Malawi

key figures

• Land area, thousands of km^2	118
• Population, thousands (2005)	12 884
• GDP per capita, $ PPP valuation (2005)	580
• Life expectancy (2000-2005)	39.6
• Illiteracy rate (2005)	35.7

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Malawi

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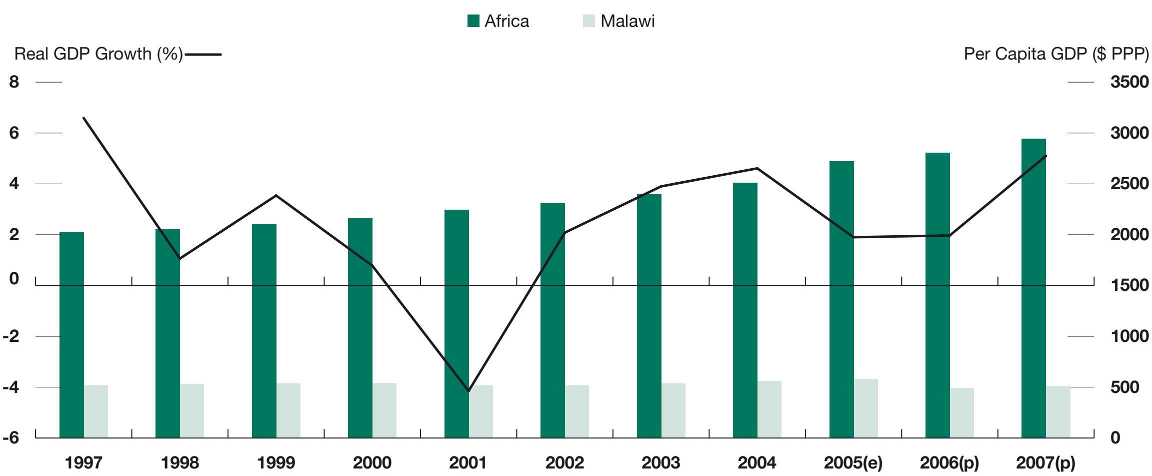
MALAWI IS ONE OF THE POOREST countries in the world. It was ranked 165th out of 177 countries according to the 2005 United Nations Human Development Index and had the second lowest GDP per capita in 2003. By all measures, the Malawian economy went through very difficult times in 2005. It faced serious food shortages with an estimated 4.85 million people, i.e. nearly 50 per cent of the population in need of emergency food support. Moreover, 2005 has been a year of political turmoil, with the president facing possible impeachment and resigning from his party to form a new one, an initiative which has very little support in parliament.

The government faces three major challenges in the coming years. First, it must find a permanent solution to the recurrent food shortage. The yearly food shortage in Malawi constrains development and has strong negative effects on the welfare of nearly half the population. Second, the government must tackle its recurrent budget deficit and refrain from systematically exceeding the agreed budget. Third, the high prevalence of HIV/AIDS has reduced life expectancy in Malawi to below 40 years in 2003 and increased the under-5 mortality rate to 230 per 1 000, one of the highest in the world. Such a high death rate has already started to exert a heavy toll on Malawi's human capital and slow down its economic development.

Food crisis and high HIV/AIDS rates are compromising stability and growth.

Figure 1 - **Real GDP Growth and Per Capita GDP**
($ PPP at current prices)



Source: Central Statistical Office data; estimates (e) and projections (p) based on authors' calculations.

Recent Economic Developments

Real gross domestic product (GDP) is expected to grow by 1.9 per cent in 2005 compared to 4.6 per cent in 2004. This lower growth is due to contraction in the agricultural sector, caused in part by the dry spell experienced during January-March 2005. Indeed, agriculture, which constitutes about one-third of GDP, contracted by 9.1 per cent in 2005 compared to a growth of 2.7 per cent in 2004. Most of the major crops (maize, tobacco, groundnuts, rice and beans) were severely affected by the dry spell and all yielded lower harvests than in 2004. For instance, the 2005 maize harvest, of great importance for Malawi's food security, is estimated to have been 24 per cent lower than in 2004. It is expected that the growth rate will remain below 2 per cent in 2006 but that it will pick up in 2007.

Tobacco production fell to 146 000 tonnes in 2005 from 180 000 tonnes in 2004. The fall in production can mainly be attributed to there now being fewer incentives for farmers to produce tobacco. Indeed, tobacco prices were low in 2004 and prompted farmers to shift away from tobacco production in 2005. Tobacco prices remained disappointingly low during 2005 when prices averaged $1.11 per kg compared to $1.14 per kg in 2004. Of great concern were burley tobacco prices, as burley makes up the bulk of tobacco grown in Malawi. For the 2005 season, burley prices averaged $0.99 per kg, which is 9.2 per cent lower than the price in 2004. Given the low prices that prevailed in 2005, the incentives to produce tobacco will be even lower in 2006 and an even lower output should be expected. This is alarming for Malawi as tobacco production generated $202 million in export revenue in 2004, and is expected to have generated $226 million in 2005.

There have also been some recent changes in the tobacco market in Malawi. Two of the three top tobacco buyers, Dimon and Standard Commercial, merged in November 2004 to form Dimon-Stancom. The other company, Limbe Leaf, is a subsidiary of the US parent company Universal Leaf. These two companies are supplemented by smaller niche market companies such as Africa Leaf and Premier Leaf, which have negligible market shares. The near duopoly situation gave rise to some concern about collusion but no evidence has been found to that effect.

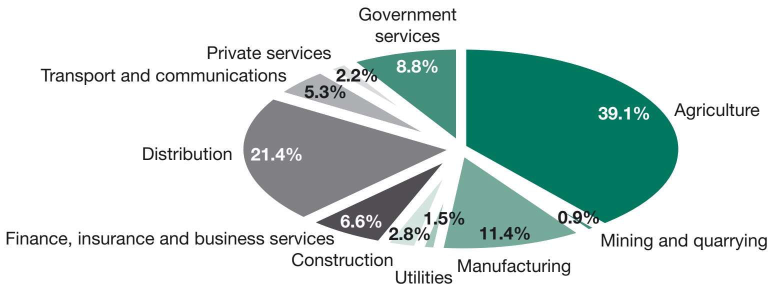
Total tea production in 2005 is estimated to have reached 40 000 tonnes, which is lower than the 2004 harvest. Lower tea production arose because of the dry weather conditions in 2005. Moreover, tea prices have been depressed over the years due to over-supply on the world market. Lower tea production and low prices resulted in a considerable decline in earnings to $0.9 million during the third quarter of 2005 compared to $3.2 million in a similar quarter of 2004.

Manufacturing and mining account for 17 per cent of GDP, and services for 27 per cent of GDP. Despite the continued poor overall economic performance, output in the manufacturing sector grew by 11.9 per cent in 2005 compared to 6.9 per cent in 2004. Value added in the construction sector grew by an impressive 14.7 per cent in 2005 compared to 10.4 per cent in 2004. The growth in 2005 mainly reflected an increase in medium- and small-scale construction activities. Output in the transport sector grew by 8.8 per cent in 2005, an increase from 6.7 per cent in 2004. The increase in 2005 was mainly the result of the transport of donor relief items, especially maize, as well as improved performance in the communication sub-sector.

Inflation in 2005 is expected to reach 16.4 per cent. The main source of inflationary pressure is the higher price for maize, which has a weight of 58 per cent in the consumer price index. This was due to a shortage of domestically produced food and an increase in maize prices on international markets. As can be seen below, monetary policy also added to inflationary pressure. However, at the end of 2005 there were signs that the inflation rate had slowed down marginally during the third quarter of 2005 to an average of 13.5 per cent from 15.5 per cent as recorded in the preceding quarter. The slowdown can be attributed to some deceleration in the price increase of food. Non-food inflation, however, exhibited some acceleration but this only partially offset the decline in food price inflation. Unless there is severe drought, it is expected that the inflation rate for 2006 and 2007 will be almost 10 per cent.

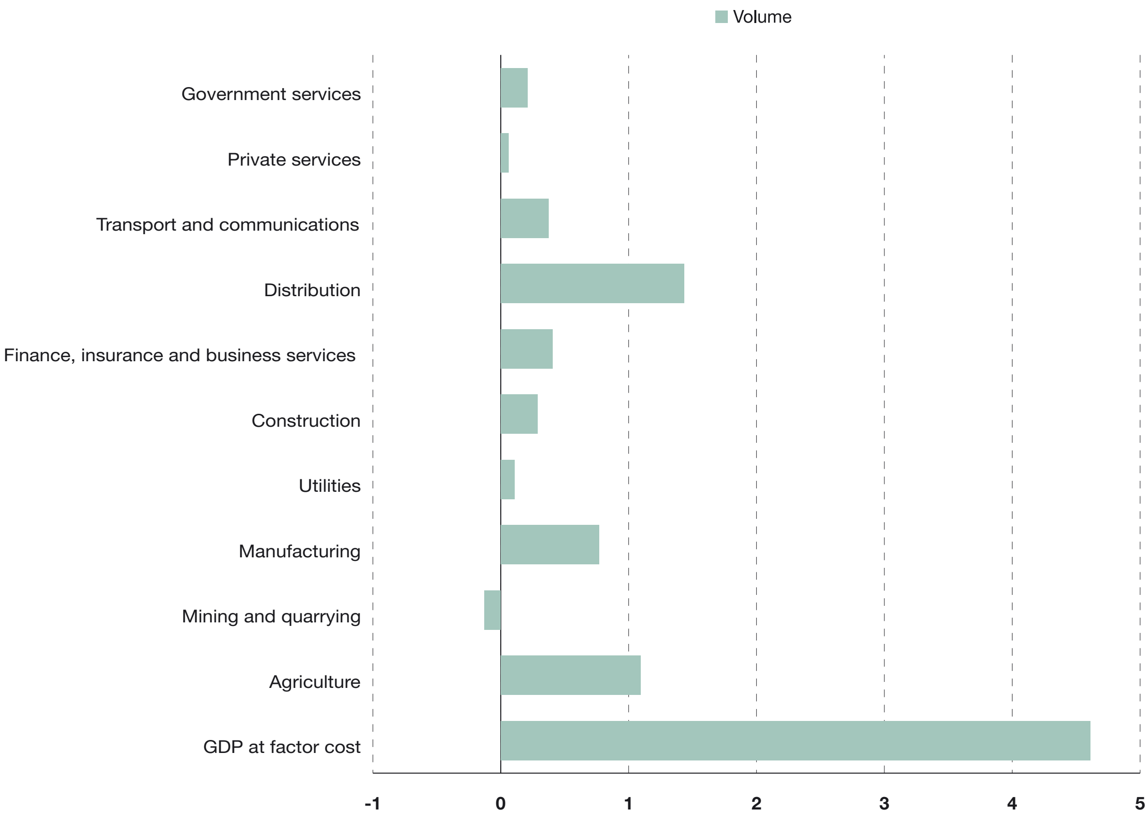
Output shortfalls in the agricultural sector and acceleration in inflation depressed household incomes, with the result that growth in both private consumption and private investment slowed down in 2005. The degree of stimulus provided by the fiscal deficit also fell, and the balance on traded goods and non-factor services deteriorated, exerting further downward pressure on GDP.

Figure 2 - **GDP by Sector in 2004** (percentage)



Source: Authors' estimates based on Central Statistical Office data.

Figure 3 - **Sectoral Contribution to GDP Growth in 2004** (percentage)



Source: Authors' estimates based on Central Statistical Office data.

Malawi has consistently had negative savings rates for the past five years. This mirrors prevailing poverty in the country. Such a situation places serious constraints on Malawi's capacity to leverage private investment and explains its reliance on overseas development assistance to finance investment projects. Over the past five years, gross investment as a share of GDP has been hovering around the 11 per cent mark. It is expected that it will reach 11.3 per cent in 2005, which is lower by 0.1 percentage points than in 2004. However, some progress has been made in 2005 and the 2005/06 budget allocates 30 per cent of total expenditure to development, which is the highest allocation yet in the history of Malawi.

Table 1 - **Demand Composition** (percentage of GDP)

	1997	2002	2003	2004	2005(e)	2006(p)	2007(p)
Gross capital formation	**11.3**	**11.7**	**12.5**	**11.4**	**11.3**	**12.0**	**12.1**
Public	6.7	7.7	8.4	7.5	7.4	8.0	8.1
Private	4.6	4.0	4.1	3.8	3.8	4.1	4.0
Consumption	**101.0**	**106.2**	**110.2**	**105.4**	**108.8**	**107.6**	**107.5**
Public	17.5	14.7	16.3	17.1	16.1	16.9	16.9
Private	83.4	91.5	93.9	88.3	92.7	90.7	90.6
External sector	**-12.3**	**-17.9**	**-22.7**	**-16.8**	**-20.0**	**-19.6**	**-19.5**
Exports	21.7	23.9	26.8	28.8	25.7	23.6	22.7
Imports	-34.0	-41.9	-49.5	-45.5	-45.7	-43.2	-42.2

Source: National Statistics Office data; estimates (e) and projections (p) based on authors' calculations.

Macroeconomic Policies

Fiscal Policy

The government of Malawi has consistently run large budget deficits for the past five years. From a high of nearly 8.3 per cent of GDP in 2003/04, the budget deficit is expected to decline to 7 per cent of GDP in 2004/05. Improvement in the budget deficit is expected to continue over the next two years. In the past, the government was in the habit of overspending on activities of little benefit to the poor, e.g. travel, state residences, foreign affairs, defence, the National Intelligence Bureau and Special Activities. For the first time, the government has not had to recourse to unbudgeted expenditure in 2005. However, the lower current budget deficit appears to have been achieved mainly because of higher grants obtained by the central government.

Although there appears to be some political will to control government expenditure, some measures have been taken which seriously worsened the budget deficit. In 2004/05, the government put in place a fertiliser subsidy at a cost of 3.3 billion kwachas. The objective was to allow farmers to obtain fertilisers cheaply so that they could increase their productivity. Unfortunately, the programme was poorly managed in 2004, and the government was late in placing the orders for fertiliser, which reached the farmers only late in the season. The subsidy programme was renewed in 2005 and extended to include tobacco farmers, which has substantially increased its cost. The cost of the subsidies programme in 2005 was initially programmed at 2.8 billion kwachas, but was then increased to almost 5.7 billion kwachas. Higher than expected fertiliser expenditure was offset by postponing the 1 billion kwachas budgeted for local elections to the following year, and through cuts to the budgets of all other ministries except agriculture, education and health. However, these budget cuts were insufficient as the real cost of the subsidy was underestimated. Moreover, the subsidy also had a negative impact on the private sector fertiliser industry as it undermined distribution and pricing mechanisms.

On the revenue side, the government of Malawi has been quite successful in collecting taxes, especially in comparison with the rest of Africa. The political will to improve fiscal management has contributed to an increase in government revenues recently. Taxes, which account for almost all of the government’s non-grant revenue, have exceeded 20 per cent of GDP since 2003/04. However, 50 per cent of taxes are paid by one company (Prescorp), which makes government finances highly vulnerable. Moreover, grants have consistently accounted for a large share of the government’s total revenue. This share is projected to increase from 33 per cent in 2004/05 to 45 per cent in 2005/06. Such heavy reliance on grants to fund government expenditure presents some unique challenges. First, grants are highly unpredictable and may be withheld whenever the government does not meet donor expectations. This unpredictability means that it is difficult for the government of Malawi to commit to long-term expenditure programmes. Second,

Table 2 - **Public Finances** (percentage of GDP)

	1996/97	2001/02	2002/03	2003/04	2004/05	2005/06(e)	2006/07(p)
Total revenue and grants	**17.1**	**29.9**	**26.2**	**34.6**	**35.8**	**41.2**	**40.5**
Tax revenue	14.7	16.8	17.3	21.5	20.1	21.1	20.8
Grants	1.3	11.4	5.6	12.2	13.7	17.5	17.1
Total expenditure and net lending	**20.9**	**34.6**	**33.0**	**42.8**	**42.7**	**45.5**	**45.6**
Current expenditure	18.7	28.2	28.3	36.6	35.9	37.0	36.8
Excluding interest	*13.9*	*23.4*	*25.0*	*31.1*	*27.4*	*30.1*	*30.8*
Wages and salaries	4.5	5.9	7.1	6.3	7.9	8.2	8.1
Interest	4.8	4.8	3.2	5.6	8.4	7.0	5.9
Capital expenditure	0.5	5.0	4.6	5.6	6.3	7.6	7.9
Primary balance	**0.9**	**0.0**	**-3.6**	**-2.6**	**1.5**	**2.7**	**0.8**
Overall balance	**-3.9**	**-4.8**	**-6.8**	**-8.2**	**-7.0**	**-4.2**	**-5.1**

Source: Reserve Bank of Malawi data; estimates (e) and projections (p) based on authors' calculations.

a high level of grants flowing into the country can crowd out other productive activities. However, in view of the current food crisis and deep poverty in Malawi, there is a pressing need for increased aid. Nevertheless, it is advisable for the government to put in place a long-term strategy to reduce the dependency of Malawi on grants.

Finally, the financial performance of the agricultural marketing board of Malawi (ADMARC) has deteriorated over the years. It has consistently made losses and it is projected to lose 572 million kwachas during the 2004/05 fiscal year, up from a loss of 1 million kwachas in 2003/04. Such continued losses will only aggravate the government's consolidated budget deficit and this situation is not sustainable. Fortunately, unlike many non-oil producing countries in Africa, the state-owned electricity company was not affected by the oil price increase, because most electricity is generated by hydropower, and the rest from coal.

Monetary Policy

The fiscal deficits for 2001/02 to 2003/04 were largely financed by short-term borrowing through Treasury Bills issued by the central bank for sale to domestic banks. This high demand for local funds pushed T-bill rates to very high levels with the highest level reached in 2002 at 41 per cent. These rates have since been falling. However, they were still very high at 24.5 per cent in 2005. The consequences of using short-term instruments, which carry high interest rates, to bridge the budget deficit are that Malawi faces very high domestic debt servicing which is expected to reach 7 per cent of GDP in 2005.

From a high of 45 per cent in 2003, the Malawi Reserve Bank rate was lowered to 35 per cent in June 2004 and further reduced to 25 per cent in 2005. The high interest rate was a consequence of the previous government issuing T-bills to finance its budget deficit. A side effect of such behaviour was the high inflation rate which prevailed over the same period. A second inflationary factor, linked to the first, is the growth in money supply. The Reserve Bank of Malawi is allowed to provide short-term financial support to the government of up to 20 per cent of the government's expected revenue for the fiscal year. Money supply increased by 29.3 per cent in 2003 and 29.8 per cent in 2004. Such high growth rates in money supply are bound to yield high inflation rates. A third contributing factor to the high inflation rate was the shortage of food on the domestic market, leading to price increases that were accommodated by monetary expansion.

External Position

Malawi is a member of the Common Market for East and Central Africa (COMESA) and the Southern African Development Community (SADC). It has bilateral agreements with Zimbabwe and South Africa. Malawi is in the process of signing a Free Trade Agreement (FTA) with Mozambique and has negotiated a FTA with Tanzania. Malawi has been granted preferential market

Table 3 - **Current Account** (percentage of GDP)	1997	2002	2003	2004	2005(e)	2006(p)	2007(p)
Trade balance	-5.9	-9.4	-14.2	-16.6	-18.8	-18.5	-18.5
Exports of goods (f.o.b.)	20.2	21.4	24.6	26.6	24.9	22.8	21.9
Imports of goods (f.o.b.)	-26.2	-30.7	-38.8	-43.2	-43.7	-41.3	-40.3
Services	-6.4	-8.5	-8.5	-9.1	-8.9		
Factor income	-1.3	-1.9	-1.9	-2.4	-2.2		
Current transfers	-0.3	0.4	0.4	0.9	2.3		
Current account balance	**-14.0**	**-19.4**	**-24.2**	**-27.1**	**-27.5**		

Source: Reserve Bank of Malawi data; estimates (e) and projections (p) based on authors' calculations.

access to the United States and the European Union through the Africa Growth and Opportunities Act (AGOA) and Everything but Arms (EBA).

Malawi's traditional markets have been the European Union and the United States, which attracted more than 70 per cent of Malawi's exports. Over 95 per cent of Malawi's exports are made up of tobacco, sugar, tea, coffee, cotton, textiles and garments. Agricultural produce (mostly unprocessed) has comprised 85 per cent of major exports over the last three years. The textiles and garments sector is struggling to recover from the recent ending of the Multi-Fibre Agreement (MFA). Textile and garment export volumes remain small, particularly when compared with those achieved by other emerging clothing exporters in the region, such as Mauritius and Lesotho.

Malawi is currently developing a national export strategy. Central to this has been the analysis of development of the value chain on cotton, textiles and the clothing industry. The findings are not very positive for the garment-manufacturing sector for the following reasons. First, there is only one textile company in Malawi, which is small and inefficient, and has lobbied for increased tariffs on textiles. Second, the actual cotton staple in Malawi is not of the right quality for use by the textile company in Malawi. Third, the end of the MFA and long transport distances to ports mean that the window of opportunity for the existing textile and garment industry is limited.

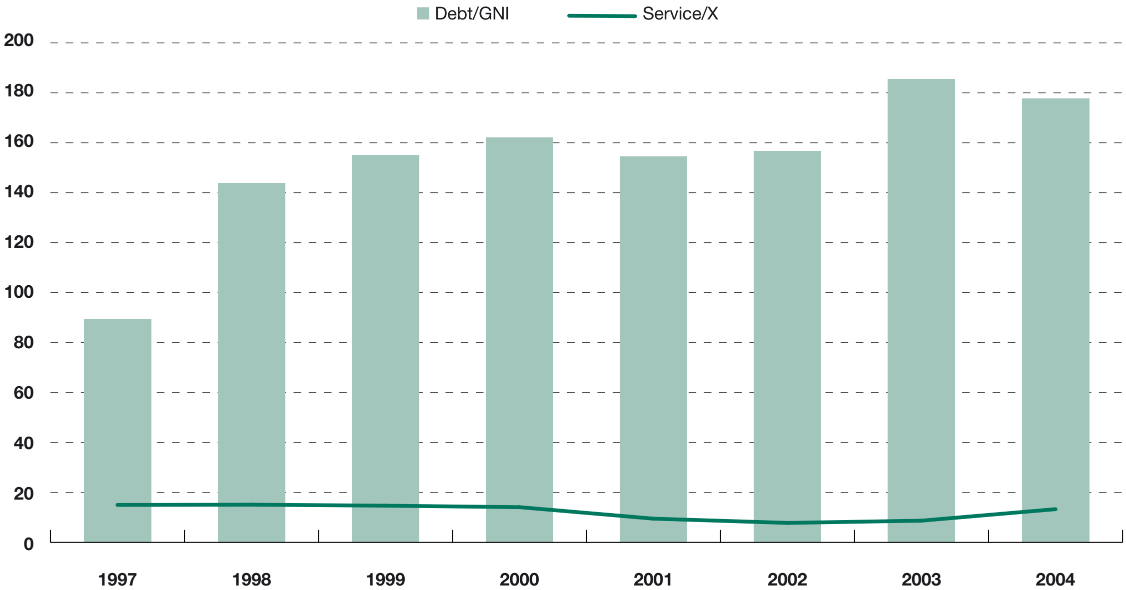
The composition of imports is far less concentrated than Malawi's merchandise exports and no single product category accounts for more than 17 per cent of total imports. Malawi's leading imports are vehicles (and parts), petroleum fuels, various types of machinery and fertilisers. During the drought years of 2001/02 and 2005, maize has been a major import. Other prominent imports are pharmaceuticals, iron and steel, paper and paperboard, plastics and plastic articles, products for the printing industry, wheat flour and cement.

Domestic debt levels are very high due to the previous government's loose fiscal policy. It is estimated that outstanding domestic debt is projected to rise to 23 per cent of GDP in 2005, from 22.6 per cent in 2004. The total debt stock as at the end of the third quarter of 2005 was $3 billion. Debt owed to multilateral creditors, at 91.9 per cent of the total debt stock, constituted the bulk of the country's external obligations.

Malawi is eligible for the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative for debt relief. However, reaching the HIPC completion point depends upon meeting several conditions, including *a)* the government achieving at least six months of successful PRGF implementation; and *b)* concurrently, achieving one year of implementation of the donor-supported Poverty Reduction Strategy which was recently put in place. It is expected that Malawi will reach the HIPC completion point by mid-2006. Given that 81 per cent of Malawi's external debt is with multilateral institutions, it stands to gain considerably when it reaches its HIPC completion point.

The kwacha has been depreciating regularly since the beginning of the year. In March 2003, the exchange

Figure 4 - **Stock of Total External Debt** (percentage of GNI) **and Debt Service** (percentage of exports of goods and services)



Source: IMF and World Bank.

rate was $1 to 97 kwachas. In 2005, the current official exchange rate was $1 to 115 kwachas. The foreign exchange reserves in December 2005 were estimated to cover only 1.2 months of imports. This was at the beginning of the lean period when the inflow of currencies is very low. The forex situation is hampering the imports of maize being brought in to alleviate the food shortage.

Structural Issues

Recent Developments

A large section of the population in Malawi has regularly faced an annual food deficit between maize harvests. This shortfall was, in the past, alleviated by the region's maize reserves. However, this is no longer the case. Internally, maize stocks have been reduced by poor government decisions. In addition, the drought at the beginning of 2005, poor provision of fertilisers and price controls all contributed to lower maize harvests. The government has been controlling the price of maize at 17 kwachas per kg. Externally, the neighbouring countries of Zambia and Zimbabwe have also suffered from adverse weather conditions. They are now importing, rather than exporting, maize. As a result, the government of Malawi estimates that 2.1 million metric tonnes of maize is needed to cover the needs of the population for the 2005/06 marketing season. Taking into consideration carry-over stocks, the food shortfall for 2005 amounts to approximately 482 608 tonnes.

Government interventions in the maize market have generally undermined the private sector, which cannot enter into import contracts on maize with the confidence that the government will not interfere and bring in subsidised maize. Moreover, the export ban stops commercial farmers from growing maize, as they will not be able to export their surpluses. Price controls on the maize market also force the private sector to sell at a loss. The main subject of discussion in Parliament over the past 35 years has always been maize and fertiliser. The government does not have the confidence to leave maize distribution to the private sector. As a result, discussions between the private sector and government on the importation of maize frequently break down and there is no real partnership on these issues.

A direct consequence of the food shortage is increased poverty, which has remained persistently high during the past 10 years. The second Malawi Integrated Household Survey (carried out between March 2004-April 2005) found that 52 per cent of the population is poor (living on less than $0.40 per day), and that 22 per cent is ultra-poor (living on less than $0.24 per day). The incidence of poverty does not appear to have changed significantly over time, as 54 per cent of the population was classified as poor in the previous 1997/98 survey. There are, however, important regional variations in poverty rates. The southern region has the highest poverty rate (60 per cent), followed by the northern region (54 per cent) and the central region has the lowest proportion (44 per cent) of poor people. About 25 per cent of the population in urban areas is poor, compared to 56 per cent of the rural population. A similar pattern is observed for the ultra-poor with an ultra-poverty rate of 7 per cent in urban areas compared to a minimum of 16 per cent in rural areas. Finally, while 51 per cent of individuals in male-headed households are poor, the corresponding number for female-headed households is 59 per cent.

Poverty is also having a negative impact on children's development. In 2004, 48 per cent of children under five years of age in Malawi were growth-stunted and 22 per cent were severely growth-stunted. Five per cent of children are emaciated or too thin, and 22 per cent are underweight. Children's nutritional status in 2004 was virtually identical to their status in 1992 and 2000, indicating that there has been no improvement in the nutritional status of children under age five since 1992. The under-five mortality rate in 2004 is still one of the highest in the world at 133 deaths per 1 000 live births.

The commercial cultivation of tobacco in Malawi dates back to the 1890s. Since then, tobacco has been the main cash crop of Malawi. The number of smallholders producing tobacco has increased dramatically since the repeal of the Special Crops Act in 1994, which restricted the production and marketing of high value crops to big farm holders. As a result, smallholders now account for 80 per cent of national crop production. Tobacco producers face three main problems. First, the declining international price of tobacco has had adverse effects on their profitability. Second, they find it difficult to compete against EU tobacco producers because of the subsidies these receive. Producers in four EU tobacco-producing countries receive $1.60 per kg of tobacco, which was higher than the average auction price of tobacco in Malawi in 2005. Third, the demand for tobacco in developed countries has not grown because of the anti-smoking lobby.

Malawi tobacco producers also face stiff competition from other developing countries, in particular Brazil. There is some concern that if Brazil is granted duty-free access to the EU, Malawi tobacco will lose out because of its higher cost. Tobacco imports into the EU from some competing countries such as Brazil and the United States, are charged with a levy of $0.26-0.29 per kg. Without that levy, Brazil would be more competitive than Malawi because farming there is carried out on a larger scale.

Between 80 000 and 100 000 smallholder households typically cultivate cotton together with maize and drought-resistant small grain crops. Current crop estimates are in the region of 40 000 tonnes, much lower than the 80 000 tonnes produced in 1988. A variety of factors have contributed to these adverse developments, namely the deteriorating quality of available planting seeds, with limited introduction (or approval) of newer varieties, inefficiency in marketing arrangements translating into substantially lower prices for farmers and limited farmers' access to credit. The formation of the Cotton Development Association (CDA) in 2003, which brings together the main private sector stakeholders in the cotton sector, has had some success in stimulating production.

There have been some efforts to diversify agriculture. For instance, there has been considerable investment in the cotton sector where output has doubled over the past two years. There has also been investment in coffee to sell it fully processed and packaged and to build niche markets. Finally, macadamia nuts are also actively being promoted. These efforts have contributed to the slight diminishing of reliance on tobacco as a source of foreign reserves for Malawi. However, it should be noted that tobacco exports have also decreased because of lower world prices and market changes.

The private sector in Malawi is small, with a shrinking manufacturing sector amounting to about 13 per cent of GDP, employing about 3 per cent of the labour force. Malawi does not offer a favourable environment for private-sector development. Drawbacks include its landlocked situation, geographical distance from seaports and poor power supply. Indeed, the 40 megawatt capacity Tedzani I & II power station has been out of service for two years, the interconnection from Caborra Bassa (Mozambique) is progressing too slowly and the current Walkers Ferry power station suffers from stoppages. The cost of telecommunications is high in Malawi because of monopoly control of landline services by the state-owned Malawi Telecommunications Limited, the current duopoly on mobile phone networks, and over-regulation and control of the market by the Malawi Communications Regulation Authority. Internet access is also very expensive; a dedicated 64 kilobyte broadband line cost more than $400 per month in 2005. In that regard, it is unfortunate that the privatisation of Malawi Telecommunications Limited was called off at the eleventh hour by presidential order.

Transport Infrastructure

Malawi has 7 717 km of roads, a third of which are paved. While 94 per cent of paved roads are in good condition, only half of those that are unpaved are deemed to be in good condition. The poor road conditions in Malawi mean that domestic transport costs are much higher than in neighbouring countries. In Malawi they are equivalent to about $0.065-0.075 per tonne/km while in South Africa and Zimbabwe they are much lower at about $0.02 on trunk roads and $0.035 on rural roads. With freight rates being set or "recommended" by the Road Transport Operators Association, the full benefits of a more liberalised market have not yet reached Malawian producers and consumers.

Malawi has a total of 797 km of single-track public railway line of which 717 km are operational. The rail network extends from near the Mozambique border in the south through Blantyre, up to Salima in the north, at which point it changes direction and continues west through Lilongwe, to Mchinji and the Zambian border. There is also a privately-owned 25 km branch off the main north-south line from Namatunu to Changalume. Rail is only used to carry freight, as passenger services are currently suspended. In fact, rail was the main mode of transport for Malawi's foreign trade before the lines to Beira and Nacala were severely damaged in 1984/85. In addition, a 77 km section of track between Cuamba and Entrelagos that was damaged in floods in 2001, has not yet been repaired.

Malawi has four international airports; two major airports in Lilongwe and Chileka (Blantyre) and two minor airports in Mzuzu and Karongo. In addition to these international airports there are a further 19 registered airfields in Malawi, of which four are privately owned. There are also at least 10 known unregistered airfields throughout Malawi. Passenger and airfreight flight schedules and services have been cut, and more use is now made of regional hub airports for international flight links. There are no direct links between Malawi and Europe. The decline of international commercial flights into and out of Malawi, together with restrictions on landing rights (minimum 48 hours prior notice), the high landing and service fees, and a requirement to pay Air Malawi a royalty of 4 per cent on all air cargo, have all contributed to the relatively poor availability and very high cost of airfreight services out of Malawi. As a result, Malawi's cut-flower exporters have had to pay upwards of $2.20 per kilogramme for airfreight to Western Europe, compared with rates of between $1.60-1.85 per kg paid by their Kenyan, Zimbabwean and Zambian competitors.

Lake transport was commercialised in 1994 with the establishment of the state-owned Malawi Lake Services Ltd. However, the company continued to run at a loss, receiving a government subsidy of approximately 25 million kwachas per annum. The service has now been privatised to Glens Waterways Limited and ports are to be privatised next. Lake traffic has fallen since a parallel road to the north was built. The competitiveness of lake transport is compromised by the unsuitability of much of the sailing fleet. Investment is required to improve infrastructure, including the construction of jetties, at some of the ports. River transport provided a barge service all the way to Chinde on the Mozambican coast before being stopped by the Mozambican civil war. The investment required to reinstate this service would be significant, but it could contribute to diverting some of the excessive Beira road traffic.

Transport costs are by far the single largest expenditure factor for Malawian farmers. For example, in 2004, transport costs accounted for 46 per cent of the landed cost for urea in Lilongwe and one-third of the retail price paid by farmers. Nearly one-third of the pump price for fuel in Malawi can be attributed to transport costs. While Malawi is an efficient producer of sugar, regional and international transport costs add nearly 50 per cent to production costs for Malawian sugar. Logistical bottlenecks along the Nacala and Beira rail routes have resulted in nearly 60 per cent of Malawi's tobacco exports being sent overland to the more distant port of Durban. The government of Malawi is tasked with the formidable challenge of improving both internal transportation and external links in a context of severe budget constraint. It is clear that it will need foreign assistance and the involvement of the private sector to improve the capacity of the transport sector.

Political and Social Context

The latest presidential election was held on 20 May 2004, which voted in the current president who had campaigned as a United Democratic Front (UDF) candidate. However, since coming to power, President Bingu wa Mutharika has faced severe opposition within his own party, allegedly over his stance on corruption. He consequently left the UDF to found his own Democratic Progressive Party, which, however, has no seat in parliament. It is prohibited for a deputy to cross the floor in this manner in between elections in Malawi. Moreover, no party has a clear majority in parliament. This puts the president of Malawi in the awkward position of having to fight for support on every single issue, which has resulted in a hung parliament, making it difficult for the president to implement the current reform programme or government policies. Hence, only four acts of parliament have been passed since the new government took over. Parliament has failed to approve the budget on time.

This political fight culminated in October 2005 with more than 50 members of parliament signing a petition ordering the president to appear before court for impeachment hearings. The impeachment hearings were temporarily halted by the constitutional court. The general conflict in parliament between the political parties and the president have increased Malawi's risk profile internationally and increased the cost of borrowing as the Berne Union credit rating dropped one level.

Civil society is strengthening in Malawi but is still considered weak. A culture of not speaking out against the government was prevalent during Banda's rule. Many civil society organisations and networks educate the public about their rights and responsibilities and in how to interact with government. Recently civil society groups have been monitoring the government's budget and pro-poor expenditure (PPEs). The Civil Society Agriculture Network (CISANET) includes about 50 organisations that monitor three PPEs: agricultural inputs, agricultural extension, and small-scale irrigation. CISANET wants monitoring and evaluation systems implemented in communities so that information will be available to district and central offices of the agriculture ministry. CISANET also participated in monitoring the budget.

In the 2004 and 2005 Transparency International Corruption Perceptions Index, Malawi scored 2.8 and ranked 93rd out of 145 countries. This ranking is comparable with countries in the region such as Mozambique (2.8), Tanzania (2.8), and Zambia (2.6). Unfortunately, Malawi's score has deteriorated since 2000, when it had a CPI rating of 4.1. However, there is ground for optimism. The new government has declared a policy of zero tolerance on corruption and has already taken steps to enforce this policy. The Anti-Corruption Bureau (ACB) was strengthened in early 2004 through an amendment to the Corrupt Practices

Act. It is now required that cases referred to the Director of Public Prosecution, but that are not prosecuted, be reported to Parliament. The ACB is very active and has not been afraid to prosecute high-profile individuals. The minister of education was dismissed because of misappropriated funds. There is progress in the audit of domestic arrears. The passage of legislation to strengthen financial management will contribute to a more efficient government. In November 2005, an electronic central payments system came into operation whereby all financial transactions are verified and paid through the office of the Accountant General.

The national adult literacy rate is still low at 63 per cent. It is higher among males (76 per cent) than among females (50 per cent). The overall youth literacy rate is 76 per cent, which is far higher than the adult literacy rate. Interestingly, there is not much disparity between the literacy of young females and males. The primary gross enrolment ratio is 137 per cent. The rate is significantly higher for boys (144 per cent) than for girls (130 per cent). These high enrolment numbers indicate that a large proportion of primary school pupils are over-age for their grade. This could partly be explained by delayed enrolment, and high dropout as well as high repetition rates.

The 2004 Malawi Demographic and Health Survey found that 8 per cent of children aged 5 to 14 worked for non-household members. About 40 per cent of these children work without pay. Among children who help around the house with household chores, 68 per cent do these chores for an average of less than 4 hours per day and 2 per cent work for 4 or more hours per day. Overall, older children and children in rural areas are more likely to be working. Girls are more likely than boys to do domestic work. It is particularly worrying that a recent ILO (International Labour Organisation) survey found that at least 71 per cent of children were employed in the worst form of child labour.

Malawi, like the rest of southern Africa, has very high levels of HIV prevalence. HIV prevalence at rural clinics increased from 12.1 per cent in 1999 to 14.5 per cent in 2003. Much remains to be done in order for behavioural change to take place. In 2004, only 5 per cent of women and 15 per cent of men who had sex in the past year reported having used a condom during their last sexual intercourse with any partner. At 1.8 per cent, condom use is alarmingly low among married women. This may point to the difficulty women face in negotiating the use of a condom with their husband. Better-educated persons are more likely to use condoms. For example, while 2 per cent of women with no education used a condom during sex with their last partner, the corresponding proportion for women with secondary or higher education is 14 per cent. The proportions for men are 6 and 27 per cent respectively.

The total fertility rate for women aged 15 to 49 has declined from 7.6 births per woman twenty years ago to 6 in 2004. Contraceptive use, especially modern methods, has continued to rise since the early 1990s and is one of the principal causes of the fertility decline. The prevalence of modern contraceptive methods among married women aged 15 to 49 has increased from 7 per cent in 1992 to 33 per cent in 2004. The most popular contraceptive method among married women is injectables, followed by female sterilisation, and the pill.

