FINANCIAL MARKETS DEPARTMENT

WEEKLY FINANCIAL MARKET DEVELOPMENTS
(30 AUGUST – 03 SEPTEMBER 2021)

Main Highlights

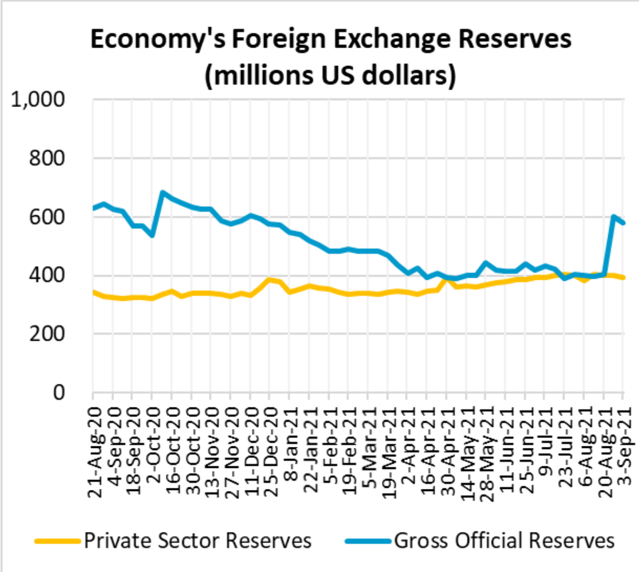
- ***Gross official foreign exchange reserves, which have been falling steadily over past several weeks, have improved significantly***. Last week, the gross foreign exchange reserves increased to US$580.9 million (2.32 months of imports), from US$404.2 million (1.62 months of imports) recorded at end July 2021, mainly on account of IMF SDR inflows.

- ***The Malawi Kwacha has stabilised around K818 per US dollar,*** and registered a depreciation rate of 0.01% (11 tambala loss in value) against the US dollar during the review week and 0.34% (K2.79 loss) throughout August 2021.

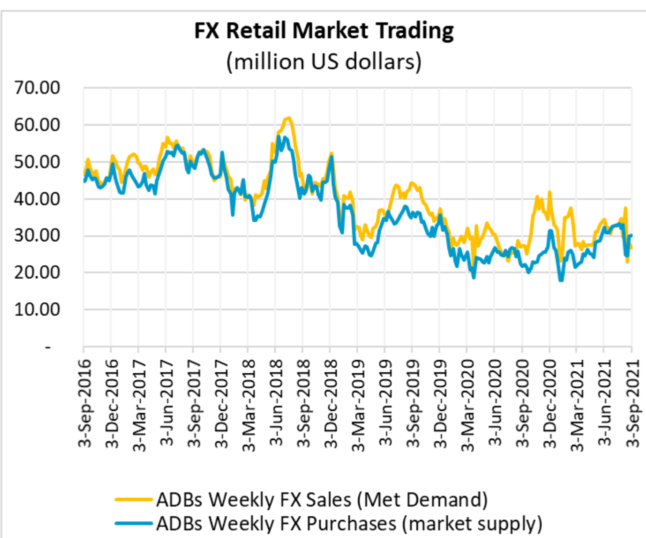
- ***Liquidity conditions in the banking system remain very tight***. The daily commercial banks' excess reserves, *before borrowing from the central bank*, averaged negative K46.1 billion during week ended 3rd September 2021, compared to negative K40.1 billion recorded during the preceding week.

- ***Government continues to raise less funds on the Treasury securities primary market than indicated in the issuance calendar during the 2021/22 fiscal year*** amid tight liquidity conditions.

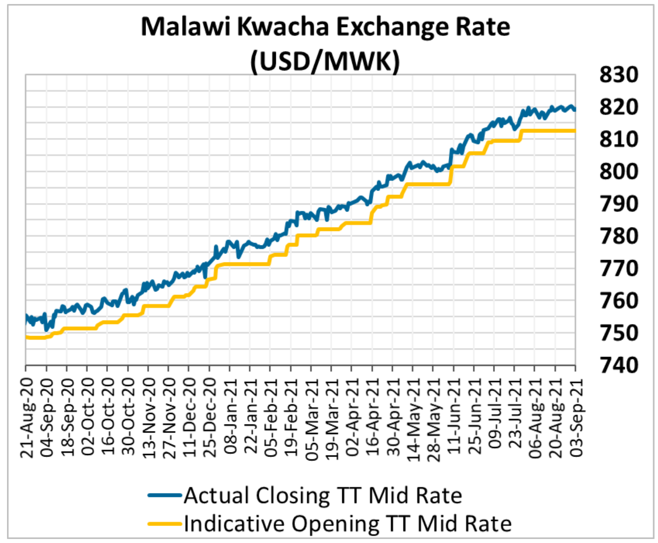
The gross official foreign exchange (FX) reserves recovered from a declining trend observed during the year through August 2021, and closed the review period at US$580.9 million (2.32 months of imports), mainly reflecting the IMF SDR inflow of US$188.70 million. Despite the significant improvement, the reserves are inadequate to cover essential imports for a prolonged period. The low reserves reflect underlying macroeconomic imbalances, which have been manifested in the foreign exchange market, with demand increasingly outstripping supply. The bigger concern is the weak export base and an ever-increasing appetite for imports, which poses a risk for accumulating a sustainable foreign exchange reserves position. The need for diversifying the export base and generating more foreign exchange has become more apparent.



Trading on the FX retail market improved especially during the second quarter to date compared to similar period last year, albeit remained subdued relative to similar periods in years preceding the Covid-19 pandemic. Supply of FX to the market averaged US$27.3 million per week this year to date, compared to US$24.3 million, US$32.5 million, US$44.0 million, and US$47.6 million recorded during similar periods in 2020, 2019, 2018, and 2017, respectively.

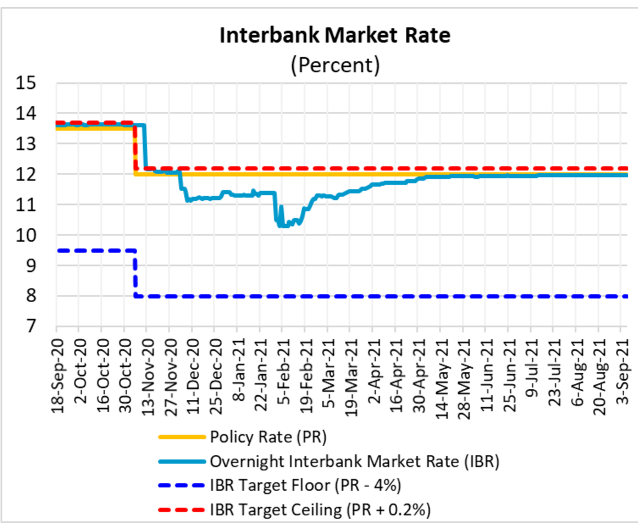


The Malawi Kwacha has remained broadly stable at around K818 per US dollar since end-July 2021, losing a mere 0.19 percent (K1.55) in process. Week-on-week, the Kwacha closed the review period at K818.9767 per US dollar compared to a position of K818.8623 per US dollar recorded by end of preceding week, representing a minor depreciation rate of 0.01% (11 tambala movement). Since the beginning of this year, Kwacha has cumulatively lost 5.6 percent (K45.86 movement) against the US dollar, 8.7 percent (K104.18 movement) against the British Pound, 5.0 percent (K51.83 movement) against the Euro, and 7.8 percent (K4.78 movement) against the South African Rand.



Kwacha liquidity conditions in the banking system has remained tight since second quarter of 2021, mainly on account of net issuance of Treasury securities, net withdrawals from foreign exchange operations and, recently, the central bank's gradual reduction of reverse repo operations. During the review week, daily commercial banks' excess reserves, before borrowing from the central bank, averaged negative K46.1 billion compared to negative K40.1 billion recorded during the week ended 27th August 2021 and negative K46.6 billion observed in week ended 20th August 2021. In tandem with the prevailing liquidity conditions, daily average access on the Lombard window increased to K73.7 billion from K55.3 billion recorded during the previous week. Similarly, borrowing on the interbank market increased to average K13.5 billion per day from K11.6 billion per day recorded during the preceding week.

The Overnight Interbank Market Rate (IBR) has stayed closely aligned to the policy rate since mid-November 2020. During the week ending 3rd September 2021, the IBR stood at 11.98 percent, and remained within the target corridor of +0.2/-4.0 percentage points around the policy rate, which is essential for the signaling role of the Policy rate and effectiveness of monetary policy transmission through the interest rate channel. The interbank market represents the first stage of monetary transmission channel, where monetary policy actions first come into contact with the rest of the financial system.



During the review week, total central bank operations with the commercial banks were contractionary, withdrawing a net of about K24.0 billion from the banking system. Government operations withdrew a net of K4.5 billion by issuing more Treasury securities than what was maturing [resulting in K19.7 billion net withdrawal] and in process overriding the K15.2 billion liquidity injection emanating from running a primary deficit. Commercial banks currency withdrawals from the central bank to meet customer demands and net foreign exchange operations further drained K7.8 billion and K6.0 billion, respectively from the banking system. Lastly, central bank open market operations (OMO) withdrew a net of K6.8 billion through K14.6 billion net maturity of reverse repos that were partially countered by K7.8 billion net commercial banks access on the Lombard facility.

The tight liquidity conditions have hit the Government securities auction. Consequently, Government continues to under-allot relative to planned issuance on Treasury securities auctions in 2021/22 fiscal year. During the review week, government raised a total of K29.0 billion against total subscription amounting to K31.3 billion, planned issuance of K55.6 billion, and Treasury securities maturity totaling K61.0 billion. The Treasury bills allotment was 97.0% of subscription and 102.7% of planned issuance while Treasury notes allotment was 89.0% of subscription and 35.7% of planned issuance. Cumulatively in 2021/22 fiscal year, Treasury securities allotment stands at 82.7% of subscription and 38.6% of planned issuance as per the issuance calendar.