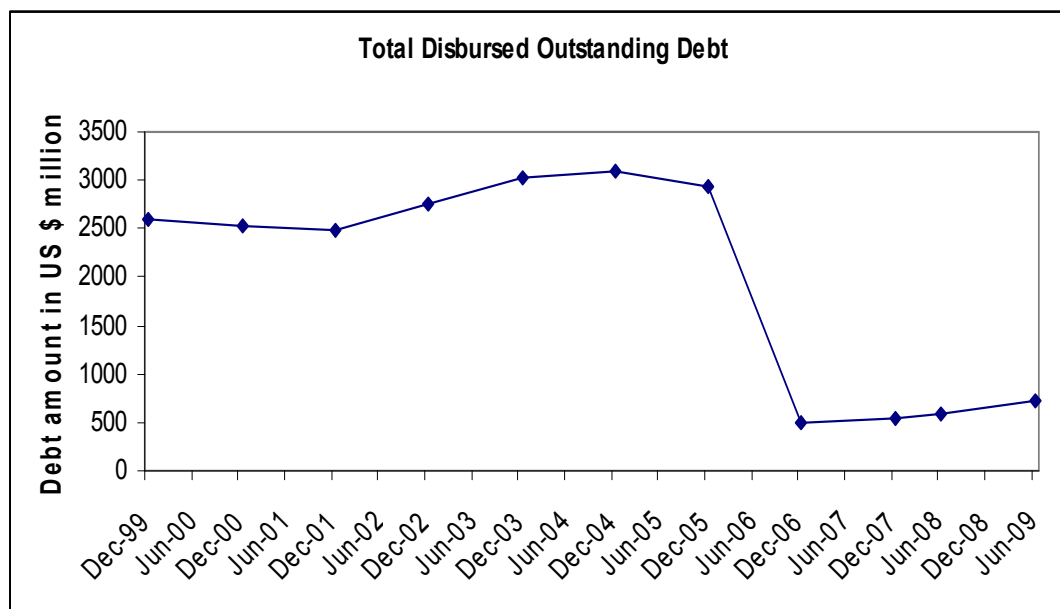
The external debt portfolio review is an analysis of trends in the public external debt stock, composition of debt by creditor category, borrower category and currency composition. The review also includes analysis of the new external loans that were contracted in 2008/09FY.

Malawi's external debt stock has increased gradually since accessing debt relief under the Heavily Indebted Poor Countries Initiative (HIPC) and the Multilateral Debt Relief Initiative (MDRI) in August 2006. Disbursed Outstanding Debt (DOD) increased from US\$487 million in December 2006 to US\$541 million in December 2007 and to US\$683 million in December 2008 (Graph 2.1). As of end June 2009, DOD amounted to US\$712 million compared to US\$585 million reported in June 2008, an increase of 22%. This is on account of significant disbursements from the International Monetary Fund and the African Development Fund under the balance of payment loans. Some disbursements were also received under project loans.

**Malawi's external
DOD was US\$712
million by end
June 2009**

This moderate debt accumulation is in line with the projections that were made at the time when Malawi qualified for debt relief in 2006.

Graph 2.1: Total DOD Stock in US\$ million (1999-2009)



Source: CS-DRMS Debt Database, DAD, MoF

2.2 External debt indicators

Malawi's external debt indicators improved significantly after receiving debt cancellations under the HIPC and MDRI Initiatives. The ratio of external debt stock to GDP was reduced from 108% before debt relief in 2005 to 15% after debt relief as of end-2006 and gradually rose to 17% in 2007. The ratio of external debt stock to GDP is projected to be 20% in 2009.

External debt is highly sustainable after the debt stock cancellations of 2006.

The ratio of external debt service to exports, also known as liquidity ratio, declined from an unsustainable position of 24% before debt relief in 2005 to 2.1% after debt relief in 2006. The debt service ratio is estimated to remain below 5% as of end-2009. These low debt ratios indicate that Malawi's debt is highly sustainable.

2.3 Disbursed Outstanding Debt Stock by Creditor Category

The current pattern of debt composition by creditor category remains similar to June 2008, with a large proportion of debt owed to multilateral creditors. As of end June

External debt to multilateral creditors amounted to US\$630 million, representing 89.2% of DOD as of end June 2009. The remainder was bilateral debt.

2009, 89.2% of the DOD stock was owed to multilateral creditors which amounted to US\$630 million. This is compared to US\$522.4 million owed in June 2008 which also represented 89.2% of the total DOD. Bilateral creditors accounted for another

US\$82 million of DOD stock in June 2009, up from US\$63.2 million in June 2008, representing 10.8% of the total DOD.

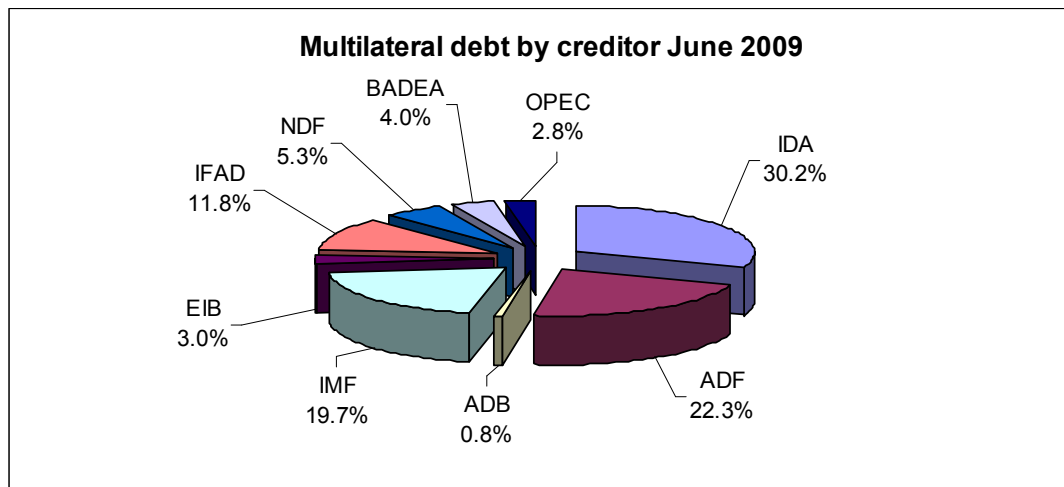
During the 2007/08FY, the remaining outstanding commercial debt was fully repaid and since then the Government has not contracted any commercial debt. According to its Debt and Aid Management Policy, the Government does not prefer short term loans with commercial interest rates. In cases where the Government may contract such non concessional loans, the activities for which the loan is contracted for should be of high economic value.

2.4 Multilateral Debt stock by creditors

The International Development Association (IDA) of the World Bank continued to be the largest creditor although its share of multilateral debt declined from 37 percent of the total debt stock in June 2008 to 30.2% in June 2009. This is attributed to the increased share of debts owed to the African Development Fund (ADF) and the IMF. The ADF was the second largest creditor with 22% (or US\$140.5 million) of the total debt stock, up from 17.6% (or US\$92 million) reported in the previous year. (Chart 2.1 & 2.2). This increase was largely due to disbursements under the programme loan that was contracted within the reporting period.

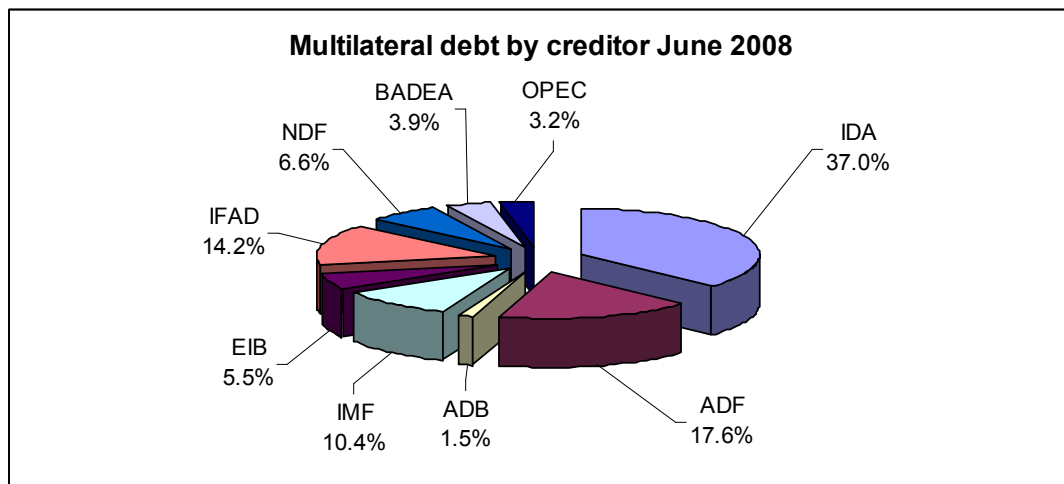
IDA of the World Bank Group is the largest multilateral creditor, accounting for 30% of multilateral debt. It is also Malawi's largest creditor.

Chart 2.1: Multilateral debt by Creditor in June 2009, in %



Source: CS-DRMS Debt Database, DAD, MoF

Chart 2.2: Multilateral debt by Creditor in June 2008, in %



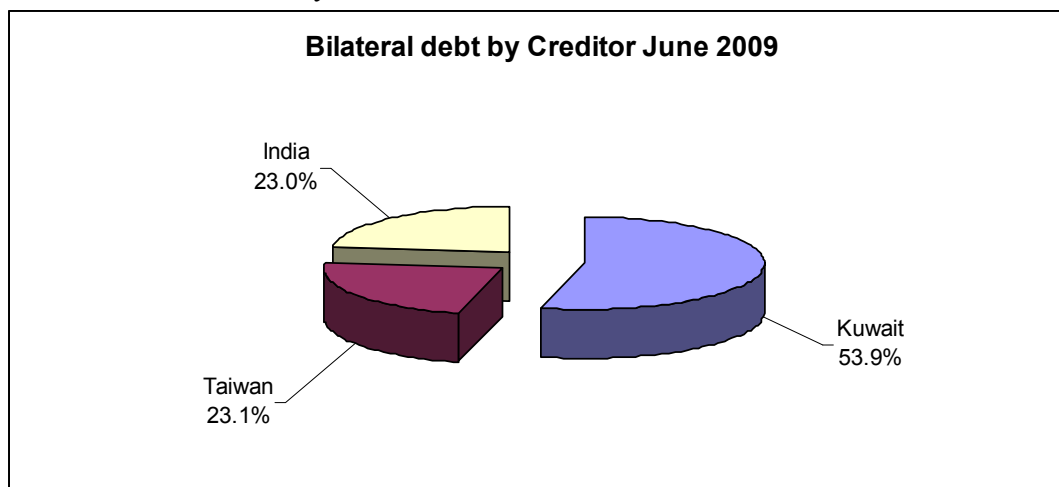
Source: CS-DRMS Debt Database, DAD, MoF

IMF is the third largest creditor, with a contribution of US\$124.3 million, representing 19.7% of total multilateral debt. This is an increase from US\$54.5 million (or 10.4%) from June 2008 (Chart 2.1 & 2.2). The significant increase in the share of the IMF debt is due to disbursements made under the Poverty Reduction Growth Facility (PRGF) and Exogenous Shock Facility (ESF). Other creditors include the International Fund for Agricultural Development (IFAD) whose share of total multilateral debt declined from 14.2% in June 2008 to 11.8% in June 2009, as well as the Nordic Development Fund (NDF), the Arab Bank for Economic Development in Africa (BADEA) and the OPEC Fund who accounted for 5.3%, 4% and 2.8% of total multilateral debt respectively (Chart 2.1 & 2.2).

2.5 Bilateral Debt by Creditor

In the previous Annual Debt and Aid Report, the analysis of bilateral debt by creditor covered two non Paris Club creditors, namely, the Kuwait Fund and Taiwan. With the signing of the line of credit loan with the Export and Import Bank of India, this analysis takes on board India as a third bilateral creditor to Malawi.

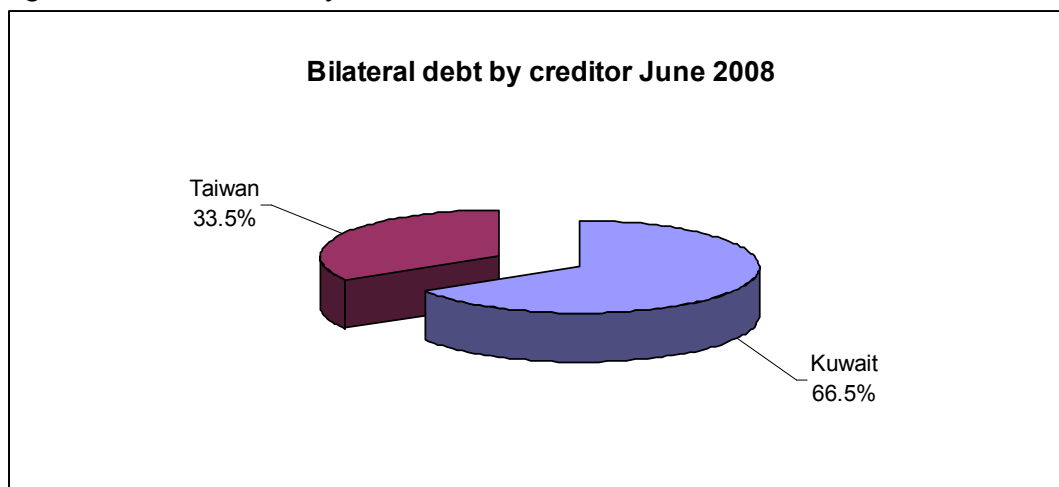
Chart 2.3: Bilateral debt by Creditor in June 2009



Source: CS-DRMS Debt Database, DAD, MoF

The Kuwait Fund continued to be the largest bilateral creditor. In proportional terms, however, Kuwait's share of debt declined from 66% in June 2008 to 54% in June 2009. This was largely due to disbursements of the India loan as opposed to the reduction in the actual debt stock owed to the Kuwait Fund. The debt to India amounted to US\$18.8 million in June 2009, representing 23% of total bilateral debt (Chart 2.3 & 2.4). Taiwan's proportion of total bilateral debt has also declined from 34% to 23% during this period.

Figure 2.4: Bilateral debt by Creditor in June 2008



Source: CS-DRMS Debt Database, DAD, MoF

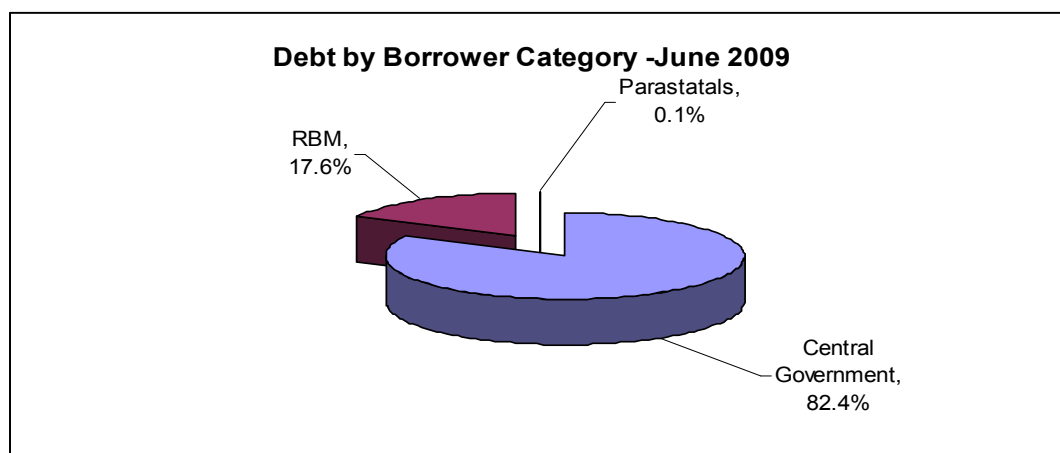
2.6 Debt Stock by Borrower Category

The main borrower categories of Malawi's debt include the Central Government, the Reserve Bank of Malawi and Public Corporations. The analysis shows that the composition of debt by borrower category has marginally changed from the previous financial year. The proportion of debt on account of Central Government has decreased from 85% in June 2008 to 82% in June 2009 whilst the share of external debt owed by the Reserve Bank of Malawi has increased from 13% to 18% across the same period. This is attributable to relatively large disbursements under the PRGF and ESF (Chart 2.6 & 2.7).

Most of the external debt is owed by the Central Government.

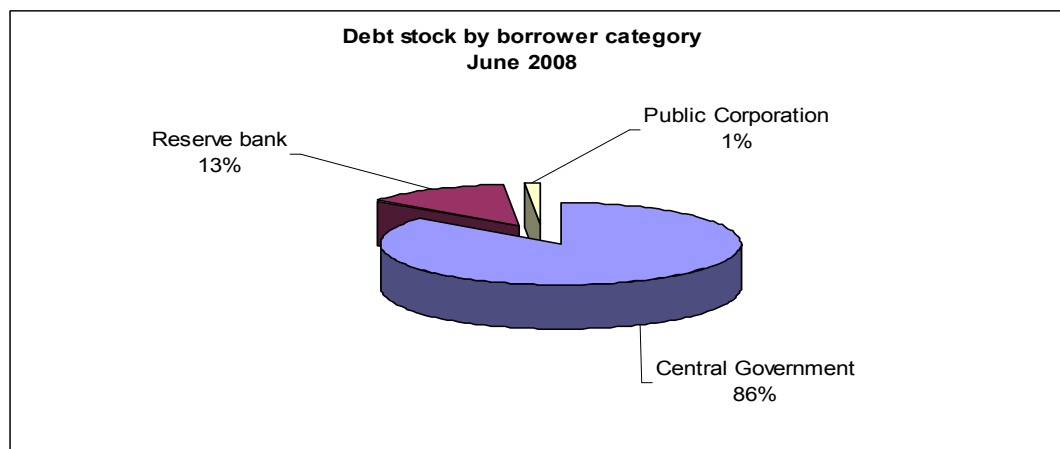
The Public Corporations debt arises from loans contracted by parastatals organizations. The proportion of such debts has declined from 1% in June 2008 to 0.1% in June 2009 (Chart 2.5 and 2.6 below) due to the increase in the share of debt owed by RBM.

Chart 2.5: Debt Stock by Borrower category in June 2009



Source: CS-DRMS Debt Database, DAD, MoF

Chart 2.6: Debt Stock by Borrower category in June 2008

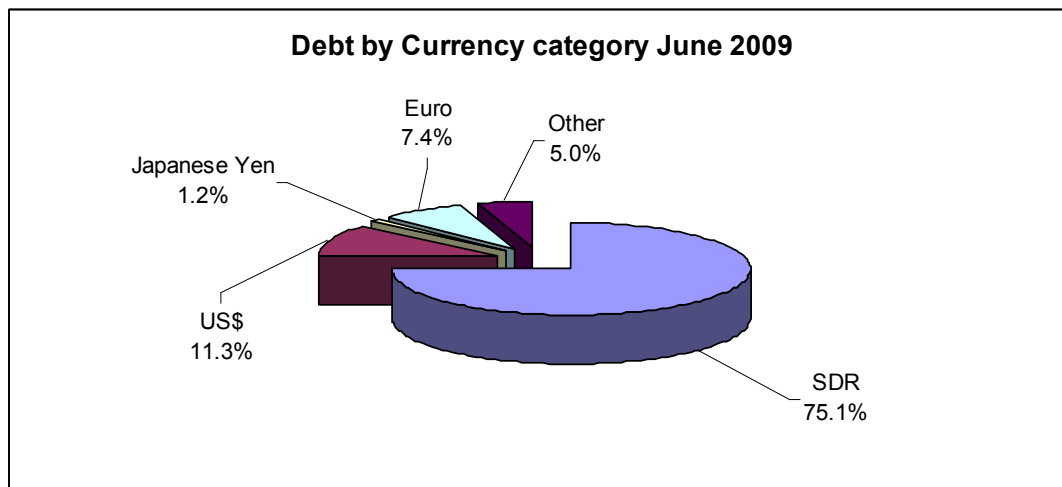


Source: CS-DRMS Debt Database, Debt and Aid Management Division, MoF

2.7 Debt Stock by Currency

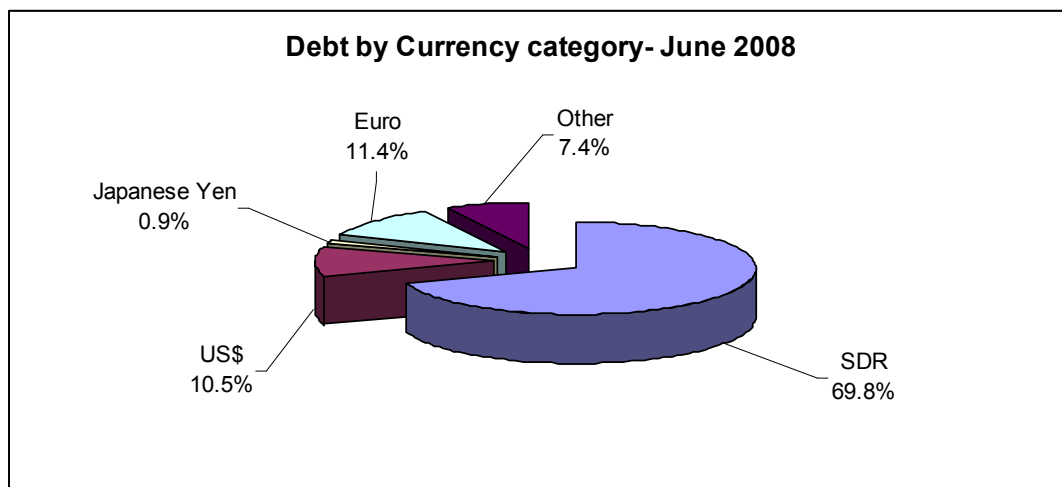
The share of debt denominated in Special Drawing Rights (SDR) rose to 75% from 69.75% in June 2008 (Chart 2.7 & 2.8). The increase was mainly due to IDA and IMF loan disbursements. The United States Dollar denominated debt also increased from 10.5% reported in June 2008 to 11.3% as a result of disbursements from India.

Chart 2.7: Debt by Currency category in June 2009 in %



Source: CS-DRMS Debt Database, DAD, MoF

Chart 2.8: Debt by Currency category in June 2008, in %



Source: CS-DRMS Debt Database, DAD, MoF

The proportion of debt denominated in Euro declined from 11.4% to 7.4% due to the increase in the SDR & US\$ denominated debts. The Japanese Yen denominated debt marginally increased to 1.2% from 1% of June 2008 as a result of disbursements from ADF project loans

Most of the external debt is denominated in SDR. The current currency composition is considered prudent.

The current currency composition is considered as desirable since the risk of currency mismatch between the debt service payments and sources of foreign exchange is minimal. Most debt service payments are made in US\$ and Euro while a large proportion of export earnings are also denominated these currencies.

Although the current currency composition is prudent, Malawi's external debt portfolio is exposed to the risk of depreciation of the local currency to the foreign currencies which would lead to increased debt service costs in Kwacha terms.

2.8 External Debt Service Payments

External debt service payments in 2008/09FY totalled to US\$14.7 million as compared to US\$9.9 million in 2007/08FY. The increase is a result of principal maturities and interest payments. Debt Service is projected to increase to US\$17.3 million in 2009/10FY as more loans are due for repayment after the expiry of grace periods.

2.9 Analysis of Debt Flows

Loan disbursements and debt service payments form the basis of the debt flows analysis. This analysis is based on net flows and net transfers on loans. Net flows are defined as loan disbursements less principal repayments that are made within the reporting year while net transfers are calculated by subtracting interest payments from net flows.

Loan disbursements totalled to US\$144.9 million in 2008/09FY, an increase from US\$73 million recorded in 2007/08FY. This is on account of disbursements under the balance of payment loans from IMF and ADF which are fast disbursing.

Principal repayments amounted to US\$9.8 million while interest payments amounted to US\$4.9 million. This implies that the net flows stood at US\$135.1 million and the net transfers at US\$130.2 million. As was the case in 2007/08FY, both net flows and net transfers were positive implying that Malawi received more disbursements from creditors compared to what was paid as principal repayments and interest payments.

2.10 Analysis of New Loans

a) Volume of Committed New Loans

New loans that were signed and approved in 2008/09FY amounted to US\$117 million. These loans were contracted from IDA of the World Bank and ADF. These

New loan commitments for 2008/09FY amounted to US\$117 million, to be disbursed over an average of 5 years

loans were contracted in support of both programme and project activities. Programme loans are contracted with the aim of financing the Government's budget gap or balance of payments gap while project loans are used to finance specific activities. One ADF loan was contracted for balance of payment support in the period under review while

the rest were project loans and were channeled to the following economic sectors: integrated rural development, water, sanitation and irrigation.

b) Interest rate structure of New Loans

All the newly contracted loans have fixed low interest rates just like the rest of the loans in the external debt portfolio. The fixed rate structure minimises the interest rate risks associated with the market interest rate fluctuations. On average, the newly contracted public sector loans have an interest rate of 0.75% compared to an average 1.5% for the entire portfolio.

c) Concessional of New Loans

In addition to the interest rate structure, concessionality is determined by the grace period and the maturity period. For the newly contracted loans, the average grace period is 10 years and the maturity period is 45 years. Based on these terms, the newly contracted loans are highly concessional with an average grant element of 69%. This is in line with Government policy which favours highly concessional borrowing.

**All new loans contracted
in 2008/09FY are highly
concessional**

CHAPTER 3: DOMESTIC DEBT PORTFOLIO REVIEW

3.1 Developments in Domestic Debt Stock

Malawi's gross domestic debt stock (at cost) increased from MK114.2 billion as of end June 2008 to MK138.1 billion as of end June, 2009. This represents an overall increase of 20.3%. This was largely due to lower than expected donor inflows especially for the months between July and November 2008. Consequently fiscal pressures were financed through domestic borrowing.

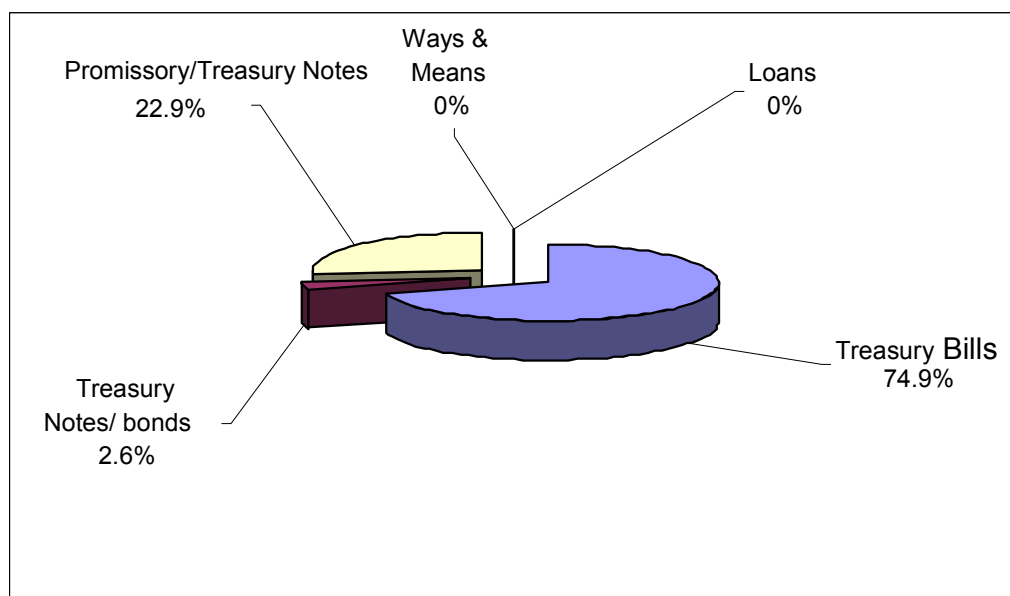
Domestic debt amounted to MK138 billion by end June 2009

3.2 Structure of Domestic Debt

As at end June 2009, Treasury Bills accounted for 74.9% of domestic debt compared to 70.3% as at end June 2008. Treasury bonds and other long term securities with maturities between 3 and 25 years accounted for 25.5% as at end June 2009 compared to 29.7% in June 2008 (Chart 3.1 & 3.2), mainly mirroring the increase in the Treasury Bills share other than the actual drop in the stock of long term securities. The share of Treasury Bills increased due to Government borrowing on the domestic market, particularly from the Reserve Bank of Malawi (RBM) through Ways and Means Advances. These were eventually converted into Treasury Bills in order to remain within the statutory limit of Ways and Means advances. Despite the fiscal pressures arising from the fiscal gap, the monetary authorities ensured that by June 2009, the outstanding ways and Means advances were zero.

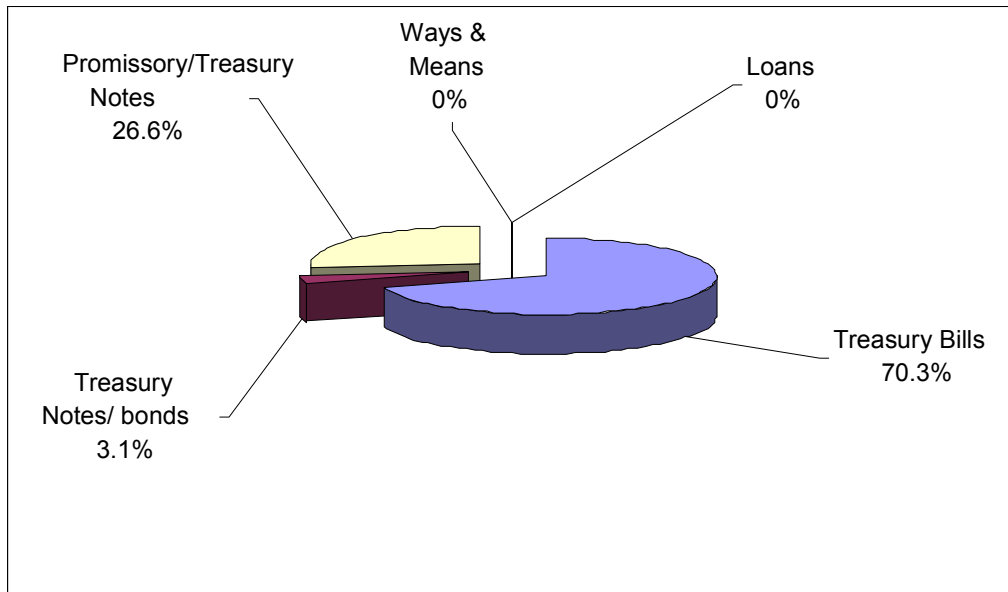
Most of the domestic debt is in the form of short term Treasury Bills, accounting for 74.9% of the debt stock as of end-June 2009

Chart 3.1: Structure of domestic debt as of end-June 2009, in %



Source: Reserve Bank of Malawi

Chart 3.2: Structure of domestic debt as of end-June 2008, in %

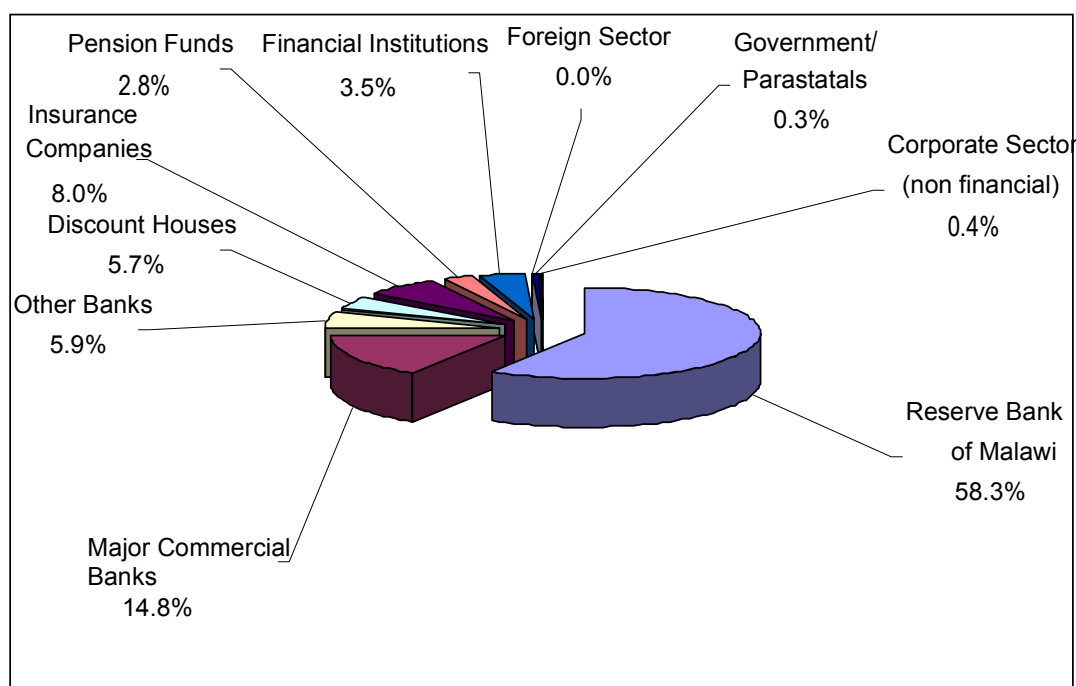


Source: Reserve Bank of Malawi

3.3 Distribution of domestic debt by holder

As at end June 2009, RBM was holding 58.3% of domestic debt compared to 48.2% as at end June 2008 (Chart 3.3 & Table 3.1). This represented an increase of 10.1% in the holding of domestic debt by the RBM mainly on account of conversion from ways and means advances. Other participants (commercial banks, insurance companies, discount houses) registered decreases in their holding of domestic debt. During the period under review, foreign investors did not participate in the domestic market.

Chart 3.3: Domestic debt by holder as of end-June 2009, in %



Source: Reserve Bank of Malawi

Table 3.1: Domestic Debt Holdings by Sector (%), 2008-2009

	June 2008	June 2009
Reserve Bank of Malawi	48.2	58.3
Major Commercial Banks	19.2	14.8
Other banks	5.0	5.9
Financial Institutions	6.4	3.5
Insurance companies	9.8	8.0
Discount Houses	5.7	5.7
Foreign Sector	2.1	0.0
Government parastatals	0.5	0.3
Corporate Sector (non financial)	0.5	0.4
Pension Funds	2.3	2.8

Source: Reserve Bank of Malawi

3.4 Treasury Bills by Tenor

The holding of 273-day Treasury Bills slightly decreased to 43.4% in June 2009 from 45.3% in the previous period. There was also a slight decrease in the holding of the 91 day Treasury Bills from 43.7% in 2008 to 42.7% in June 2009. However, the holding of 182 day Treasury Bills increased from 11.1% as at end June 2008 to 13.9% as at end June 2009. The increase in the 182 day tenor reflected investors' preference to lock their funds for a relatively moderate duration of 182 days compared to a very short duration of 91 days or relatively longer duration of 273 days.

3.5 Yields on Domestic Treasury Bills

The bank rate remained constant at 15%, during the period under review. However, Treasury Bill yields increased from an average of 11.5% in June 2008 to 12.8% in June 2009 due to a lack of liquidity in the market.

Table 3.2: Domestic Interest Rates in %: 2003-2009

Nominal Rates	2003	2004	2005	2006	Jun-07	Jun-08	June- 09
Bank Rate	35.0	25.0	25.0	25.0	20.0	15.0	15.0
91 Days	33.1	24.6	24.4	19.0	16.5	12.2	12.78
182 Days	34.0	24.6	24.5	19.4	16.4	9.6	12.82
273 Days	33.9	24.6	24.3	20.4	16.9	12.6	12.92

Source: Reserve Bank of Malawi