



Economic update – 2019 Q1 to date

Investment Banking

12th March 2019

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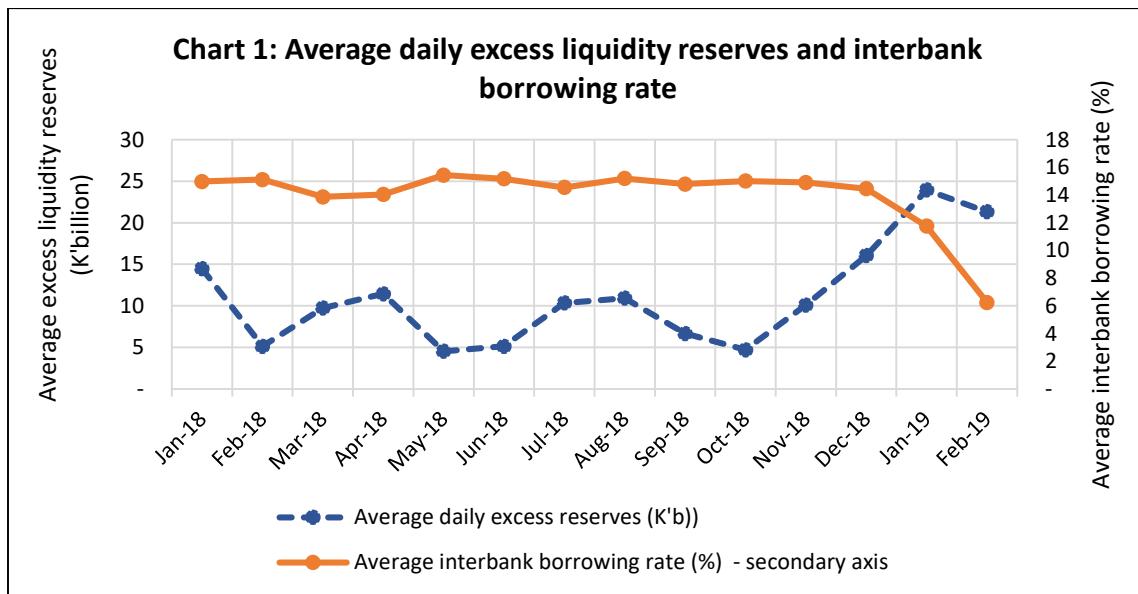
1. Interbank market

1.1 The Reserve Bank of Malawi (RBM) made significant monetary policy changes in January 2019, including the reduction of the Policy Rate (PR) from 16.0% to 14.5%; the reduction of the Liquidity Reserve Requirement (LRR) ratio from 7.5% to 5.0% for domestic currency deposits and from 7.5% to 3.75% for foreign currency deposits; the reduction of the Lombard rate from 18.0% to 14.9%; and the pegging of the Base lending rate for commercial banks to the Lombard rate. These policy changes led to a significant increase in the level of liquidity on the interbank market and a decrease in various market interest rates during the first two months of 2019 under review. These policy changes are discussed in detail in Section 5 of this report.

1.2 Excess liquidity reserves for banks increased from an average of K16.05b per day in December 2018 to K23.95b per day in January 2019 and K21.31b per day in February 2019, which were much higher compared the average volume of K14.48b per day recorded in January 2018 and K5.14b per day recorded in February 2018.

1.3 On account of high liquidity levels, coupled with the reduction in the Policy and Lombard rates, the interbank borrowing rate decreased from the average of 14.45% in December 2018 to the average of 11.75% in January 2019 and 6.24% in February 2019. In 2018, the interbank borrowing rate averaged 14.97% in January and 15.12% in February.

1.4 Chart 1 provides a summary of excess liquidity reserves and overnight interbank rate movements over the past year.



(Source: Reserve Bank of Malawi)

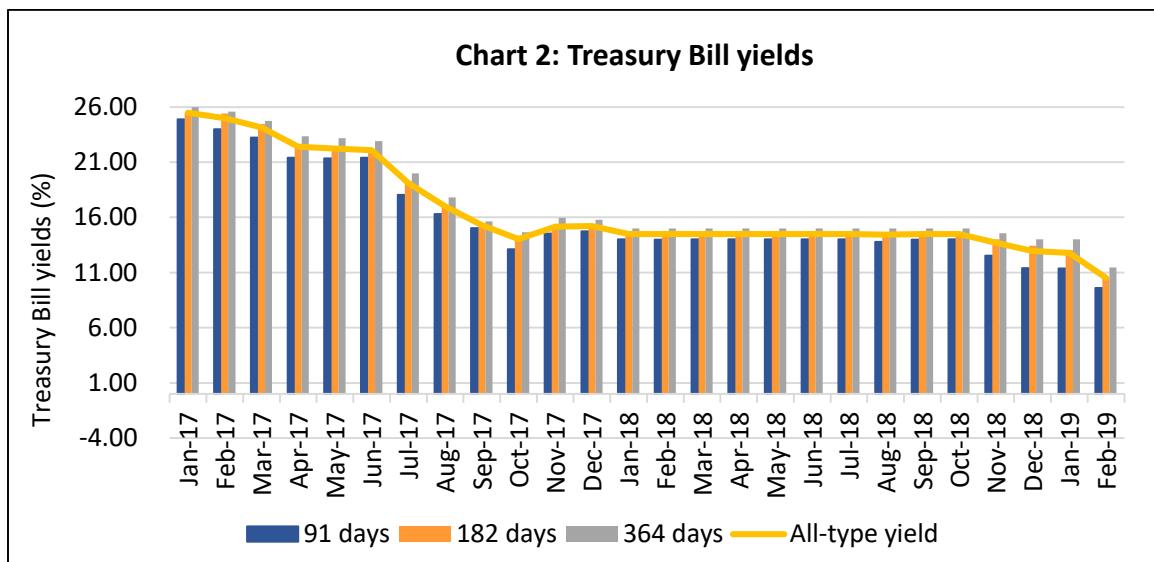
- 1.5 The volume traded among banks on the interbank market increased by 3.55% from the average of K8.84b per day in December 2018 to the average of K9.15b per day in January 2019 and later decreased by 4.13% to the average of K8.78b per day in February 2019.
- 1.6 Further, in line with higher liquidity levels, access to the Lombard facility decreased from a total of K37.46b in December 2018 to a total of K15.30b in January 2019 and K11.40b in February 2019. In the previous year, access to the Lombard facility totaled K78.96b in January 2018 and K96.90b in February 2018.
- 1.7 The Lombard rate decreased from 18.00% in December 2018 to the average of 17.38% in January 2019 and 14.90% in February 2019. The Lombard rate was at 18.00% in the previous corresponding period, namely January and February 2018.
- 1.8 While there were no Open Market Operations (OMOs) in December 2018, RBM withdrew from the market a total of K2.5b at the average rate of 12.50% in January 2019 and a total of K45.14b at the average rate of 10.43% in February 2019. In 2018, OMOs amounted to K100.71b at the average rate of 14.99% in January and K61.15b at the average rate of 15.00% in February.

2. Government securities

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- 2.1 Government raised a total of K78.42b in January 2019 and K55.89b in February 2019 during auctions for Treasury Bills (TB), registering a significant increase when compared to a total of K25.23b raised in December 2018, K25.48b in January 2018 and K35.13b in February 2018. Total applications for TBs for January 2019 and February 2019 amounted to K100.09b and K67.65b, representing rejection rates of 22% and 17%, respectively, which are higher than rejection rates of 9.57% recorded in December 2018, 3.84% in January 2018 and 1.89% in February 2018.
- 2.2 TB yields declined in the period under review following the reduction of the Policy rate and the Lombard rate by RBM on 30th January 2019. The 91-day TB yield decreased from the average of 11.41% in December 2018 to the average of 11.36% in January 2019 and 9.61% in February 2019; the 182-day yield decreased from the average of 13.44% in December 2018 to the average of 13.01% in January 2019 and 10.50% in February 2019; and the 364-day yield decreased from the average of 14.01% in December 2018 to the average of 14.00% in January 2019 and 11.47% in February 2019. Consequently the all-type (average) TB yield decreased from 12.96% in December 2018 to 12.79% in January 2019 and 10.52% in February 2019. During a corresponding period in the previous year, TB yields were higher, with the 91-day yield at 14.00% in January 2018 and 13.97% in February 2018; the 182-day yield at 14.50% in both January 2018 and February 2018; and the 364-day yield at 15.00% in January and February 2018; resulting in an all-type yield of 14.50% in January 2018 and 14.49% in February 2018.

2.3 Chart 2 shows that after remaining broadly stable in 2018, TB yields resumed the declining trend towards the end of the year- a phenomenon that has been registered since 2017. The decline has been influenced by reductions in the Policy rate, the most recent on 30th January 2019.



(Source: Reserve Bank of Malawi)

2.4 In the period under review, there were also auctions for Treasury Notes (TN), particularly 2-year, 3-year and 7-year TNs. Through these auctions, the Government raised a total of K51.47b in January 2019 and K8.93b in February 2019 at the average yield of 17.32% for the 2 year TN, 14.77% for the 3-year TN and 24.00% for the 7-year TN. In December 2018, the Government raised a total K15.37b through auctions for 5-year and 7-year TNs at the average yield of 20.50% and 24.00%, respectively.

2.5 Looking ahead, yields on Government securities are expected to continue to decline in the near term before stabilizing later in the year when the market fully responds to the policy changes.

3. Foreign exchange market

3.1 The Kwacha was broadly stable against the USD in January 2019 and February 2019, with the USD/MWK exchange rate averaging 735.96 in January 2019 and 735.83 in February 2019, appreciating marginally from the average of 736.44 recorded in December 2018. The Kwacha, however, depreciated albeit marginally against the GBP and ZAR during the two months as the GBP/MWK exchange rate increased from 931.14 in December 2018 to 944.19 in January 2019 and 956.15 in February 2019; and the ZAR/MWK exchange rate increased from 50.54 December 2018 to 53.00 in January 2019 and 53.29 in February 2019. When compared to a

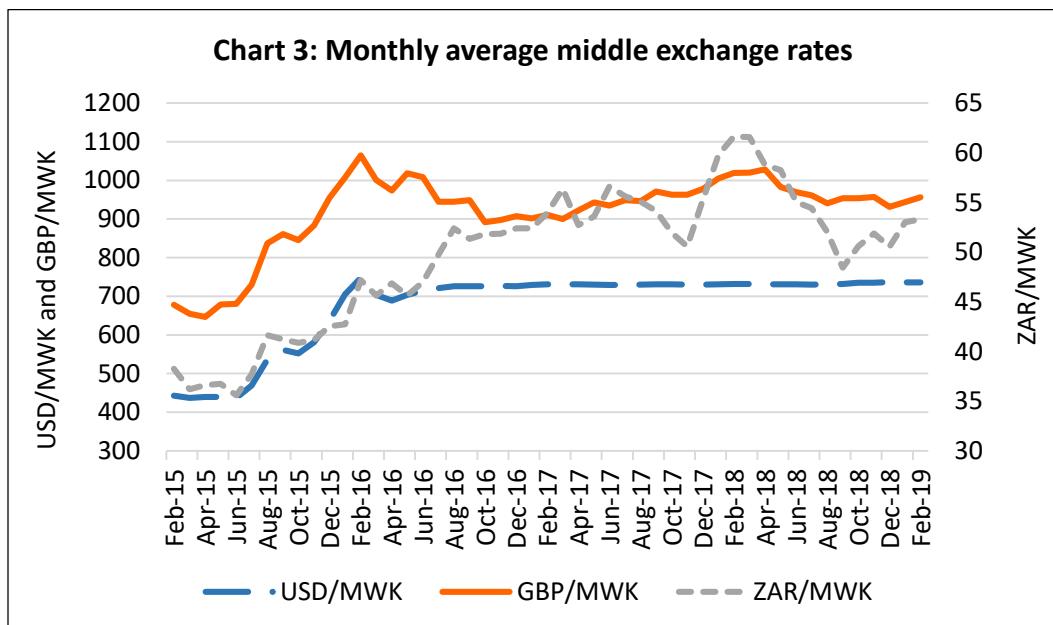
corresponding period in the previous year, the Kwacha depreciated by 0.59% against the USD and appreciated by 6.17% against GBP and by 13.55% against ZAR.

3.2 Table 1 and Chart 3 below provide an overview of how the Kwacha has fared against the three major trading currencies in the last four years.

Table 1: Average middle exchange rates							
Currency	Feb-19	Jan-19	Dec-18	Feb-18	M-O-M Change	Y-O-Y Change	YTD Change
USD	735.83	735.96	736.44	731.49	▲ -0.02%	▼ 0.59%	▲ -0.08%
GBP	956.15	944.19	931.14	1019.05	▼ 1.27%	▲ -6.17%	▼ 2.69%
ZAR	53.29	53.00	50.54	61.64	▼ 0.55%	▲ -13.55%	▼ 5.44%

Source: Reserve Bank of Malawi

Note: Upward arrow represents appreciation and downward arrow represent depreciation of the Kwacha.

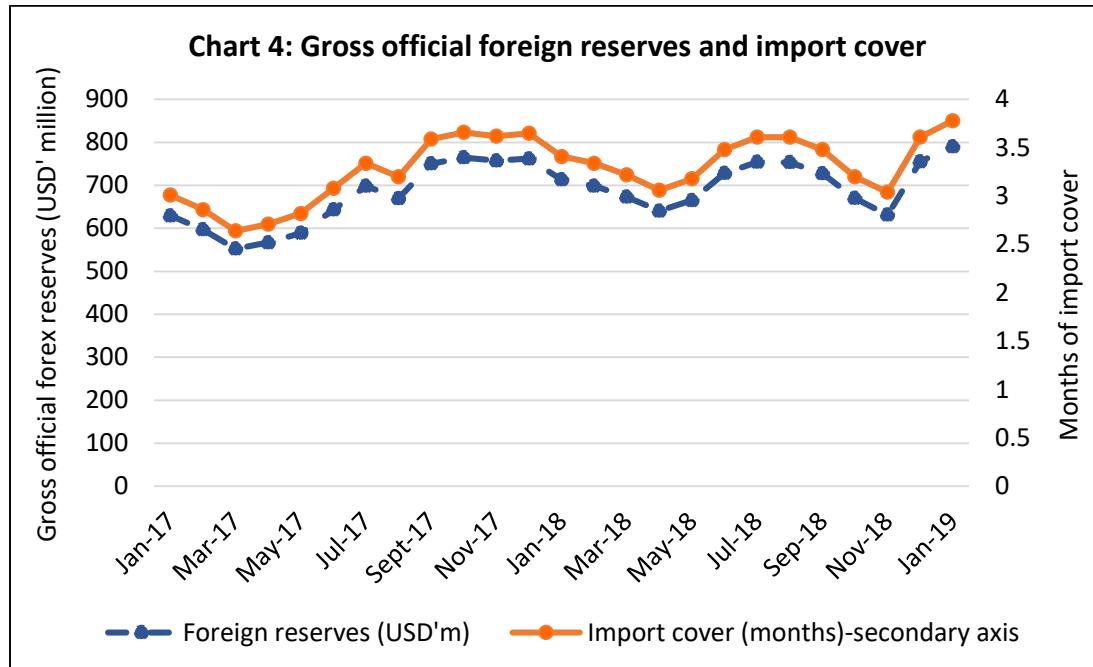


(Source: Reserve Bank of Malawi)

3.3 The continued stability of the Kwacha against the USD during the review period could be attributed to stronger confidence in the Kwacha from market players, robust forex reserves which ensured consistent availability of forex on the market and tight monetary conditions which resulted in weak demand for imports. Besides these factors, the appreciation of the Kwacha against the other major trading currencies was on account of pressures on these currencies on the international market, partly due to uncertainty in the UK regarding Brexit negotiations.

3.4 With regard to forex reserves, the RBM managed to keep official reserves above 3.0 months of import cover during the period, as depicted in Chart 4 below, largely due to an increase in

forex purchases from the market. Gross official foreign reserves stood at USD790.28m (3.78 months of import cover) as on 31st January 2019, higher than USD755.22m (3.61 months of import cover) on 31st December 2018 and USD629.37m (3.01 months of import cover) on 31st January 2018.



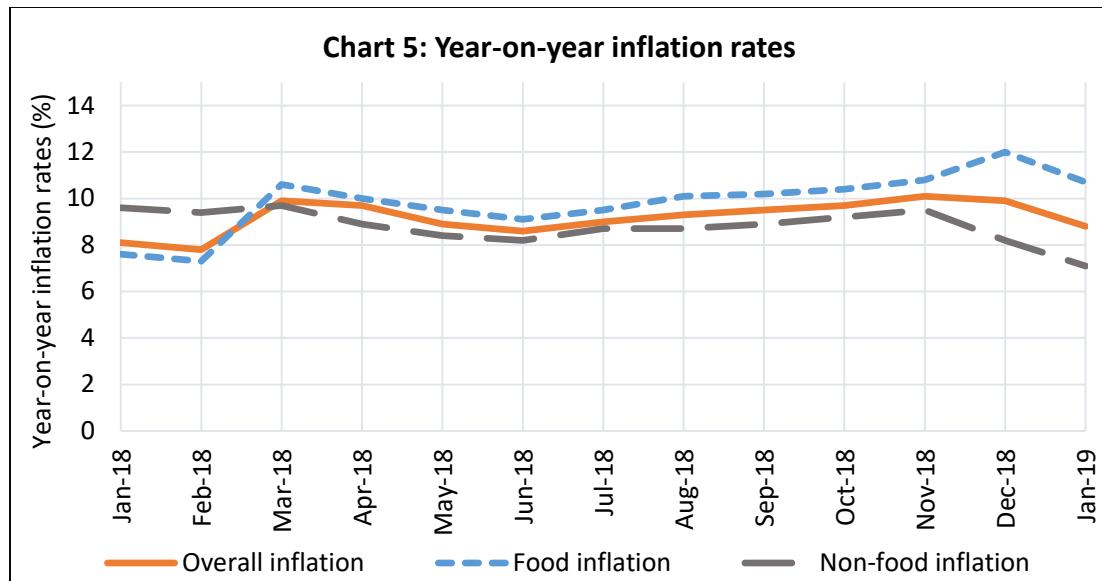
(Source: Reserve Bank of Malawi)

3.5 Looking ahead, the Kwacha is expected to remain broadly stable in the short to medium term, supported by a robust forex reserves position. In the long term, however, depreciation risks could emanate from trade imbalances due the country's weak and less diversified export base and from exogenous shocks such as rising international oil prices.

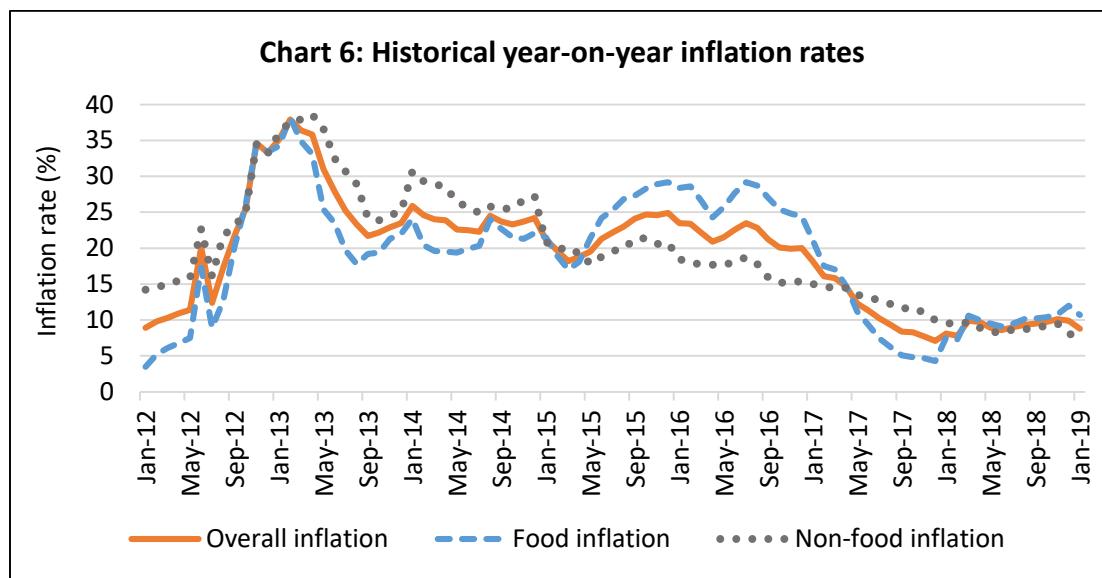
4. Inflation

4.1 Year-on-year headline inflation rate stood at 8.8% in January 2019, declining from 9.9% in December 2019 on account of a decrease in both food and non-food inflation rates. Year-on-year food inflation rate decreased to 10.7% in January 2019 from 12.0% the preceding month and year-on-year non-food inflation rate decreased to 7.1% from 8.2%. During the same period in 2018 (January), year-on-year headline inflation rate and food inflation rate were lower at 8.1% and 7.6%, respectively, while year-on-year non-food inflation rate was higher at 9.6%.

4.2 Chart 5 depict the trend of inflation rate in the past year and Chart 6 depict a longer period trend.



(Source: National Statistical Office)



(Source: National Statistical Office)

4.3 Looking forward, inflation is expected to remain relatively low in 2019, partly supported by continued stability in the exchange rate and expected moderate improvement in agricultural output following a better rainfall pattern in the 2018/2019 season compared to the previous season. However, the recent floods experienced in the southern part of the country are a big threat to the bumper harvest that was earlier projected by the Ministry of Agriculture. Other risks to continued low inflation could emanate from increased Government expenditure especially during the elections period, increased Government borrowing in the second half of the 2018/2019 fiscal year due to an increase in the budget deficit as some development partners delayed disbursement of budget support and rising oil prices on the international market.

4.4 RBM earlier in January 2019 projected an average headline inflation rate of 8.5% in 2019 and targets an average annual rate of 5% by 2021.

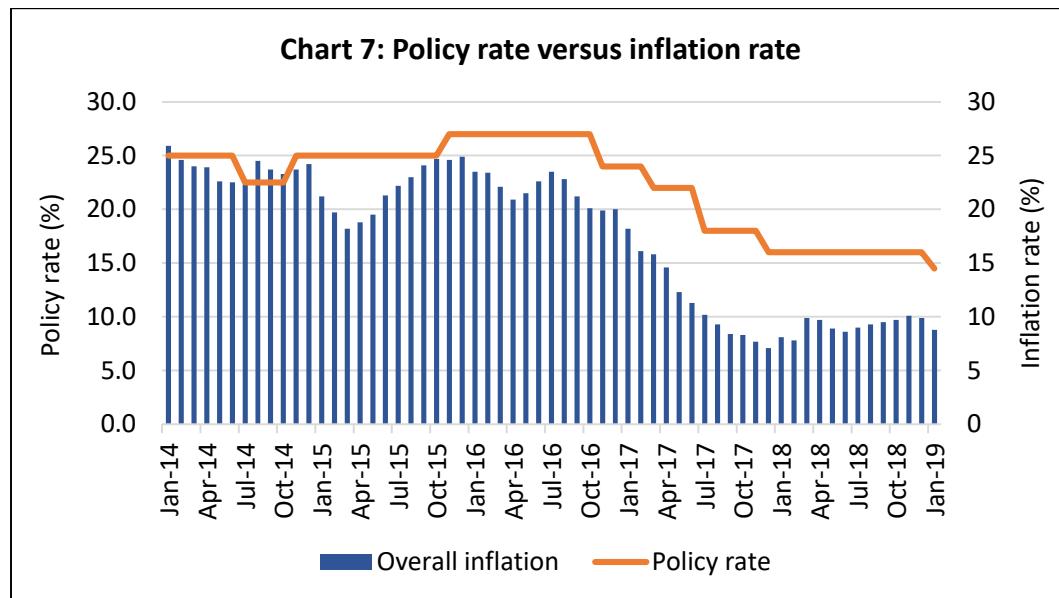
5. Monetary policy

5.1 The Monetary Policy Committee (MPC) held their first meeting of 2019 on 29th and 30th January 2019. After taking into consideration developments in the domestic and global economy and macroeconomic outlook, the MPC observed that risks to inflation experienced in 2018 had started to dissipate with a favourable macroeconomic outlook for 2019. The Committee thus decided to loosen monetary policy as follows:

- 5.1.1 reduce the Policy rate (PR) from 16.0% to 14.5%;
- 5.1.2 reduce the Liquidity Reserve Requirement (LRR) ratio from 7.5% to 5.0% for domestic currency deposits and from 7.5% to 3.75% for foreign currency deposits;
- 5.1.3 reduce the Lombard rate from 18.0% to 14.9%; and
- 5.1.4 peg the Base lending rate for commercial banks at the Lombard rate.

5.2 These policy changes were aimed at assisting the financial sector and the private sector to harness synergies and effectively contribute to economic growth.

5.3 The chart below depicts the historical trend of the Policy rate relative to inflation rate. The chart shows that the Policy rate has been on a declining trend since November 2016.



(Source: RBM, NSO)

5.4 In response to the monetary policy changes, commercial banks reduced their maximum lending rates which now range from 25.80% to 26.9%, compared to the range of 32.00% to 39.00% before the revision. Details are shown in the table below:-

Table 2: Commercial banks' lending rates

Bank	Revised (February 2019)				Previous rates		
	Base rate	Maximum rate	Maximum premium	Effective date	Base rate	Maximum rate	Maximum premium
CDHIB	14.90%	25.80%	10.90%	18-Feb-19	24.50%	27.50%	3.00%
Ecobank	14.90%	26.75%	11.85%	11-Feb-19	25.00%	31.00%	6.00%
FDH	14.90%	26.00%	11.10%	1-Mar-19	25.00%	32.50%	7.50%
First Capital	14.90%	26.00%	11.10%	11-Feb-19	23.00%	33.00%	10.00%
NBM	14.90%	25.90%	11.00%	11-Feb-19	23.00%	33.00%	10.00%
NBS	14.90%	26.90%	12.00%	11-Feb-19	25.50%	34.50%	9.00%
Nedbank	14.90%	26.50%	11.60%	13-Feb-19	25.00%	31.00%	6.00%
NFB	14.90%	26.50%	11.60%	11-Feb-19	29.00%	39.00%	10.00%
Standard	14.90%	25.90%	11.00%	13-Feb-19	23.00%	32.00%	9.00%
Average	14.90%	26.25%	11.35%		24.78%	32.61%	7.83%

5.5 Looking forward, we expect the MPC to take a cautious stance in the short to medium term to allow the market to fully respond to the recent changes. All other interest rates in the market could continue to decline in the near term and then stabilise later in the year. In the long term, we expect further interest rate cuts if shocks to inflation and the exchange rate continue to be contained.

6. Economic growth

6.1 RBM and the World Bank estimate that economic activity moderated to around 4.0% and 3.7%, respectively, in 2018 from around 5.2% in 2017, owing to a decline in agricultural production as erratic rains and a fall army worm infestation negatively impacted crop output. Structural challenges related to the intermittent supply of power and water were also a significant constraint on production in 2018.

6.2 In 2019 economic growth is expected to be slightly better than in 2018 largely on account of a moderate rebound in agriculture following an expected better rainfall pattern and a favourable macroeconomic environment. RBM and the Government project a real GDP growth rate of 4.1% for 2019 driven by good performance in the following economic activities: agriculture; wholesale and retail trade; transportation and storage; information and communication; and professional, scientific and technical services, among others. Agriculture output in 2019 is expected to recover to 2.0% from 0.6% in 2018, the wholesale and retail trade sector is estimated to grow by 4.9%, transport and storage by 5.4% and information and communication by 7.5%.

Table 3: Government estimates and forecasts of growth rates

	2017 ^e	2018 ^f	2019 ^f
Agriculture, forestry and fishing	6.1	0.6	2.0
Mining and Quarrying	1.6	1.9	1.5
Manufacturing	2.0	3.8	3.5
Utilities	2.6	4.4	3.1
Construction	4.4	4.9	3.7
Wholesale and retail	5.0	4.4	4.9
Transport and storage	6.0	5.2	5.4
Accommodation and food service activities	4.2	5.9	4.0
Information and communication	6.5	7.0	7.5
Financial and Insurance activities	5.5	7.1	3.9
Real estate activities	4.4	3.9	2.8
Professional, scientific and technical services,			
Administrative and support service activities	4.0	5.2	5.9
Public administration and defense	5.7	7.2	6.1
Education	6.6	9.4	7.6
Human health and social work activities	5.3	6.0	5.7
Other services	4.3	5.2	5.0
Sum of all industries	5.0	3.8	3.9
<i>Plus taxes less subsidies on products</i>	7.7	7.1	7.7
GDP in 2010 constant prices	5.2	4.0	4.1

(Source: *Business Interviews Summary Report, September 2018 - compiled by National Accounts and Balance of Payments Technical Committee*)

Table 4: World Bank growth rate estimates for Malawi

	2016	2017	2018 ^f
Real GDP	2.5	4.0	3.7
Agriculture	-2.3	5.0	2.5
Industry	2.4	2.2	3.0
Services	4.4	4.0	4.5

(Source: *World Bank's Malawi Systematic Country Diagnostic: Breaking the Cycle of Low Growth and Slow Poverty Reduction - December 2018*)

7. Stock market performance

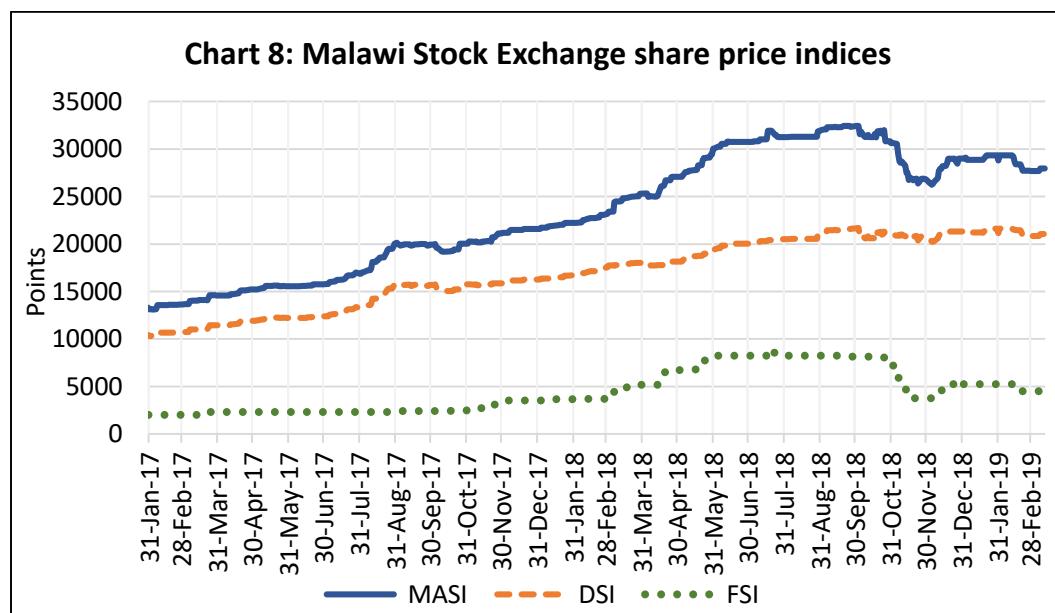
7.1 The Malawi Stock Exchange (MSE) was bearish in January 2019 and February 2019 as it registered a negative return on investment of -0.60% in January 2019 and -3.89% in February 2019. The Malawi All Share Index (MASI) closed the month of January 2019 at 28,808.89 points and the month of February 2019 at 27,687.33 points, down from 28,983.53 as at the end of December 2019.

7.2 The market transacted a total of 165,978,557 shares at a total consideration of K6.98b in February 2019 and a total of 46,773,797 shares at a total consideration of K2.36b in January

2019 compared to a total of 42,869,348 shares at a total consideration of K2.41b in December 2018. This represented a 254.85% increase in February 2019 and a 9.11% increase in January in terms of share volume and a 196.25% in February 2019 and a 2.20% decrease in January 2019 in terms of share value. Of the total shares traded in February 2019, 152,755,283 NBS shares were traded as a negotiated deal.

7.3 Two counters registered capital gains in February 2019, three counters registered no share price movement while the rest registered losses, as shown in Table 4 below.

7.4 ICON Properties, a property development and management firm, was officially listed for the first time on the Malawi Stock Exchange on Monday, 21st January 2018. A total of 6,680,000,000 shares were listed at the unit price of K8.75. During the listing day, ICON share price gained by 37.14% and closed at K12.00.



(Data source: MSE)

Table 5: Share trading summary							
	28-Feb-19	31-Jan-19	31-Dec-18	28-Feb-18	M-O-M Δ	YTD Δ	Y-O-Y Δ
Market indices							
MASI	27,687.33	28,808.89	28,983.53	23,182.59	⬇ -3.89%	⬇ -4.47%	⬆ 19.43%
DSI	20,829.45	21,159.22	21,318.07	17,535.66	⬇ -1.56%	⬇ -2.29%	⬆ 18.78%
FSI	4,521.94	5,265.12	5,265.12	3,706.12	⬇ -14.12%	⬇ -14.12%	⬆ 22.01%
Gainers (M-O-M)							
MPICO	13.04	13.00	13.20	15.70	⬆ 0.31%	⬇ -1.21%	⬇ -16.94%
NBM	315.01	315.00	332.02	270.08	⬆ 0.00%	⬇ -5.12%	⬆ 16.64%
Flat (M-O-M)							
ILLOVO	200.00	200.00	200.00	240.00	➡ 0.00%	➡ 0.00%	⬇ -16.67%
NITL	75.00	75.00	75.00	60.06	➡ 0.00%	➡ 0.00%	⬆ 24.88%
STANDARD	670.00	670.00	670.00	609.99	➡ 0.00%	➡ 0.00%	⬆ 9.84%
Loosers (M-O-M)							
FMBCH	85.00	100.00	100.00	70.70	⬇ -15.00%	⬇ -15.00%	⬆ 20.23%
SUNBIRD	138.00	145.00	145.00	110.00	⬇ -4.83%	⬇ -4.83%	⬆ 25.45%
TNM	25.01	26.00	28.00	19.03	⬇ -3.81%	⬇ -10.68%	⬆ 31.42%
PCL	1,100.00	1,140.00	1,140.00	600.00	⬇ -3.51%	⬇ -3.51%	⬆ 83.33%
ICON	11.94	12.00	8.75		⬇ -0.50%	⬆ 36.46%	
BHL	12.98	13.00	13.00	28.00	⬇ -0.15%	⬇ -0.15%	⬇ -53.64%
NBS	9.99	10.00	10.00	8.70	⬇ -0.10%	⬇ -0.10%	⬆ 14.83%
NICO	41.99	42.00	43.00	45.00	⬇ -0.02%	⬇ -2.35%	⬇ -6.69%
OMU/OML	2,513.23	2,513.25	2,513.25	1,990.00	⬇ 0.00%	⬇ 0.00%	⬆ 26.29%

(Source: MSE)

8. Financial results for 2018

8.1 In January 2019 and February 2019, some listed companies and financial institutions published their financial results for 2018. Some companies also published statements announced expected movements in profits for the year. The reported profits and expected profit movements are summarized in Table 5 and Table 6 below:

Table 5: Published financial results for 2018			
	2018 PAT (K'b)	Movement	2017 PAT (K'b)
Listed company			
ILLOVO	16.45 	113%	7.74
Standard Bank	10.58 	-13%	12.16
Unlisted financial institutions			
FDH Bank	5.97 	694%	(1.00)
First Discount House	1.13 	-17%	1.35

(Sources: MSE and The Nation and Daily Times newspapers)

Table 6: Expected profit movements for 2018			
	Expected 2018 PAT (K'b)	Expected movement	2017 PAT (K'b)
BHL	0.35 	-30%	0.51
MPICO	6.62 	30%	5.09
NBS	0.33 	130%	(1.09)
NITL	1.67 	-25%	2.22
TNM	16.39 	25%	13.11

(Source: MSE)

9. Interest rate capping bill

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9.1 A member of parliament moved a motion in parliament on 8th December 2016 to cap interest rates on loans obtained from banks and other lending institutions with an aim of protecting consumers from exorbitant loan prices. The issue sparked debate in 2018 as members of parliament held consultations with various stakeholders on the issue to inform decisions regarding a bill that was being drafted. The RBM also organized a conference on the same.

9.2 The general consensus from the debate was that lending rates in Malawi are too high compared to other countries in the Sub-Saharan African region but the debaters deferred on whether capping interest rates by law was the way to go to bring down the lending rates.

9.3 The first draft of the bill was presented in Parliament on 13th December 2018. The members of parliament, however, resolved that there was need for further consultations on the bill and so referred the matter to a Joint Parliamentary Committee comprised of the Public Accounts Committee, the Government Assurances Committee and the Women's Caucus.

9.4 The Joint Committee conducted consultations with various domestic stakeholders on the bill, including:-

9.4.1 Ministry of Finance, Economic Planning and Development

- 9.4.2 Reserve Bank of Malawi (RBM)
- 9.4.3 Bankers Association of Malawi (BAM)
- 9.4.4 Malawi Union of Savings and Credit Cooperatives (MUSCCO), and
- 9.4.5 Microfinance Network and Human Rights Defenders Coalition (HRDC).

9.5 The Joint Committee also conducted study tours in Ghana and Zambia where they met the following institutions:

- 9.5.1 The Parliamentary Committee on Finance
- 9.5.2 Officials from Ministry Finance in Ghana and Zambia
- 9.5.3 Officials from the Central Banks
- 9.5.4 Microfinance networks, and
- 9.5.5 Centre for Economic and Business Research in Ghana

9.6 From these consultations, study tours and other research, the Joint Committee gathered that the unintended consequences of interest rate capping outweigh the benefits. Therefore, in their report released recently in March 2019, the Committee recommended that Malawi should not legislate but rather regulate the issues of interest rates in order to protect the borrower.