



Economic update - October 2018 and outlook for the rest of Q4

Investment Banking

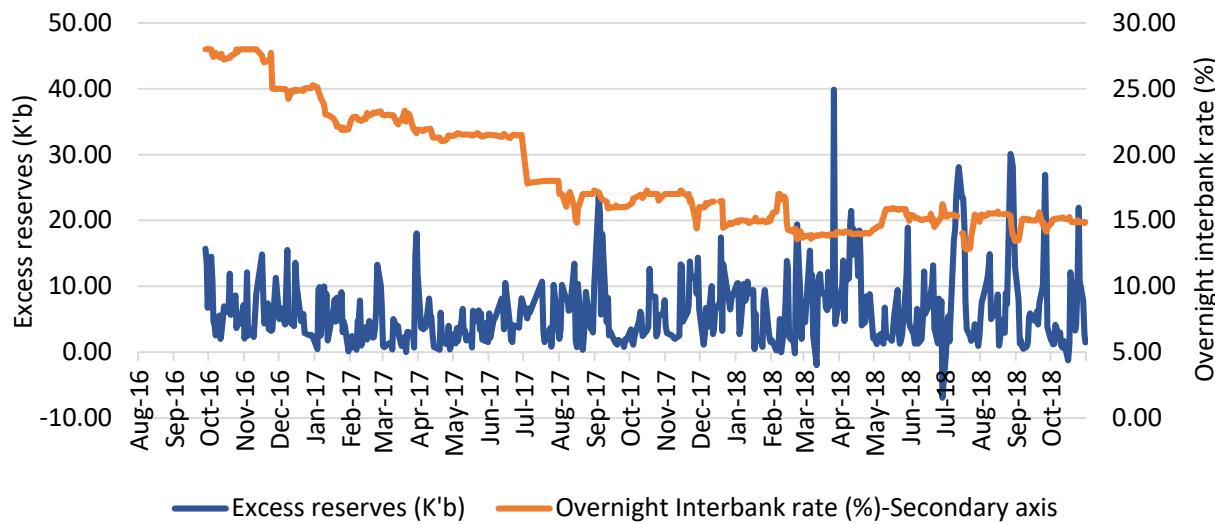
20th November 2018

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1. Interbank market

- 1.1 Liquidity levels tightened during the month of October 2018 following the closure of the tobacco market in the preceding month. Excess liquidity reserves decreased by 29.35% to an average of K4.71b per day from an average of K6.67b per day recorded in September 2018. Similar levels of liquidity were observed in October 2017, averaging about K4.95b per day. However, the levels of liquidity in October 2018 were much lower when compared to the average of K9.32b per day for the third quarter (Q3) of 2018, K7.04b per day for the second quarter (Q2) of 2018 and K9.79b per day for the first quarter (Q1) of 2018. It is expected that liquidity conditions will remain tight for the rest of the fourth quarter (Q4) of 2018 and in the first quarter of 2019 due to increased expenditures directed towards the purchase of farm inputs for the 2018/19 growing season. The Reserve Bank of Malawi (RBM) is also likely to ensure liquidity conditions remain tight (through open market operations) during the lean period so as to keep in check expected inflation pressures.
- 1.2 In line with reduced liquidity levels in the system, the overnight interbank rate increased to a daily average of 15.01% per annum in October 2018 compared to 14.79% in the previous month, 14.84% in Q3 of 2018, 14.89% in Q2 of 2018 and 14.65% in Q1 of 2018. However, when compared to the corresponding month in 2017, the interbank rate was much higher at the average of 16.84%.
- 1.3 Overnight interbank borrowing marginally decreased to an average of K8.24b per day in October 2018, from K8.71b the previous month compared to a daily average of K7.95b per day for October 2017 and K8.15b, K8.14b and K8.40b during Q3, Q2 and Q1 of 2018, respectively.
- 1.4 Access from the Lombard facility averaged K7.01b per day during the month, decreasing from the average of K10.21b per day the previous month, K8.68b in Q3 2018 and K7.43b in Q2 2018, and increasing from the average of K5.90b per day in Q1 2018. In October 2017, access from the Lombard facility was significantly higher at the average of K20.56b per day. The Lombard rate was stable at 18.00%.
- 1.5 There were no open market operations (OMOs) conducted by RBM throughout the month of October 2018, as was the case in the previous month. In Q3 2018, RBM through OMOs mopped up a total of K23.88b at an average daily rate of 15.00% and in Q2 2018, it mopped up a total of K63.01b at an average rate of 15.01%, and in Q1 2018 mopped up a total of K250.17b. In October 2017, through OMOs the RBM mopped up a total of K15.56b
- 1.6 Chart 1 provides a summary of excess liquidity reserves and overnight interbank rate movements over the last two years. The chart shows that the interbank rate has remained within the RBM target band of +2/-4 percentage points of the Policy rate which has been stable at 16% in 2018.

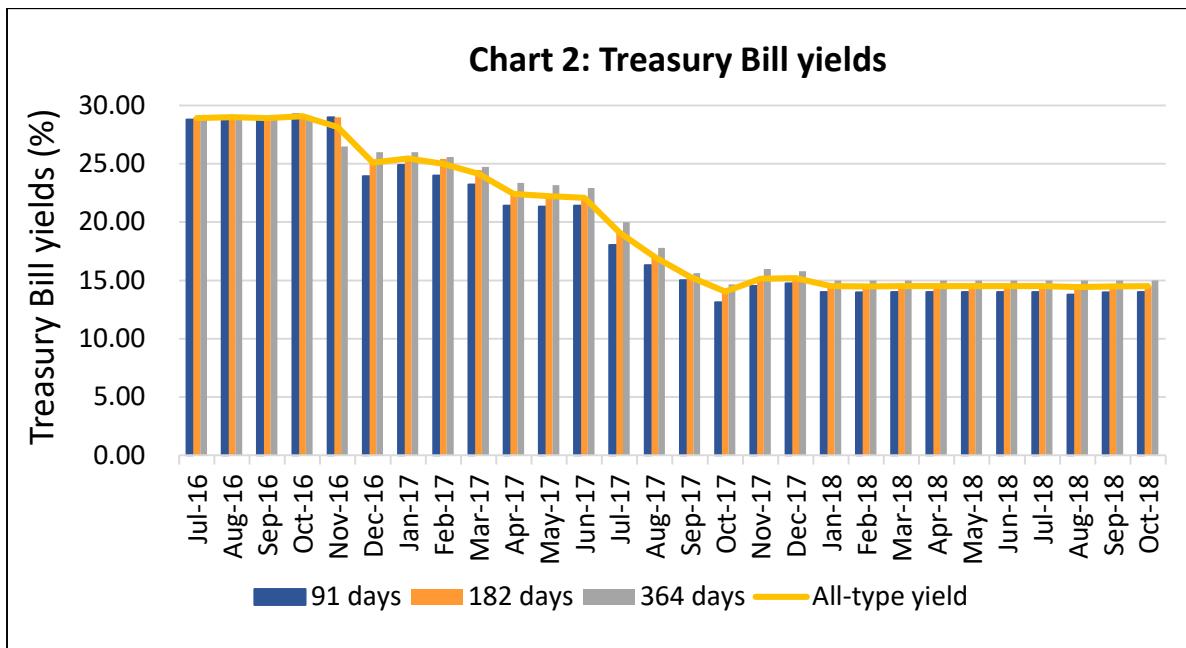
Chart 1: Banks' excess liquidity reserves and overnight interbank rate


(Source: Reserve Bank of Malawi)

2. Government securities ..

- 2.1 The Government raised a total of K23.85b through Treasury Bill auctions in October 2018, compared to K32.12b in the previous month with rejection rates of 19.72% and 33.51%, respectively. Compared to the previous quarters, the Government raised a total of K163b in Q3 of 2018, K138.72b in Q2 of 2018 and K128.27b in Q1 of 2018 with rejection rates of 16.88%, 4.27% and 1.31%, respectively.
- 2.2 Treasury Bill yields remained stable throughout the month, with the 91-day yield averaging 14.00%, slightly increasing from the average of 13.97% in September 2018, 13.92% in Q3 2018, 14.00% in Q2 2018 and 13.99% in Q1 2018. The 182-day and 364-day yields were steady at 14.50% and 15.00%, as has been the case throughout 2018. The all-type yield averaged 14.50% in October 2018, slightly increasing from 14.49% the previous month. The all-type yield averaged 14.47% in Q3 2018 and 14.50% in Q2 and Q1 2018.
- 2.3 Chart 2 shows that Treasury Bill rates declined between July 2016 and September 2017 before stabilizing throughout 2018.
- 2.4 Auctions for a 3 year Treasury Note continued during the month in which a total of K11.98b was raised at a yield of 20.00%. As at the end of October 2018, a total of K89.07b had been raised through Treasury Note auctions in 2018 at an average yield of 18.08% for a 2 year Note and 19.53% for a 3 year Note.

2.5 Maturities of Treasury Bills, Treasury Notes, Promissory Notes and OMO Repos for the month amounted K72.00b, resulting in a net injection of K36.17b.



(Source: Reserve Bank of Malawi)

2.6 Looking forward, following the decision made during the third meeting of the Monetary Policy Committee (MPC) on 25th and 26th September 2018 to maintain the Policy rate at 16%, Treasury Bill yields could be expected to remain stable in the near term. However, persistent inflation risks threaten continued stability of interest rates in general. Additionally, the ongoing debate about the persistence of high interest rates and interest rate capping could put a downward pressure on interest rates, including TB yields.

3. Interest rate capping

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3.1 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 recently sparked debate within the economy as members of parliament held consultations with various stakeholders on the issue to inform decisions regarding a Bill that is currently being drafted. The RBM also organized a conference on the same.

3.2 From the ongoing debate it seems that the general consensus about the issue is that lending rates are too high in Malawi compared to other countries in the Sub-Saharan African region. As such, whether through capping or other means, authorities will most likely ensure that the

lending rates keep declining. The RBM has explicitly indicated that they are aiming for a Policy rate of 11% by 2021 as inflation rate falls to 5%.

4. Foreign exchange market

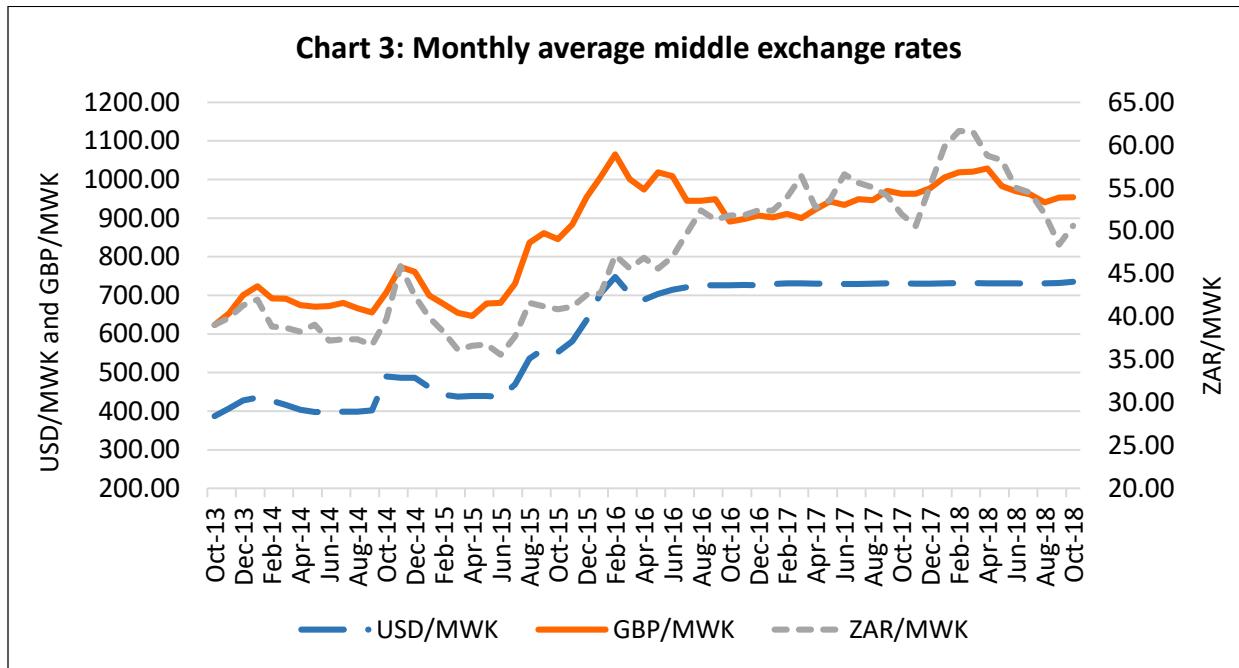
- 4.1 The Kwacha depreciated against most major trading currencies in October 2018. The USD/MWK middle exchange rate during the month averaged 735.17, increasing by 0.42% from the average of 732.13 in September 2018, and by 0.57% when compared to the average of 731.03 in October 2017.
- 4.2 Against the GBP, the Kwacha depreciated albeit marginally by 0.03% during the month to the average middle rate of 953.70 from 953.41 in September 2018. However, when compared to the average middle rate of 962.77 recorded in October 2017, the Kwacha registered an appreciation of 0.94% against the GBP.
- 4.3 Relative to ZAR, the Kwacha depreciated by 4.50% in October 2018 to the average middle rate of 50.61 from 48.43 in the previous month, but appreciated by 2.59% when compared to the average middle rate of 51.95 in October 2017.

Table 1: Monthly average exchange rates						
Currency	Oct-18	Sep-18	Oct-17	M-O-M Change	Y-O-Y Change	
USD	735.17	732.13	731.03	▼ 0.42%	▼ 0.57%	
GBP	953.70	953.41	962.77	▼ 0.03%	▲ -0.94%	
ZAR	50.61	48.43	51.95	▼ 4.50%	▲ -2.59%	

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

Month	USD/MWK	% Change from the previous month	GBP/MWK	% Change from the previous month	ZAR/MWK	% Change from the previous month
Oct-17	731.03	0.12%	962.77	1.73%	51.95	-5.66%
Nov-17	730.49	-0.07%	962.82	0.00%	50.57	-2.66%
Dec-17	730.24	-0.03%	977.63	1.54%	55.27	9.29%
Jan-18	730.67	0.06%	1005.23	2.82%	59.81	8.22%
Feb-18	731.49	0.11%	1019.05	1.37%	61.64	3.06%
Mar-18	731.64	0.02%	1019.95	0.09%	61.58	-0.10%
Apr-18	731.05	-0.08%	1028.34	0.82%	58.77	-4.56%
May-18	730.67	-0.05%	982.86	-4.42%	58.26	-0.87%
Jun-18	730.91	0.03%	969.45	-1.36%	55.03	-5.54%
Jul-18	730.34	-0.08%	961.41	-0.83%	54.44	-1.08%
Aug-18	730.91	0.08%	940.68	-2.16%	52.00	-4.48%
Sep-18	732.13	0.17%	953.41	1.35%	48.43	-6.87%
Oct-18	735.17	0.42%	953.70	0.03%	50.61	4.50%

(Source: Reserve Bank of Malawi)



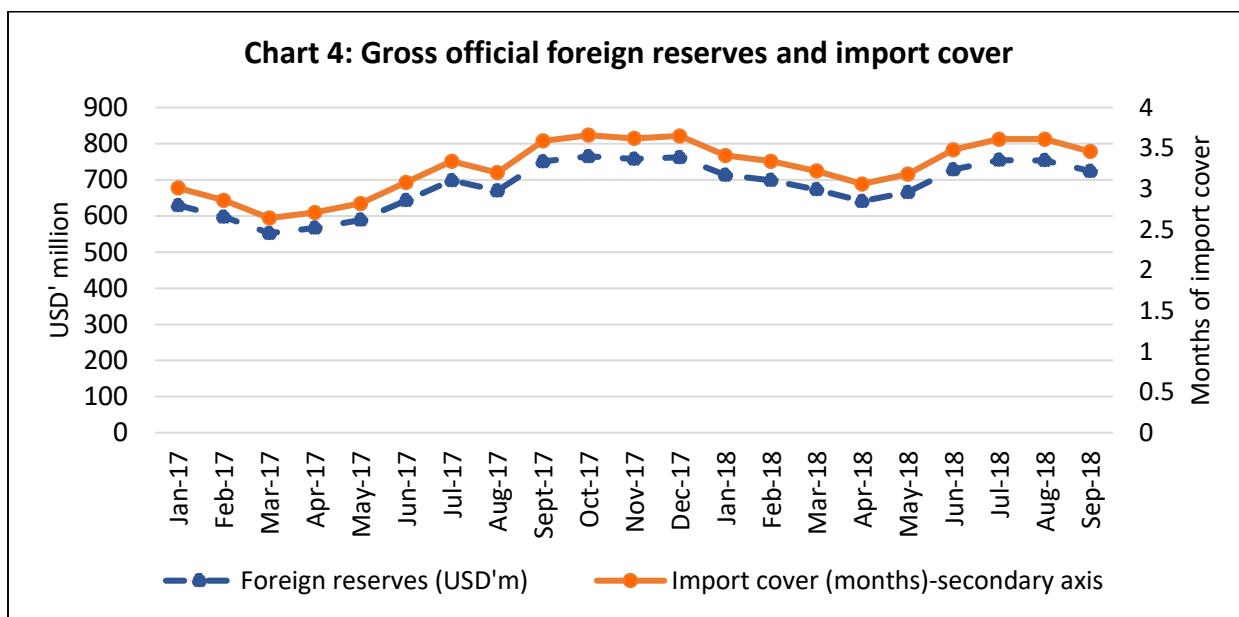
(Source: Reserve Bank of Malawi)

4.4 The depreciation of the Kwacha against the major trading currencies in October 2018, relative to the previous month, was on account of a decline in the supply of forex in the market following the closure of the tobacco market in the previous month.

4.5 After running for 26 weeks, the tobacco auction market closed in September 2018, by which a total of USD337.50m had been realized, compared to USD212.51m realized during the 2017 season, representing a 58.82% increase. The increase in proceeds from tobacco sales in 2018 relative to the previous year is on account of an increase in volumes sold. In the 2018 season, the total volume of tobacco sold amounted 202.00 million kilograms, 89.60% higher than 106.54 million kilograms sold during the 2017 season. The increase in volumes is on account of higher production for 2018 and also an influx of leaf imports from Zambia and Mozambique sold in Malawi.

4.6 Looking ahead, the Kwacha might continue to marginally depreciate during the rest of Q4 of 2018, the lean period, as demand for forex increases due to increased farm input imports and a possible rise in oil prices on the international market. The RBM is expected to intervene more in the forex market during the period in an effort to prevent excessive volatility of the exchange rate.

4.7 However, the position of forex reserves is currently uncertain. The RBM stopped publishing daily positions of forex reserves since 28th September 2018, on which gross official forex reserves were observed at USD727.63m (3.48 months of import cover), 3% lower than USD753.52m (3.61 months of import cover) observed on 31st August 2018. In 2017, gross official forex reserves stood at USD764.42m (3.66 months of import cover) as at the end of October 2018 and at USD750.23 (3.59 months of import cover) as at the end of September 2017.

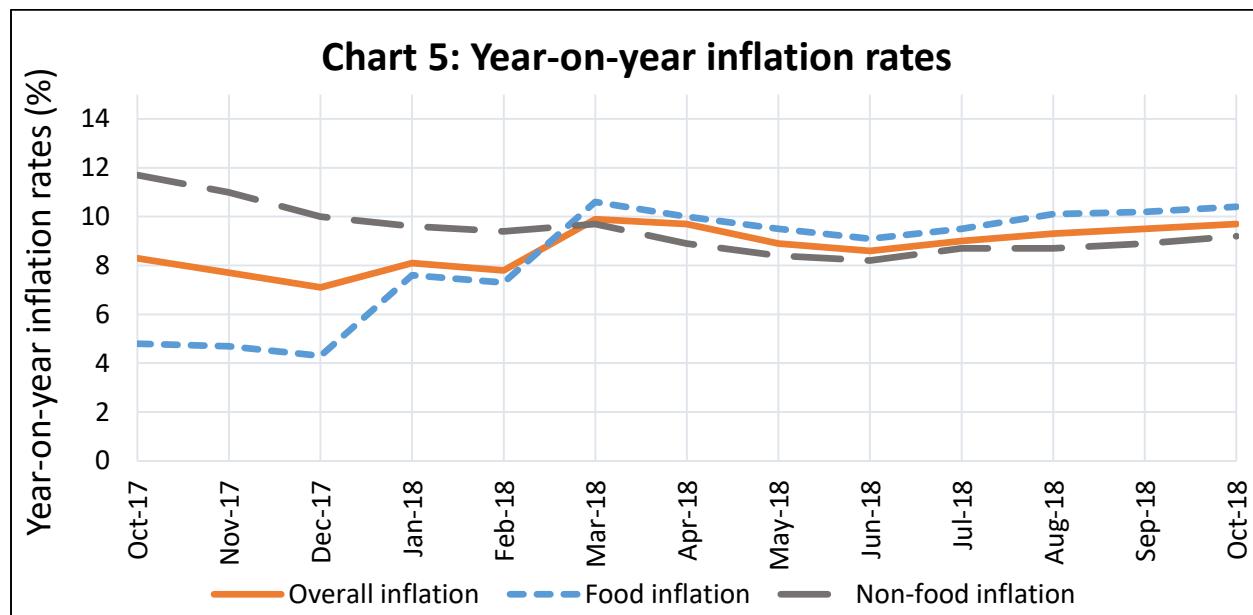


(Source: Reserve Bank of Malawi)

4.8 In the medium to long term, depreciation risks to the Kwacha still remain current account imbalances emanating from the country's weak and undiversified export base and external shocks such as rising oil prices.

5. Inflation

5.1 Annual headline inflation stood at 9.7% in October 2018, up from 9.5% in September 2018 and 8.3%¹ in October 2017. The increase in inflation during the month was on account of an increase in both food and non-food prices. Annual food and non-food inflation increased to 10.4% and 9.2%, from 10.2% and 8.9% respectively, in September 2018. Annual food and non-food inflation for the same period last year (October 2017) stood at 4.8% and 11.7% respectively.



(Source: National Statistical Office)

5.2 Looking ahead, inflation risks are expected to persist in the ensuing months. Food inflationary pressures are expected to remain elevated for the rest of the last quarter of 2018 into the first quarter of 2019 due to a reduced supply of food following a reduced food harvest in the 2017/2018 season. However, the effect on inflation could be lessened by Government's intervention in the food market by offloading maize stocks held by ADMARC. The prices could be dampened further by food relief programmes which are currently underway.

5.3 Non-food inflationary pressures are also expected to remain elevated following the recent upward adjustments in utility tariffs and pump fuel prices and increased government

¹ The Consumer Price Index was rebased in December 2017. Hence the inflation rates for 2018 are not strictly directly comparable to the rates for the previous years.

expenditure especially as we draw towards general elections, among other factors. Recently the Malawi Energy Regulatory Authority (MERA) approved a 31.8% electricity tariff hike over a period of four years, with 20% effective on 1st October 2018. Pump fuel prices were also further adjusted upwards by 5% effective 6th October 2018 due to rising oil prices on the international market.

5.4 RBM expects a short-lived up-tick in inflation between the third quarter of 2018 and the third quarter of 2019. They recently adjusted upwards their outlook for average inflation for 2018 to 9.3% from the earlier projection of 9.0% and are expecting an average inflation rate of 9.6% in 2019. In the medium term (three to five years) RBM maintains the inflation rate target of 5%. NKC African Economics expects Malawi annual average inflation to remain in the single digit in the next five years as shown in the following table:

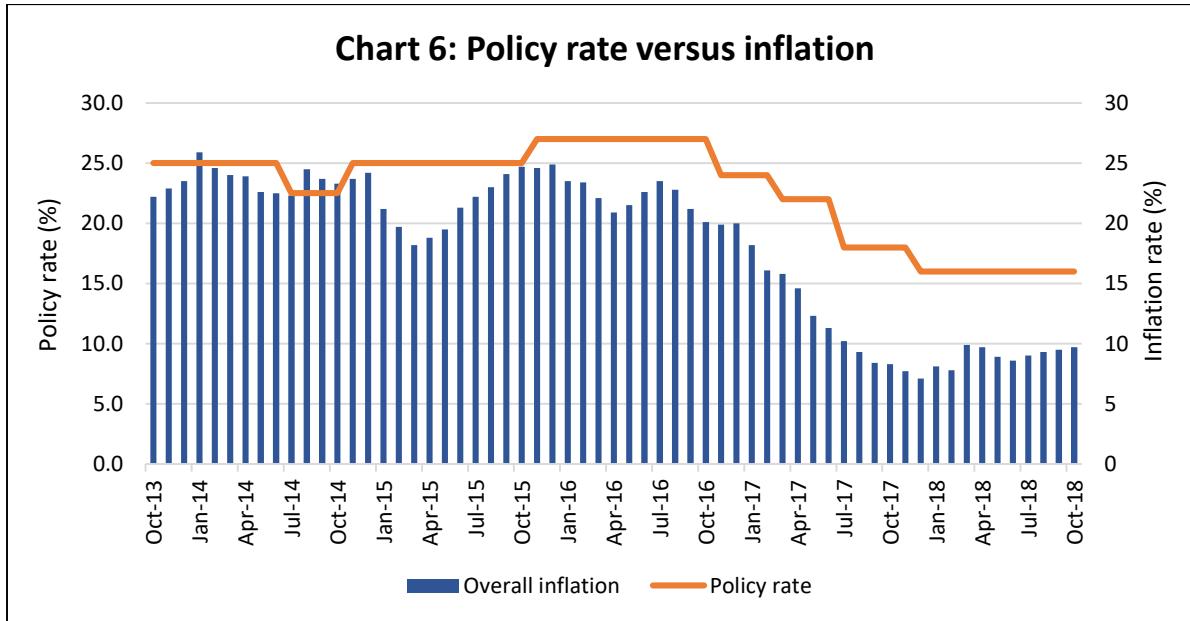
Table 3: Average annual inflation and forecast							
	2016	2017	2018f	2019f	2020f	2021f	2022f
National Statistical Office (NSO)	21.7%	11.5%					
Reserve Bank of Malawi (RBM)			9.3%	9.6%			
Government of Malawi	21.8%	11.5%	7.9%	8.2%	7.7%	7.5%	7.7%
World Bank	21.7%	11.5%	10.9%				
International Monetary Fund (IMF)			10.4%				
Economic Intelligence Unit		12.2%	11.4%	12.9%	9.2%	10.0%	11.2%
NKC African Economics	21.71%	12.18%	8.88%	8.39%	8.20%	8.07%	
Average	21.7%	11.8%	9.8%	9.8%	8.4%	8.5%	9.5%

6. Monetary policy

6.1 The MPC met on 25th and 26th September 2018 to review local and global economic developments that inform monetary policy decisions. During the meeting the MPC decided to maintain the Policy rate at 16.00%, the Liquidity Reserve Requirement (LRR) at 7.50% and the Lombard rate at 200 basis points above the Policy rate. In coming up with this decision, the MPC observed that inflation in first three quarters of 2018 remained elevated on account of rising food and utility prices; and that risks to the inflation outlook still persist on account of further increases in administered prices, higher food and global oil prices, and increased public sector financing requirements. The decision to maintain the monetary policy stance was, therefore, made to ensure that the policy stance remains adequately tight to manage these inflation risk and ensure that inflation declines gradually towards the medium-term objective of 5.0%. It was indicated that the RBM would complement this policy stance with consistent mop-up operations to maintain liquidity conditions at required levels.

6.2 The final MPC meeting for 2018 is scheduled for 12th and 13th December 2018. Under normal circumstances, with inflation at 9.7% in October 2018 and expected persistence of inflationary

pressures in the ensuing months, the MPC would more likely maintain the current monetary policy stance at the forthcoming meeting. Besides, the RBM has a number of times indicated that the current spread of 6 percentage points between the inflation rate and the Policy rate is ideal for the country at the moment. However, the growing concern about the persistence of high interest rates in the country could coerce the RBM to reduce the Policy rate.



(Source: RBM, NSO)

7. Economic growth

7.1 RBM and the World Bank estimate that the Malawi economy grew by 5.1% and 4.0%, respectively, in 2017 on the back of a bumper harvest, recovering from an estimated subdued growth of 2.5% in 2016. In 2018, RBM and the World Bank project that economic activity will moderate to around 4.0% and 3.7%, respectively, due to a decline in agricultural production. Erratic rains and a fall army worm infestation are expected to have had a negative impact on 2018 agricultural output.

Table 4: Government estimates and forecasts of growth rates

	2015 ^e	2016 ^e	2017 ^e	2018 ^f	2019 ^f
Agriculture, forestry and fishing	-1.0	-0.10	6.3	0.1	5.8
Mining and Quarrying	1.1	0.4	1.6	2.3	2.7
Manufacturing	3.8	1.3	1.8	3.6	5.1
Utilities	2.4	0.1	2.7	5.2	5.5
Construction	3.5	3.4	4.8	5.3	5.8
Wholesale and retail	4.9	2.3	5.3	5.5	6.0
Transport and storage	4.3	4.9	6.0	5.5	5.8
Accommodation and food service activities	5.1	5.7	4.2	4.6	4.9
Information and communication	8.6	5.0	6.4	5.5	6.1
Financial and Insurance activities	5.6	5.9	6.7	6.1	4.8
Real estate activities	1.9	3.1	3.9	3.7	2.7
Public administration and defense	6.3	6.2	6.7	6.1	7.2
GDP in 2010 constant prices	3.3	2.7	5.1	4.0	6.0

(Source: Reserve Bank of Malawi)

7.2 Growth for 2018, according to the Government, will be driven by good performance in the following economic activities: human health and social work, financial services and insurance services, wholesale and retail trade, public administration and defense, information and communication, and transportation storage. However, the World Bank expects the performance of industry and services sectors to remain weak in 2018, with structural challenges related to the intermittent supply of power and water remaining a significant constraint on production.

Table 5: World Bank projected growth rates 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 Economic Monitor - May 2018)

8. Stock market performance

8.1 The Malawi Stock Exchange was generally bearish in October 2018. The MASI lost by 5.41% to close at 30,622.66 points on 31st October 2018 from 32,373.19 points on 28th September 2018, due to share price losses in TNM (-15.48%), ILLOVO (-14.65%), FMBCH (-12.03%), NICO (-1.94%) and NITL (-0.01%) which outweighed share price gains in PCL (23.53%), NBS (11.84%), BHL (11.23%) and NBM (6.75%). However, the market registered an increase in traded value of 55.54% and volume of 71.56% during the month.

8.2 The year-to-date (YTD) return on the MASI as at the end of the month stood at 41.78%, lower than the YTD return of 50.51% registered for the corresponding period in 2018.

8.3 There was no turnover on the listed bond market during the month.

Table 6: Share trading summary							
	31-Oct-18	28-Sep-18	2-Jan-18	31-Oct-17	M-O-M Δ	YTD Δ	Y-O-Y Δ
Market indices							
MASI	30,622.36	32,373.19	21,598.07	20,049.06	⬇ -5.41%	⬆ 41.78%	⬆ 52.74%
DSI	20,938.60	21,621.84	16,272.64	15,760.94	⬇ -3.16%	⬆ 28.67%	⬆ 32.85%
FSI	7,196.88	8,138.23	3,519.43	2,474.85	⬇ -11.57%	⬆ 104.49%	⬆ 190.80%
Gainers (M-O-M)							
BHL	12.58	11.31	28.00	28.00	⬆ 11.23%		
NBM	332.00	311.01	270.08	270.00	⬆ 6.75%	⬆ 22.93%	⬆ 22.96%
NBS	10.01	8.95	8.50	7.50	⬆ 11.84%	⬆ 17.76%	⬆ 33.47%
PCL	1,050.00	850.00	600.00	570.00	⬆ 23.53%	⬆ 75.00%	⬆ 84.21%
Flat (M-O-M)							
MPICO	19.50	19.50	15.61	15.61	➡ 0.00%	⬆ 24.92%	⬆ 24.92%
OMU	2,513.25	2,513.25	1,960.00	1,930.00	➡ 0.00%	⬆ 28.23%	⬆ 30.22%
STANDARD	670.00	670.00	610.00	600.00	➡ 0.00%	⬆ 9.84%	⬆ 11.67%
SUNBIRD	145.00	145.00	96.00	70.00	➡ 0.00%	⬆ 51.04%	⬆ 107.14%
Loosers (M-O-M)							
FMBCH	138.99	157.99	67.00	46.00	⬇ -12.03%	⬆ 107.45%	⬆ 202.15%
ILLOVO	204.84	240.00	240.00	240.00	⬇ -14.65%	⬇ -14.65%	⬇ -14.65%
NICO	50.99	52.00	34.00	34.00	⬇ -1.94%	⬆ 49.97%	⬆ 49.97%
NITL	85.99	86.00	60.06	60.08	⬇ -0.01%	⬆ 43.17%	⬆ 43.13%
TNM	24.51	29.00	14.50	14.00	⬇ -15.48%	⬆ 69.03%	⬆ 75.07%

(Source: Malawi Stock Exchange)

9. Financial results for the half year ended 30th June 2018

Table 7: Published financial results for the half year ended 30th June 2018

	H1 2018 PAT (K'm)	Movement	H1 2017 PAT (K'm)
Listed companies			
FMB Bank (Malawi only)	6,580 	31%	5,035
FMB Capital Holdings PLC (USD'm)	20		
MPICO PLC	3,799 	38%	2,760
National Bank fo Malawi PLC	8,541 	-10%	9,527
NBS Bank	479 	142%	(1,136)
NICO Holdings PLC	5,973 	39%	4,303
National Investment Trust PLC	1,429 	42%	1,009
Press Corporation PLC	23,079 	227%	7,061
Standard Bank	5,532 	-32%	8,163
Sunbird	1,173 	9%	1,072
TNM	6,942 	46%	4,750
Unlisted banks			
CDH Investment Bank	672 	34%	503
Ecobank	2,120 	-1%	2,134
FDH Bank	1,342 	-26%	1,820
Nedbank	(1,053) 	-15%	(912)
New Finance Bank	820 	180%	(1,022)
Discount house			
First Discount House	157 	-75%	634

(Sources: Various)

10. Conclusion

10.1 Following the closure of the tobacco market, liquidity levels tightened during the month of October 2018 which resulted in the overnight interbank rate increasing to a daily average of 15.01% per annum from 14.79% the preceding month. It is expected that liquidity conditions will remain tight for the rest of Q4 of 2018 and in Q1 of 2019 due to increased expenditures directed towards the purchase of farm inputs for the 2018/19 growing season; and that the interbank rate will remain within the RBM target band of +2/-4 percentage points of the Policy rate currently at 16%.

10.2 Interest rate stability which has been exhibited throughout 2018 continued during the month of October 2018, with the Policy rate, the average Treasury Bill yield and the 3 year Treasury Note remaining stable at 16.00%, 14.50% and 20.00%, respectively. Looking ahead, under normal circumstances, interest rates would be expected to remain stable in the near term as

Monetary Policy remains cautious amid upward pressures on inflation. However, the growing debate about the persistence of high interest rates and interest rate capping could put a downward pressure on the general level of interest rates.

- 10.3 The Kwacha depreciated against most major trading currencies in October 2018 on account of a decline in the supply of forex in the market following the closure of the tobacco market in the previous month. The Kwacha might continue to marginally depreciate during the rest of Q4 of 2018 into Q1 of 2019, the lean period, as demand for forex increases due to increased farm input imports and a possible rise in oil prices on the international market
- 10.4 Rising food and non-food prices led to an increase in inflation during the month of October 2018 to 9.7% from 9.5% recorded in September 2018. Upward inflation risks are expected to persist into Q1 of 2019 as both food and non-food prices remain elevated, mainly due to a reduced food supply, recent upward adjustments in energy prices and increased government expenditure as we draw towards general elections in May 2019.
- 10.5 It is projected that economic growth will decline from around 5.1% (according to RBM) in 2017 to the range of 3.7% and 4.0% in 2018 due to a decline in agricultural production, before rising again to 6.0% in 2019.
- 10.6 The Malawi Stock Exchange was generally bearish in October 2018. The MASI decreased by 5.41% to close at 30,622.66 points on 31st October 2018, due to share price losses in TNM, ILLOVO, FMBCH, NICO and NITL which outweighed share price gains in PCL, NBS, BHL and NBM.