RESPONSE OF THE MALAWI CONFEDERATION OF CHAMBERS OF COMMERCE AND INDUSTRY TO THE 2024/25 NATIONAL BUDGET PRESENTED IN PARLIAMENT ON 23rd FEBRUARY 2024

Contents

1. Preamble

The Malawi Confederation of Chambers of Commerce and Industry (MCCCI) (hereinafter referred to as the Confederation) is an apex body of private sector players in Malawi that exists to advance the interests of businesses and provide value-adding services to them. The Confederation's membership accounts for a significant contribution to the economic output of the country. As such, it would like to provide its response to the 2024–2025 fiscal budget that the government, through the Ministry of Finance and Economic Affairs, presented to Parliament on February 23, 2024.

This response follows proposals that the Confederation submitted to the Ministry of Finance and Economic Affairs during the 2024–2025 Fiscal Budget consultation process. The private sector makes the biggest tax contribution, and as such, ensuring its survival must be of paramount importance to the government. The private sector budget proposals are centered on taxation and economic policy as well as regulatory interventions that will provide quick wins and long-term solutions to the economic challenges that Malawi is currently facing while steering the country toward the realization of its goals and aspirations. The confederation appreciates that the 2024–25 fiscal budget has taken into account expert advice to increase the allocation towards development expenditure despite increased demand for social safety programs as a result of economic shocks. The proportion of development expenditure to the total budget now stands at 30 percent, up from 24 percent in the 2023–24 financial year. This is a clear signal to the private sector that the government is serious about its long-term development aspirations.

In a nutshell, total revenue and grants for the 2024–2025 fiscal year are estimated at K4.55 trillion, representing 24.3 percent of GDP. Domestic revenues are estimated at K3.38 trillion, representing 18.1 percent of GDP, of which, tax revenues are estimated at K3.26 trillion and other revenues have been projected at K126.54 billion. The total expenditure for the 2024–2025 fiscal year is programmed at K5.98 trillion, representing 31.9 percent of GDP. Of the total expenditure, recurrent expenses are estimated at K4.21 trillion, representing 22.5 percent of GDP and 70.4 percent of total expenditure.

2. Introduction

The theme of the 2024–2025 Fiscal budget, "From economic recovery to resilience through accelerating production and enhancing the legal and regulatory environment to protect the economy," dives deeply into the long standing issue of dwindling productivity that the country has been facing for a long time. This dwindling productivity in all economic sectors has worsened since the onset of a series of economic shocks in 2020, and this theme shows government commitment to revamping the economy. This theme recognizes the role of legal and regulatory frameworks in the creation of an economic environment that attracts and attains both domestic and foreign investment. It is our expectation as the private sector that the recovery and resilience being discussed here should trickle down to individual companies.

3. Macroeconomic analysis:

3.1 Business Environment and Economic Policy

The economic environment in Malawi continues to be unfavorable due to a number of shocks that have been hitting the country in the past 3 years. Since, 2020, the economy has been hit by the COVID-19-induced economic slowdown (2020), disruption in the global economy due to geopolitical tensions in Ukraine (2022), Cyclone Anna (2022), and Cyclone Freddy (2023), which compounded the effects of all the previous shocks. The shocks have worsened the macroeconomic imbalance, as evidenced by the scarcity of forex, higher levels of inflation, and the high cost of loanable funds due to high interest rates. Currently, the country is going through a prolonged dry spell, which will affect agriculture productivity in the 2024–25 consumption year. This poses a threat to the aforementioned economic recovery and resilience.

It is against this background that the private sector was expecting a budget that will help to incentivize productivity for both exportation and import substation purposes, and not the welfare budget that was presented in the August House. Private sector is looking forward to seeing an improvement in macroeconomic fundamentals by the end of this financial year. In its pre-budget propositions, the Confederation outlined a number of interventions to help unlock the productivity potential of businesses across all sectors.

To develop and catalyze growth, government has identified anchor sectors that have been chosen for their potential to contribute to economic growth. The anchor sectors are Agriculture, Tourism, and Mining, commonly referred to as ATM. The ATM Strategy aims at boosting domestic revenue in this budget; such that these sectors will have significant allocations. The confederation agrees with the government that the identified sectors (ATM) have untapped potential that, if unlocked, would increase productivity, employment, and the trade balance. However, the confederation is surprised that the manufacturing sector, as the second pillar of Malawi Vision 2063, has not been included as a key strategic sector. This sector plays a big role in increasing value from the other anchor sectors which cannot be overlooked.

The confederation would like to commend the government for securing the Extended Credit Facility (ECF) Program from the International Monitory Fund (IMF). The ECF amounts to US$175 million, with the first tranche of US$35 million disbursed immediately upon approval in November 2023. The intervention has assisted the country in the recovery process, as evidenced by the stability in fuel supply. The confederation also concurs with the long-term initiatives that the government has outlined to boost the forex earning capacity of the country. The initiatives include the following: Mega Farms, Labour Export, Carbon Credits Trading, Mining Discounted Projects, and Cannabis Biomass Projects for export diversification; the Golden Visa Programme; the introduction of Diaspora Cities; and enhancing diaspora remittances. However, the private sector is unable to obtain forex for the importation of raw materials, especially in the manufacturing sector. Players in the manufacturing sector noted that the problem has been exacerbated by the 30 percent export proceeds surrender requirement, which authorities introduced as a way of attracting foreign exchange into the official system. The sector was looking forward to the downward revision of the requirement in the 2024–25 budget statement.

The agriculture sector has been allocated a total of K497.75 billion, representing 8.3 percent of the total budget. This is on point, as the sector continues to be the backbone of our economy by driving the activities in the other sectors. Agriculture commercialization requires massive investment in irrigation and machinery, and the confederation is pleased to see such allocations in the budget towards the following projects: the Agricultural Commercialization Project, the Shire Valley Transformation Project, and the Programme for Rural Irrigation Development (PRIDE), just to mention a few. The confederation is also pleased to see that the government has struck a deal with the People's Republic of China on shelled groundnuts and soybean exports. It is, however, unfortunate that the country has failed to fully utilize deals of similar caliber. Therefore, there should be an allocation of resources to facilitate the private sector's uptake of all existing export deals. The confederation requests that the government also focus on making export deals involving exports of processed or finished goods, as such deals would create more value for the economy than raw goods. As the country is going through a period of drought, it is very likely that agriculture productivity will be affected. It will be of critical importance for government to react very quickly by implementing the identified irrigation projects to ensure that food prices remain stable throughout the year.

In the Transport and ICT sectors, the confederation commends government for allocating resources amounting to K439.64 billion, representing 7.4 percent of the national budget. Poor infrastructure has been one of the contributing factors to transport-related costs that feed into the final products of our goods and services. In addition to the new infrastructure projects proposed in the budget, the confederation would also like to see the timely completion of infrastructure projects that are currently underway. The introduction of a one-stop border post, a national single window, and coordinated border management has positively affected the clearance of goods at the borders. However, there are still inefficiencies, especially at the inland examination centers, that need to be ironed out. Therefore, the confederation proposes that resources be allocated to borders and inland examination centers to train agents and help in the acquisition of machinery with the aim of making clearance processes more efficient.

There is a massive improvement in the energy sector following the rehabilitation of Kapichila Power Station. The allocation of resources towards the construction of the 361 megawatt Mpatamanga Hydropower Project and the construction of the 50 megawatt Nanjoka Power Plant in Salima District will contribute significantly to the supply of electricity in the country. The confederation requests that the government finalize projects and deals in the sector as the electricity demand is currently higher than the supply.

3.2 Assumptions of the Budget

The 2024/2025 budget has been formulated with the following underlying assumptions:

i. Real GDP growth rate of 3.6 percent
ii. Average Inflation rate of 23.4 percent
iii. Tax refunds of 3.0 percent of total tax collection

The Confederation notes that the budget has been based on the assumption that the annual average inflation will be 23.1 percent. It is evident that significant inflation pressures continue to exist, both from domestic and external factors. Domestic pressures remain high on food inflation as well as nonfood inflation. Even though domestic pressure arising from food inflation have been deemed transitory on account of seasonal factors, recently experienced unfavorable weather patterns, including the cyclones that affected the county in the last two years, have complicated matters as the lagged effects continue to exert pressure on food inflation all year. Furthermore, El Nino weather has downplayed expectations from agricultural production for 2024, which might lead to a shortage of food supply on the domestic market and agricultural exports. Lagged effects of the devaluation of the Malawi kwacha by more than half in 2023 also add to the inflation risks in 2024. The Confederation is of the view that the current inflation assumption ought to be revised upward to match the situation on the ground.

The confederation also notes that the budget is based on the assumption that real economic growth will grow by 3.6 percent in 2024. The assumption on growth is higher than the projection that the Ministry of Finance and Economic Affairs made at the end of 2023. Furthermore, the assumption on growth is also on the higher side than the projections from the International Monetary Fund and the World Bank for 2024. The confederation notes that the agricultural season for 2023–2024 has been affected by dry spells, most notably in the southern region, which might affect agricultural production. Not only that, despite the approval of Extended Facility from the IMF, the availability of foreign exchange on the market continues to be a challenge for the operation of businesses. Therefore, the confederation is of the view that the assumption on growth should be revised downward.

4. Fiscal Analysis

The confederation alluded to government's commitment in implementing the Public Finance Management (PFM) reform agenda articulated in the Public Finance Management Strategy (2023–2028). The progress made by the ministry of Finance and Economic Affairs to operationalize the Public Finance Management Act (2022) through gazetting the Public Finance Management Act Regulations in 2023 is welcomed by the Confederation. The Confederation also noted that in the 2024–2025 financial year, the Ministry of Finance will go further by reviewing Treasury and Desk Instructions. The Confederation views this as a tool that could be used in strengthening budgeting, revenue and expenditure management, internal controls, and other areas of public finance management. The initiative of the Treasury Single Account (TSA) will also play a crucial role in safeguarding public resources from the misuse they have been subjected to over the years. The Confederation hopes that the enactment of the Public Finance Management (PFM) Act will ensure accountability and efficiency in the usage of public financial resources.

4.1 Revenue and expenditure

The Confederation notes that the total revenue and grants for the 2024–2025 fiscal year are estimated at K4.55 trillion, representing 24.3 percent of GDP. This is an increase in the share of GPD compared to total revenue, including grants, of K2.99 trillion, which is 19.7 percent of GDP for the 2023–2024 fiscal year. In 2024/2025, domestic revenues are estimated at K3.38 trillion, representing 18.1 percent of GDP, of which tax revenues are estimated at K3.26 trillion and other revenues have been projected at K126.54 billion. In the 2023–2024 financial year, domestic revenue is expected to reach K2.41 trillion, of which tax revenue is estimated at K2.20 trillion and K209.34 billion is other revenue, representing 14.7 percent of GDP.

Recurrent expenses are estimated at K4.21 trillion, representing 22.5 percent of GDP and 70.4 percent of total expenditure in the 2024–2025 financial year, compared to the 2023–2024 financial year, where they were estimated at K3.31 trillion. The confederation notes that recurrent expenditures will take up at least 92 percent of total revenues, which are projected at K4.55 trillion. The recurrent expenditures are also marginally higher than domestic revenues, which are projected at K3.38 trillion. The mismatch between expenditures and revenue will lead to a projected deficit or fiscal balance of K1.43 trillion, representing 7.6 percent of GDP and 23.91 percent of total expenditures. This does not bode well for the economy taking into consideration that the total public debt stood at K12.56 trillion as of December 2023, representing 84.8 percent of GDP. The Confederation is of the view that this deficit financing plan will only shrink fiscal space further. The recurrent expenditure should be within budget levels and improve planning and execution on the development budget. Doing this would have positive spill-over effects on growth and translate to an improved domestic revenue and resource envelope.

In 2024-25 fiscal budget, it is commendable that government has increased development expenditure from K896.21 billion in the 2023–2024 financial year to K1.77 trillion in 2024–2025FY. The proportion of development expenditure to the total budget now stands at 30 percent, up from 24 percent in the 2023–24 financial year. Projects include the rehabilitation of 16 roads across the country, development of tourism, and other investments in agriculture and mining sectors. The increase comes at a crucial time as the country recovers from the damage caused by Cyclone Anna. For instance, development of roads enhances logistics of goods from one place to another with ease thereby promoting a conducive environment for businesses.

Furthermore, the confederation noted that after being inactive operations for the most part of 2023, in the 2024–2025 fiscal budget, K12 billion has been allocated for maize purchases by the National Food Reserve Agency to replenish the Strategic Grain Reserves. ADMARC has also been allocated K40 billion for operations, revamping agricultural production, and value addition. The confederation commends this allocation because the National Food Reserve Agency and ADMARC play a crucial role in stabilizing food prices in the country. As seen in 2023, much as food production was low, the inactiveness of ADMARC also played a huge role in the upsurge in food inflation.

5. Tax Policy Measures

Government has put in place tax incentives and regulation. Effective on 23rd February 2024, Customs and Excise tax measures came into force, while Value Added Tax (VAT), Income Tax, and Administrative Measures will take effect on 1st April 2024 upon the passage of relevant Bills by the August House and assertion by His Excellency the President. The following are some of the measures:

5.1 Value Addition Thresholds

- Allowing the Malawi Army, Malawi Police Service and Malawi Prisons to import duty-free fabrics and accessories for making uniforms under the Customs Procedure Code (CPC) 421. The confederation commends this initiative because it will encourage growth of the local textile industry instead of importation of already made uniforms.
- The confederation commends government for Increasing import duty on finished iron sheets on tariff subheading 7210.49.90 from 15 percent to 25 percent and for sacks of tariff subheading 6305.33.00 from 20 percent to 25 percent as well as introduction of a surcharge of 10 percent on sacks for cement packaging. This will help in import substitution which is needed at this moment and also help the local industry to develop.
- The confederation also commends government for answering the call from private sector taxpayers who have been complaining on the costs associated with the use of Electronic Fiscal Devices (EFD). In order to reduce compliance costs and ease administration of VAT, Electronic Fiscal Devices will be phased out to allow for the introduction of a new electronic billing system for the effective implementation of the VAT Act.

5.2 Excise Tax Measures

- As one way of promoting the use of locally sourced raw materials for production and promote local farmers, government has reduced excise tax on clear beer made from sorghum and maize from 40 percent to 20 percent. The confederation applauds government for this initiative as it will not only boost manufacturing, it will also increase uptake of maize and sorghum into the industry hence providing a ready market for farmers.

5.3 Income Tax Measures

- To cushion employees in formal employment from the effects of the currency alignment, government has increased the zero Pay as You Earn (PAYE) bracket from MK100, 000 to MK150, 000. The confederation applauds government for this consideration as it will indeed help cushioning employees from the impacts of the devaluation of the local currency. Furthermore. it will also ease up wage demand for businesses.

- Government has further extended application of the additional 10 percent corporate income tax on profits above K10 billion to all businesses that make such profits in order to ensure equal and fair treatment of super normal profits. The confederation views that the assumption that profits above K10 billion are automatically ‘super normal’ regardless of how much is invested in the enterprise is utmost flawed. The investment capital required for each business is different hence they can never be treated same. This policy decision is counterproductive and will discourage big investments as it indirectly restricts investments to investments below K10 billion. Furthermore, this policy runs contrary to our aspirations of attracting big mining investors and big investors in mega farms as part of the ATM strategy. Furthermore, if this tax policy is implemented as proposed, Malawi’s Corporate Tax stands to be the highest in the SADC region which will ultimately push investors to other countries with more favourable policies. Government should therefore reconsider this tax policy measure by removing it in its entirety.

6. Proposals for further consideration

The Confederation appreciates government for considering some of its proposals in the 2024-2025 fiscal budget. It is again the Confederation’s considered hope that Government will reconsider the proposals that were submitted by the Confederation as these proposals are crucial in achieving the government’s agenda of achieving economic recovery and resilience. The following are some of the proposals which the Confederation would like the government to reconsider:

6.1 Manufacturing sector

1. Government should come up with a Special Purpose Vehicle (SPV) or an Industrial Development Fund in the 2024/25 budget to provide patient capital specifically targeting investments in the manufacturing sector. This will help to combat the unavailability of finance which is affecting investment and enhance development of the manufacturing sector which is one of the sectors that has so much potential for value addition.

2. Differential rates should apply to local fruit wine vis à vis imported wines. The Excise Rate on local fruit wines should be reduced to 10 percent from the current 95 percent, to encourage the survival of this emerging industry and domestic small scale fruit suppliers who derive their livelihood from this market. The importation of wines should be well monitored and the Excise Rate on imported wines should remain at 95 percent. The confederation is of the view that protecting this emerging industry and domestic small scale fruit suppliers should be considered for their growth. The growth of this industry can even add to the export basket.

6.2 Finance, Banking and Insurance Sector

The Confederation is of the view that a strong and vibrant Financial sector offers investors opportunities to acquire the much-needed finance muscle to embark on several entrepreneurial activities that benefit the country. Therefore, there is need to boost the availability of capital in Malawi through a number of incentives and a regulatory framework.

1. There are currently only 16 companies that are listed on the Malawi Stock Exchange (MSE) since its establishment in 1994. This places MSE as one of the smallest in the region in terms of number of listed companies. There is a need to incentivize films to enlist on MSE. The Confederation therefore retaliates that a preferential corporate tax of 25 percent should be introduced for a period of up to 3 years upon listing when a company raises new capital for the business i.e., an offer for subscription.

2. A stamp duty revocation notice on secondary trading of shares on the market was communicated during the 2022–2023 budget statement, and subsequently, the revocation notice was later gazetted in the year. This effectively introduced a stamp duty of three percent to be paid by buyers of shares on the securities market. A stamp duty of three percent is inconceivable and could negatively affect businesses in the sector. It also places Malawi as an outlier country with the highest rate of stamp duty on the trading of shares in Africa. The introduction of stamp duty will inhibit secondary trading of shares at a time when the Malawi Stock Exchange is trying to widen its outreach by inviting more public members to participate in the market as one way of reducing the income inequalities that persist between the rich and poor in this country. In addition to the same, the limitation of secondary trading as a result of the introduction of stamp duty will also affect the value-added tax, which is charged on brokerage commissions, hence defeating the whole purpose of tax revenue collection from the market.

   Government should therefore reconsider its position to revoke the stamp duty notice until a time when the market is well developed and has an adequate number of listed companies. The revocation will enable more secondary trading, and government will benefit from tax revenue collection through value-added tax, which is already applicable on the market.

6.3 Construction sector

The Confederation understands that the need for high-standard infrastructure can never be overstated, especially at a time when the country is going through a period of natural disasters. Currently, the industry is facing a number of challenges, including rising costs of building materials, scarcity of forex and a tough regulatory framework. Government should thus revise downwards the 10 percent withholding tax to four percent for contractors and subcontractors in the building and construction industries. The increase from four percent to 10 percent in the 2023–24 budget had a negative impact on the sector. Businesses in the sector operate on stringent margins, and the increase has affected work delivery.

6.4 ICT Sector

The cost of telecommunications in Malawi continues to be high. This increases the provision of data services in Malawi, as it is not claimed by all service providers who offer data services but is passed on to customers. This can be attributed to taxes in the sector, among many other factors.

1. To improve the sector, government should reconsider the taxes by revising the following taxes downward:
    - ❖ 15 percent Non-resident tax charged on the Internet.
    - ❖ 10 percent excise tax charged on data services

7. Conclusion

In conclusion, the Confederation once again applauds government on the identification of the three anchor sectors, namely: Agriculture, Tourism, and Mining, commonly referred to as ATM. These sectors have the potential to boost productivity and export capacity. However, the confederation suggests that manufacturing should also be added to the priority industry list due to its potential to contribute to our import substitution goals.

Furthermore, the Confederation commends all incentives that have been included in the budget that aim to increase import substitution by imposing import duty, surcharge, and a reduction of excise tax on clear beer made from sorghum and maize from 40 percent to 20 percent. On the negative side, some tax policy measures will discourage investment in the country, especially for big investors. The confederation would like to see more incentives for the manufacturing industry that will help in its development. The Confederation therefore urges government to consider further the proposals highlighted in this response to the National Budget.

The Confederation understands that the current economic period is as hard for government as it is for the private sector. The series of shocks have affected businesses and the whole economy, as evidenced by unsatisfactory growth since 2020. The shocks have increased the demand for social protection and poverty reduction interventions. The Confederation is particularly concerned that recurrent expenditures will take up at least 92 percent of total revenues, which are projected at K4.55 trillion. The recurrent expenditures are also marginally higher than domestic revenues, which are projected at K3.38 trillion. As much as we need to allocate resources to these social protection and poverty reduction interventions, government should steer clear from becoming a welfare state which puts a heavy weight on welfare at the expense of development endeavors.

Though government has increased the proportion of resources channeled towards development expenditure to 30 percent from 24 percent in the previous allocation, the Confederation is concerned with the budget deficit amounting to K1.43 trillion, which is 7.6 percent of GDP. This deficit will be financed through domestic borrowing amounting to K1.28 trillion, representing 6.0 percent of GDP, and K150 billion in foreign borrowing. Private sector is currently facing challenges in acquiring loanable funds from commercial banks due to the high interest rates. The proposed K1.28 trillion to be financed by domestic borrowing will create a crowding-out effect, thereby restricting private sector growth. Furthermore, the debt burden is already unsustainably high which will affect future development plans.