

**National Bank of Malawi**  
**Economic Newsletter**  
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Shadreck Malenga  
Economics Department  
National Bank of Malawi  
P.O. Box 945  
BLANTYRE.

TEL: (265) 01 820 622/01 770 480  
FAX: 01 820321  
Email: [smalenga@natbankmw.com](mailto:smalenga@natbankmw.com)  
Website: [www.natbank.co.mw](http://www.natbank.co.mw)

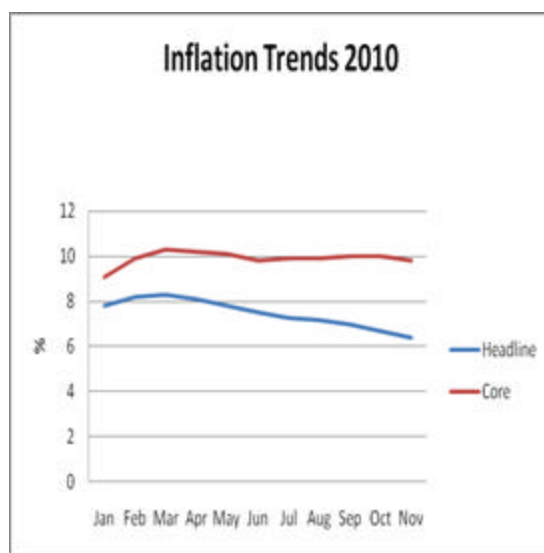
## GROWTH PROSPECTS FOR 2011

Real GDP growth is expected to slowdown in 2011 to about 6.8% from a peak of 8.6% achieved in 2008. This growth is expected to emanate from strong performances in telecommunication, construction and mining sectors. Agriculture performance which forms the mainstay of the economy is expected to rebound in 2011 from a growth rate of 1.9% recorded in 2010 to about 6.4%, according to recent National Statistics Office estimates.

Down side risks to real growth in 2011 remain the low levels of foreign exchange reserves which have severely impacted on manufacturing and potential increases in the price level as a result of recent increases in energy prices and other utilities.

### INFLATION

Headline inflation continues to trend downwards standing at 6.4% in November 2010 from 6.7% the previous month due to abundant food supplies. This notwithstanding, there is evidence



of upward pressure in prices evidenced by the diverging core inflation from headline inflation data as can be observed from the figure titled Inflation Trends 2010 above. Core inflation has averaged 9.9% in the year January to November 2010 perhaps reflecting the success of the fertilizer subsidy programme whose resultant effect of bumper harvests has led to marked reduction in food prices hence masking the overall increasing prices of other essential goods and services.

The above notwithstanding, upward pressure on the price level is expected to significantly increase on the back of electricity and water tariff increases in Q4: 2010 coupled with the more recent fuel price increase as well as expansion of credit due to relatively low interest rates. Crucially, the timing of the fuel price increase may reflect the authorities' desire to maintain overall prices low as its lagged effects may coincide with onset of the 2011 harvest. As a result, average headline inflation this year can be expected to remain moderate and within a single digit figure of around 8% .

### MONETARY DEVELOPMENTS

The tight liquidity conditions which characterized 2010 have eased as reflected in interbank rates of as low as 2% in January 2011. The loose liquidity conditions have led to declining short term interest rates in the money markets with the 91, 182 and 273 day tenor Treasury Bills yielding 6.32%, 6.80% and 6.54% respectively according to the results an auction held on 1 February 2011.

The reduction of the bank rate to 13% in August 2010 has also resulted in the expansion of credit to private sector. The relatively liquid money markets in 2011 are likely to spur credit growth further thus exerting pressure on overall prices and foreign exchange demand. As a result, the monetary authorities are likely to resist any reduction in the bank rate until perhaps Q3: 2011 when the effects of the recent energy price increase and other inflationary pressures alluded to above are quantified.

## EXCHANGE RATES

The high economic growth rates experienced in recent years have meant relatively high incomes. Growing incomes have led to the continued imbalance between the growth of imports over exports leading to the widening of the current account deficit. Weak balance of payments continues to threaten the exchange rate thus increasing pressure on the authorities to re-align the exchange rate.

The fragility of the economy is perhaps being powerfully demonstrated by the import cover statistics which have been consistently below the recommended 3 months of imports. Import cover improved in the third week of January with USD401 million or 3.11 months of imports recorded on 21 January 2011. However, this situation was short lived as USD385 million or 2.98 months of imports was recorded the following week on 28 January 2011, evidence that forex demand far outstrips supply. As a result, forex queues are still a feature in commercial banks operating in the country. This scenario notwithstanding, the authorities are likely to maintain the de facto pegging of the

Kwacha to the USD and thus the Kwacha is likely to trade around K150/1USD for the time being. If however, foreign exchange reserve targets are missed within the context of the Extended Credit Facility with the IMF, then the exchange rate may be re-aligned to around MK165/1USD in the course of the year.

## SUMMARY OF PROSPECTS FOR 2011

The biggest threat to growth prospects in 2011 remains high foreign exchange demand that has characterized the economy for the past year or so. Below par reserves positions offer little comfort and the fact that initial estimates indicate excess supply of tobacco in the 2011 auction season implies average prices of below USD2/Kg. Poor performance of tobacco may have implications for the exchange rate and hence overall prices because the USD exchange rate is effectively an anchor for overall prices.

In addition, inflationary expectations resulting from tariff increases for utilities and high international oil prices pose significant risks to inflation. As a result, the authorities are expected to maintain tight fiscal and monetary policies in the first half of 2011 at least.

### SELECTED ECONOMIC INDICATORS

INDICATOR	UNIT	2008	2009	2010	2011
GDP at current market prices	MK billion	600.3	702.3	819.4	942.9
GDP per capita	USD bn	312.8	356.4	366.5	389.5
Population	million	13.1			
Real GDP growth	%	8.6	7.6	7.1	6.8
Inflation ( average )	%	8.7	8.4	7.5	8.3
Bank rate	%	15	15	13	13
Money supply ( M 2 )	% CHANGE	33.1	19.4	16.7	13.9
Import Cover	Months	3.4	1.4	2.1	2.1
Foreign debt	% GDP	16	19.1	21.8	23.3
Domestic debt	% GDP	19	20.3	14	11
Fiscal balance	% GDP	-1.0	-1.8	4.4	3.6
Current account	% GDP	-6.4	-8.6	-1.8	-2.2

Source: NSO, RBM, NBM, IMF