

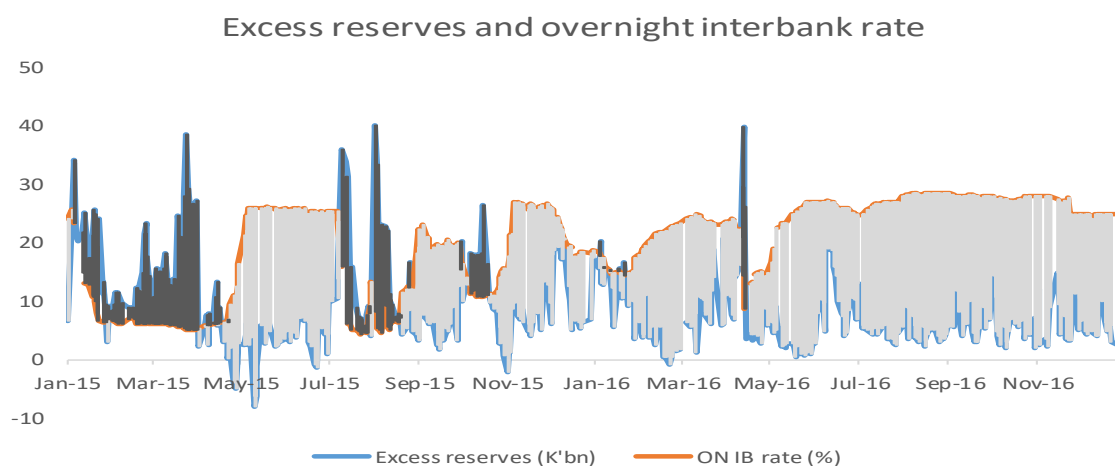


**Annual economic review, 2016**

**Investment banking department**

## 1. Interbank market and interest rates

- 1.1 Liquidity conditions on the interbank market were erratic but generally tight in 2016. Excess reserves averaged K7.33 billion per day compared to K10.83 billion per day in 2015. Excess reserves were lowest at negative K0.82 billion in February and were the highest in April prior to the opening of the tobacco auction season. As a result of tight liquidity conditions that prevailed during the year, the overnight interbank rate remained high, averaging 24.46% from 15.31% in 2015.
- 1.2 Overnight interbank borrowing increased to a daily average of K5.12 billion from an average of K4.26 billion in 2014. Access on the Lombard Facility of the Reserve Bank of Malawi (RBM) (also known as the discount window facility of the Central Bank) also increased to a daily average of K6.94 billion per day and totaled K1.62 trillion, compared to a daily average of K3.39 billion and a total of K799.94 billion observed in 2015.

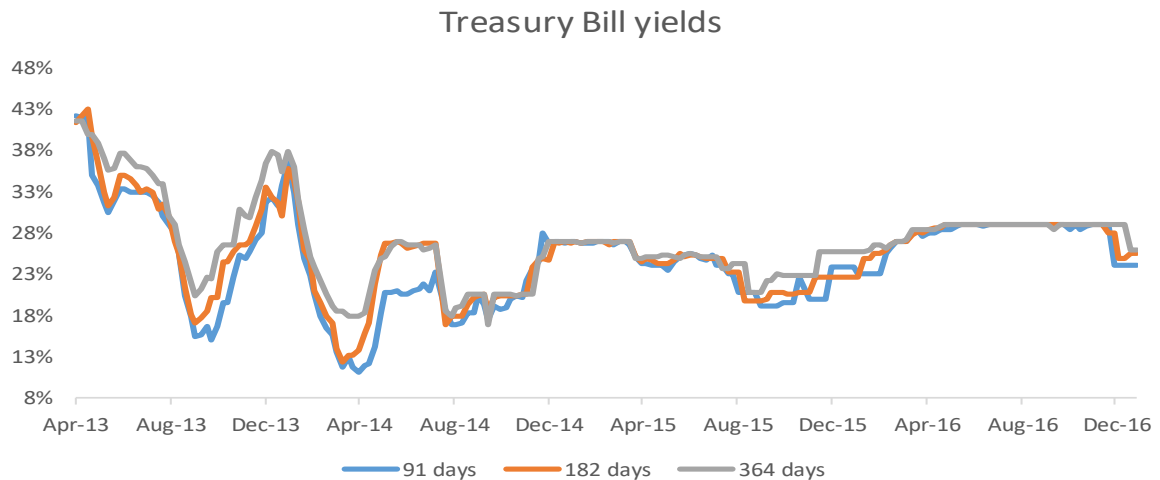


Source: RBM

- 1.3 At the 4<sup>th</sup> Monetary Policy Committee (MPC) meeting for 2016 held from 23 and 24<sup>th</sup> November 2016, the committee resolved to reduce the Policy Rate from 27% to 24%. The decision was influenced by a positive outlook on inflation which was expected to decelerate to about 18.6% by June 2017. The MPC noted that consistent implementation of a tight monetary policy stance and the actions taken by government to reduce fiscal pressure including from the farm input subsidy programme (FISP) operations and from ADMARC's maize operations have combined to reduce inflationary expectations.
- 1.4 Following the reduction in the Policy Rate, the overnight interbank rate declined from about 28% to 25%, while the Lombard rate automatically declined to 26%. Commercial banks also revised their base lending rate and currently commercial banks' base lending rates range between 32.0% and 35.0% (2015:34.0% and 38.0%).
- 1.5 Looking ahead we expect the interbank rate to remain close to policy rate amid continued tight liquidity conditions as authorities intensify mop up operations to withdraw liquidity injected from expansionary government operations. It is a stated intention of the RBM to keep the interbank rate close to the policy rate.

## 2. Treasury Bills

- 2.1 During the year, authorities managed to raise K367 billion compared to K376 billion raised in 2015. Total applications stood at K429 billion, representing a 14% rejection rate (2015: 26%). Treasury bill yields were high in 2016, with the all type Treasury Bill yield averaging 27.87% from 23.96% in 2015. However, following the reduction in the Policy rate, Treasury Bill yields declined, and currently oscillate around the policy rate of 24%.



Source: RBM

- 2.2 Looking forward, Treasury Bill yields are expected to stabilize around the policy rate supported by government's high appetite for domestic borrowing and investors' need to earn positive returns in environment of high inflationary pressures.

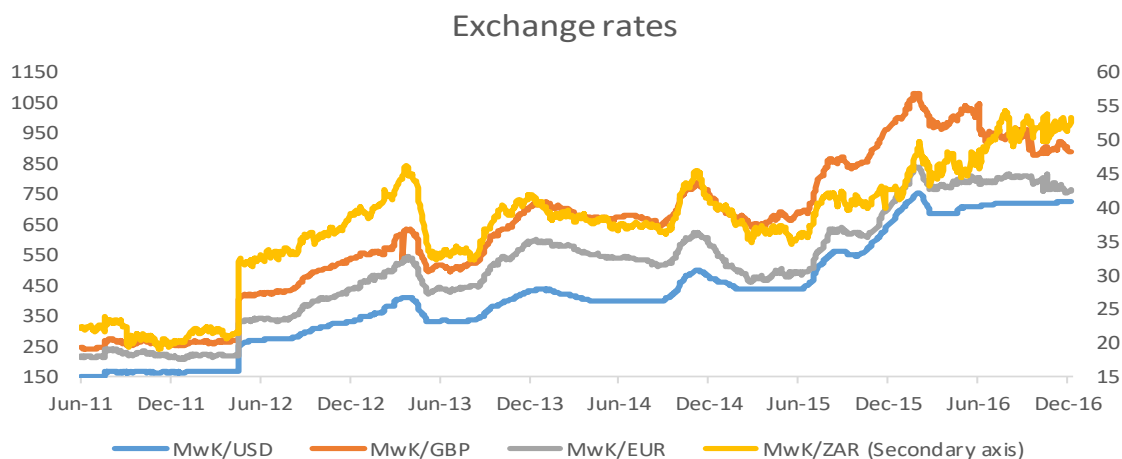
### 3. Exchange rates

- 3.1 The Kwacha was relatively stable in 2016. The Kwacha depreciated by 9%, 5% and 25% against the USD, EUR and ZAR respectively but appreciated by 10% against the GBP in 2016. This is an improvement from 2015 when the local currency depreciated by 41%, 34%, 27% and 5% against the USD, GBP, EUR and ZAR respectively.

	<b>30-Dec-16</b>	<b>31-Dec-15</b>	<b>30-Dec-14</b>	<b>2016</b>	<b>2015</b>
				<b>change</b>	<b>change</b>
USD	725.0093	664.3650	471.6971	↓ 9%	↓ 41%
GBP	890.3839	984.3232	731.9324	↑ -10%	↓ 34%
EUR	763.5798	726.3503	573.2063	↓ 5%	↓ 27%
ZAR	53.2829	42.6975	40.5848	↓ 25%	↓ 5%

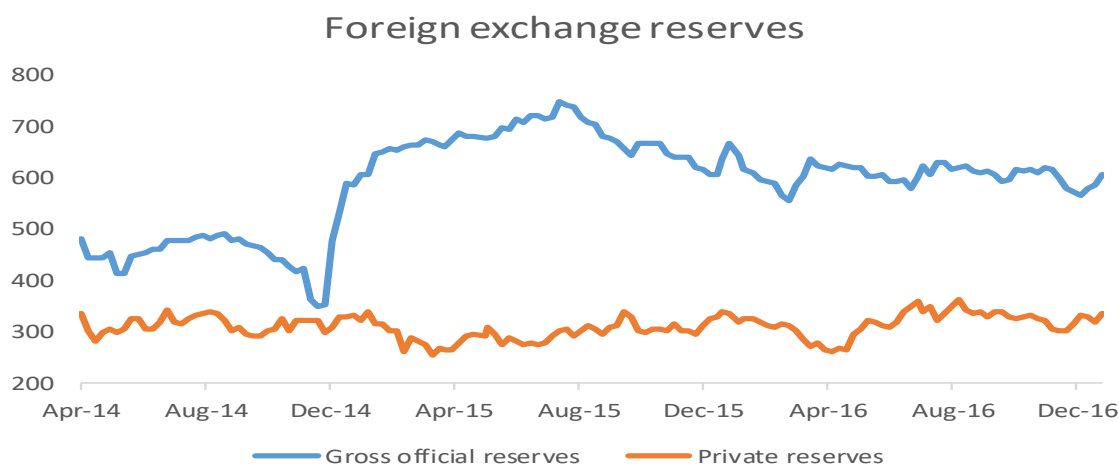
Source: RBM

- 3.2 The stability of the Kwacha in 2016 has been attributed to the monetary authority's consistent implementation of a tight monetary policy stance and actions taken by government to reduce fiscal pressures. Additionally, the country's official foreign exchange reserves remained at about 3 months of imports.
- 3.3 Looking ahead, we expect the Kwacha to slightly depreciate in the medium term. In the long term, the Kwacha is expected to depreciate further do to trade imbalances, current account deficits and increasing imports.



Source: RBM

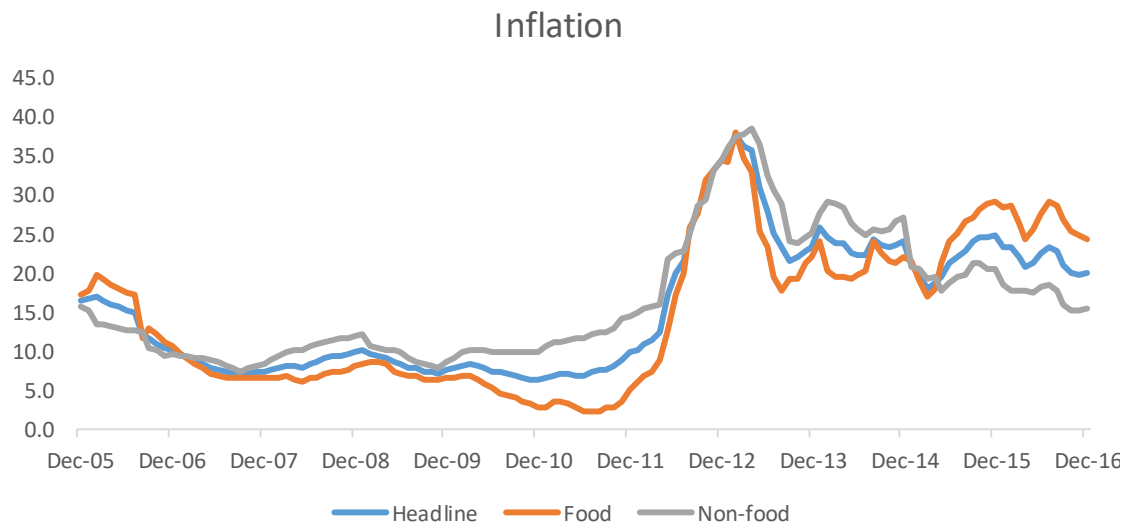
3.4 Gross official reserves were observed at USD606.93mn (2.90 months of imports) on 30<sup>th</sup> December 2016, 8.9% lower than USD666.07 mn (3.19 months of imports) observed at the end of 2015. Private reserves were observed at USD336.61mn (1.61 months of imports) from USD334.42 mn (1.62 months of imports).



Source: RBM

## 4. Inflation

4.1 Headline inflation for 2016 decreased to 21.7% from 21.9% in 2015, kept up by rising prices of food items following poor performance of the agricultural sector in the 2014/2015 and 2015/2016 growing seasons. Food inflation for 2016 stood at 26.6% from 23.9% in 2015 while non-food inflation decreased to 17.1% from 20.0% in 2015. Headline inflation for December 2016 stood at 20.1% from 24.9% in December 2015.



Source: NSO

4.2 Looking ahead, inflationary pressures are expected to decelerate in 2017 contingent upon expected better food yield. Preliminary crop estimates indicate a better yield in 2017. Coupled by the availability of maize in ADMARC markets from the last harvest, food inflation is expected to significantly decline. Risks on inflation outlook however remain on non-food inflation which could potentially increase due to exchange rate depreciation as well as potential increases in oil prices.

## 5. Stock market

5.1 The local bourse has generally been bearish in 2016, with the Malawi All-Share Index (MASI) losing 8.5% year to date, driven by price losses in 6 counters which were enough to more than offset price gains registered in the other counters. Of particular interest are the two companies operating hotel businesses namely Blantyre Hotels Limited (BHL) and SUNBIRD who registered impressive HPR's of 109% and 154% respectively. On the other hand, all financial services companies with the exception of FMB suffered significant losses. ILLOVO also registered significant losses over a prolonged period of time while TNM and PCL were fairly stable.

	30-Dec-16	31-Dec-15		Capital gain
MASI	13,320.51	14,562.53	↓	-8.5%
DSI	10,456.92	11,462.87	↓	-8.8%
FSI	2,026.07	1,762.13	↑	15.0%
<b>Gainers</b>				
SUNBIRD	58.50	23.00	↑	154.3%
BHL	20.10	9.60	↑	109.4%
FMB	17.00	14.00	↑	21.4%
OLM	1,612.00	1,402.00	↑	15.0%
STANDARD	500.00	440.00	↑	13.6%
PCL	540.00	535.00	↑	0.9%
TNM	6.05	6.00	↑	0.8%
<b>Losers</b>				
NBS	6.00	23.00	↓	-73.9%
NICO	17.00	28.00	↓	-39.3%
NITL	34.00	55.00	↓	-38.2%
ILLOVO	160.00	230.00	↓	-30.4%
NBM	237.12	258.00	↓	-8.1%
MPICO	7.83	8.20	↓	-4.5%

Source: MSE

5.2 Several listed companies released trading statements for the year 2016. The following table presents a summary of their expected results.

BHL	Blantyre Hotels Limited advised that the profit after income tax for the year ending 30 September 2016 is likely to be 20% higher than the previous financial year.
FMB	First Merchant Bank Limited advised that its forecast profit attributable to shareholders for the financial year ending 31 December 2016 is expected to be at least 40% higher than achieved for the financial year ended 31 December 2015.
ILLOVO	The company advised that profit after tax for the year ended 30 March 2017 is expected to be at least 60% higher than the prior period.
MPICO	MPICO informed all shareholders and the general public that Group's profit for the year ended 31 December, 2016 is expected to increase by over 100% above the previous corresponding period.
NBM	National Bank of Malawi advised shareholders that profit after tax for the year ending 31 December 2016 is expected to be at least 25% higher than the previous financial year.
NBS	NBS Bank Limited advised that its forecast loss attributable to shareholders for the financial year ending 31 December 2016 is expected to be at least 20% higher than that for the financial year ended 31 December 2015.
NICO	NICO Holdings advised that profit after tax for the year ending 31 December 2016 is expected to be lower than the previous corresponding period by more than 20%.

NITL	NITL advised that the financial performance for the 12 months ending 31 December 2016 is expected to be more than 200% lower than the previous 15 months period ended 31 December 2015
PCL	Press Corporation Limited advised that profit after tax for the year ending 31 December 2016 is expected to be at least 20% higher than the previous corresponding period.
STANDARD	Standard Bank Limited advised that the forecast profit after tax for the financial year ending 31 December 2016 will likely be 30% above the previous corresponding period.
SUNBIRD	Sunbird Tourism Limited announced that its profit after tax for the period ending 31 December 2016 is expected to exceed the previous corresponding period by more than 25%.
TNM	Telekom Networks Malawi Limited advised that profit after tax for the period ending 31 December 2016 is expected to be at least 20% higher than the previous corresponding period.

Source: MSE

## 6. Economic growth

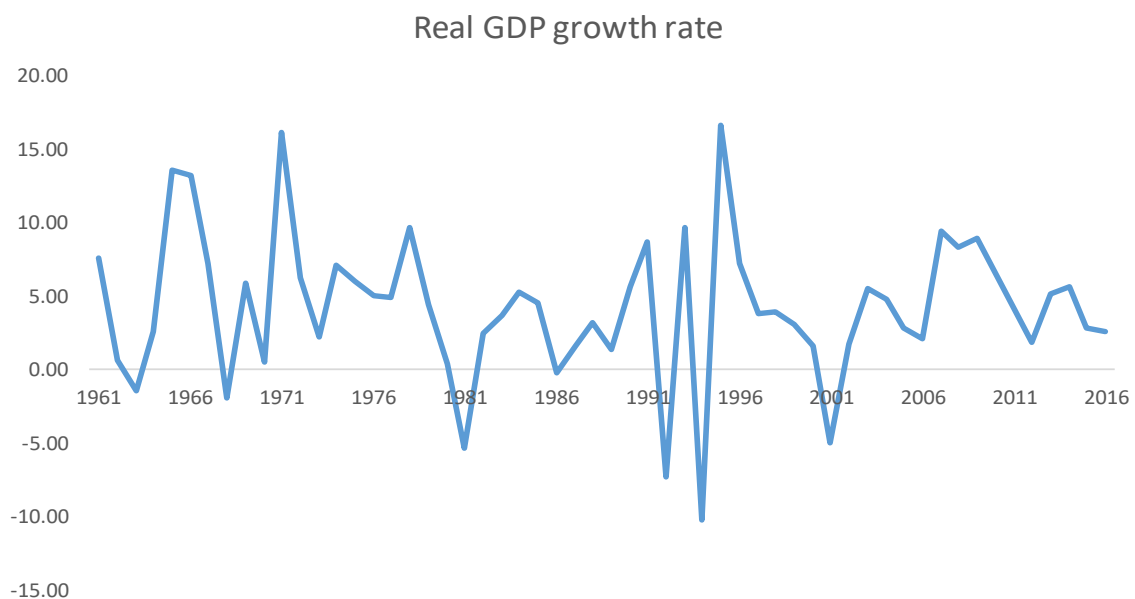
6.1 Real GDP growth for 2016 is estimated at 2.60% by the World Bank and 2.90% by the Government of Malawi. The low growth is due to the low agricultural output during the 2015/16 season because of El Nino weather conditions.

### Real Economic Growth Projections to 2018

	2015	2016	2017	2018
EIU	2.90%	2.50%	3.80%	4.70%
IMF	2.95%	2.95%	4.00%	5.50%
World Bank	2.80%	2.60%	4.10%	5.40%
Malawi Government	3.30%	2.90%	5.60%	

6.2 Risks to economic growth in 2017 are the high inflation rates, high lending interest rates and insufficient power supply which slow down economic growth as they reduce private sector activity. Lower global commodity prices and uncompetitive and falling exports also add to the risks. High government debt levels may also keep interest rates high and crowd out private sector funding for growth.

6.3 Economic growth is forecast to average 4.75% in the period 2017-2018. This will be possible if the economy recovers as a result of Government exercising tight control over public expenditure, implementation of tight monetary policy stance and reforms in fiscal management.



Source: World Bank

## 7. Commodities

### 7.1 Tobacco

7.1.1 The 2016 tobacco market underperformed in terms of turnover by about 17% in when compared to 2015, despite registering slightly higher volumes of tobacco sold. The tobacco market was extended to 38 weeks in an effort to clear volumes of unsold tobacco left by the 24<sup>th</sup> week, which is the convectional closing week. The tobacco market registered turnover of USD276.39 million (2015: USD331.92 million) from 195,124,994 kilograms of tobacco sold (2015: 184,521,055kg) at an average price of USD1.42 (2015: USD1.76).

	2016	2015	2014	2016/2015 change
Volume (kg)	195,124,994	184,521,055	188,897,790	5.7%
Turnover (USD)	276,389,957	331,924,169	359,276,180	-16.7%
Average price (US cents/kg)	141.65	176.36	188.49	-19.7%

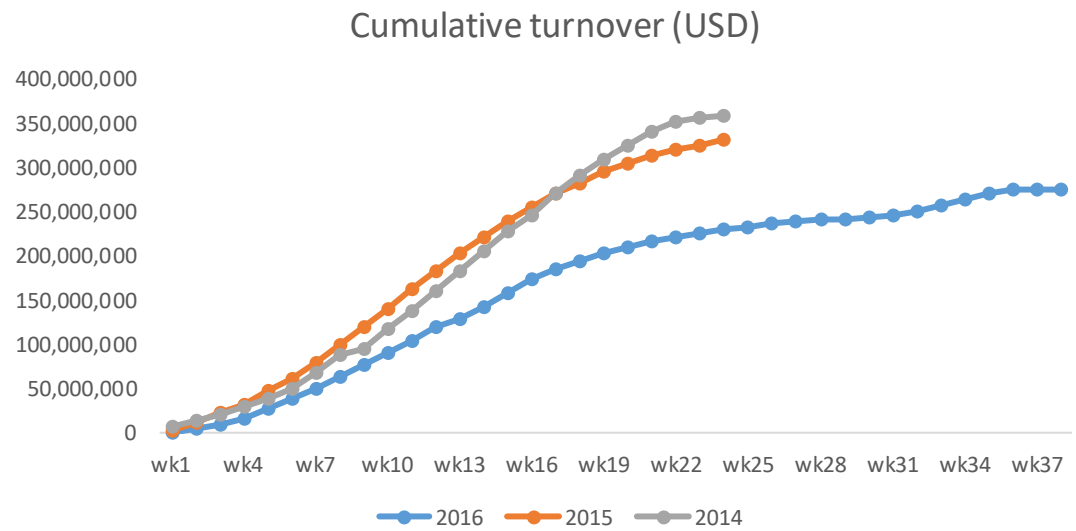
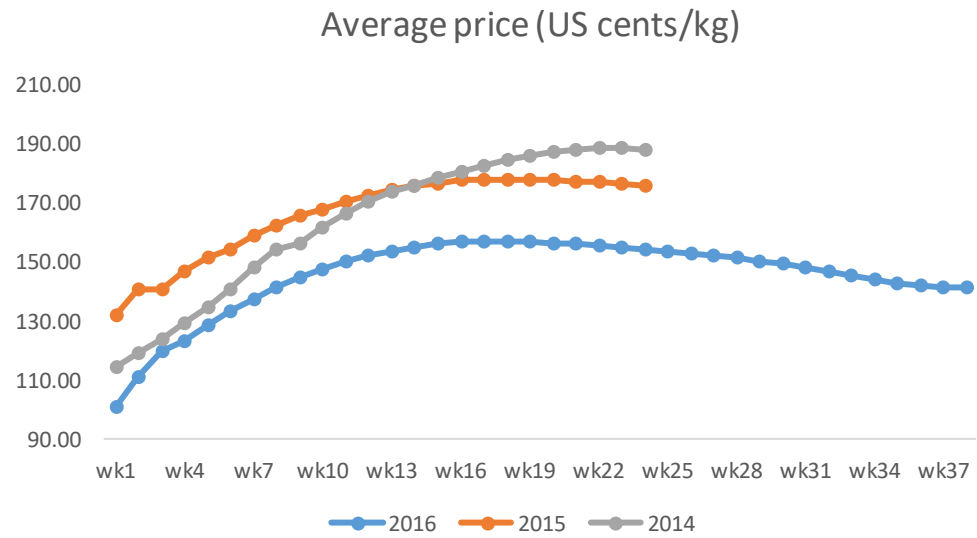
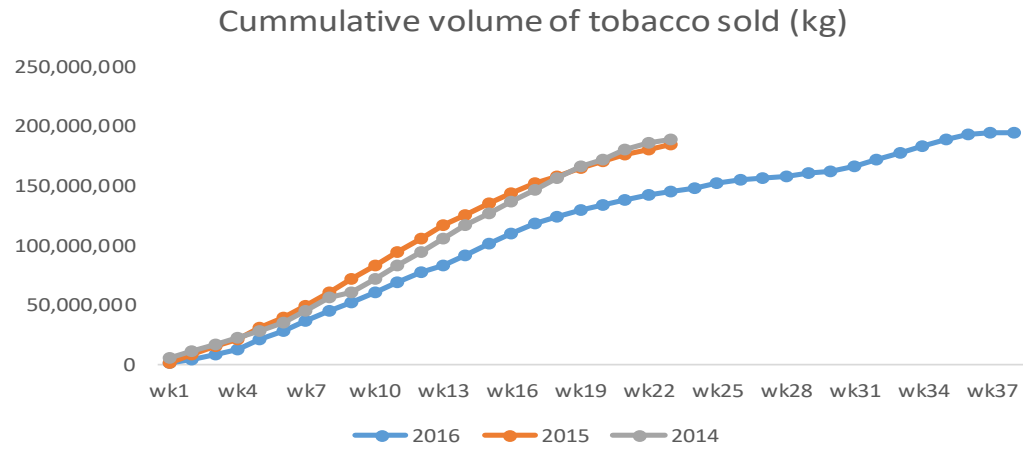
Source: Tobacco Control Commission (TCC)

7.1.2 The 2016 tobacco market was marred by poor prices and high rejection rates. This forced the authorities to extend the auction indefinitely while also abolishing the minimum price in an attempt to ensure that the tobacco sells.

7.1.3 The underperformance of tobacco has significant effects on the economy since tobacco accounts for a significant portion of Malawi's export proceeds (about 50%).

7.1.4 We present below charts showing week on week movement of tobacco volumes, prices and revenues to week 38 for the year 2016, and to week 24 for 2014 and 2015.





Source: TCC

## 7.2 Cotton

Cotton output in 2016 has fallen by about 33% to 15,000 metric tons relative to last year's production largely due to the dry spell.

## 7.3 Fuel

7.1 The Malawi Energy Regulatory authority(MERA) adjusted fuel prices three times in 2016, all of which were upward adjustments.

7.2 The most recent adjustment was in November 2016. Following developments in the international price of oil as well as local exchange rate developments, MERA observed that landed cost of petrol, diesel and paraffin increased by 11.02%, 18.66% and 16.37% respectively. According to the Automatic Fuel Pricing Mechanism (APM), these qualified for an upward price revision since the landed cost was beyond the  $\pm 5\%$  trigger limit.

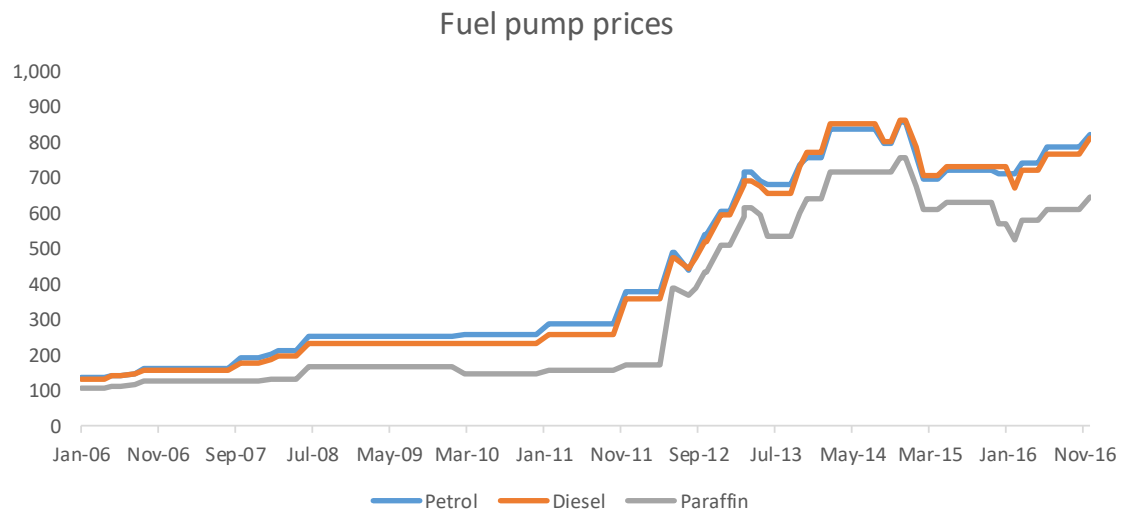
7.3 Consequently, MERA resolved to pass on only 50% of increases in the landed costs on the pump price to consumers effective 4<sup>th</sup> November 2016, while the remaining 50% will be absorbed through the Price Stabilization Fund (PSF) to cushion consumers.

7.4 We present below a table showing the changes in petroleum prices.

<i>Kwacha/liter</i>	Nov-16	Jun-16	Mar-16	Dec-15
Petrol	824.7	788.3	743.3	711.9
Diesel	815.8	766.9	722.8	734.7
Paraffin	648.7	609.8	580.4	573.1

Source: MERA

7.5 We present below a chart showing historical fuel pump prices since September 2006.



Source: MERA

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