MALAWI CONFEREDERATION OF CHAMBERS OF COMMERCE AND INDUSTRY POSITION ON FOREIGN EXCHANGE CONTROL MEASURES

BY

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BACKGROUND

Malawi relies heavily on agriculture as the backbone of its economy. The sector contributes nearly 30 percent of Gross Domestic Product (GDP) and accounts for more than 80 percent of export earnings. However, the country faces persistent challenges, including a narrow export base, trade imbalances, and heavy reliance on donor aid. Its key exports—tobacco, tea, and sugar—are highly vulnerable to external shocks, such as fluctuating global prices and climate-related risks. This dependence on a limited range of commodities leaves Malawi significantly exposed to both external and internal vulnerabilities.

Considering these challenges, Malawi needs to double down on its strategic focus to diversify the economy and strengthen the private sector investment climate. The country's development agenda, the Malawi Vision 2063, emphasizes industrialization, urbanization, and agricultural commercialization as central pillars for achieving long-term sustainable and inclusive growth. This further reinforces the need for enablers, including a dynamic and vibrant private sector.

By driving export diversification, promoting industrialization, and attracting foreign direct investment (FDI), the private sector will significantly contribute to the economy. Additionally, fostering value addition by processing raw materials into finished goods will enhance export revenues while generating employment and tax revenues.

However, the private sector is facing a constrained business environment characterized by inadequate infrastructure, weather shocks, limited access to finance, macroeconomic imbalances, and persistent foreign exchange shortages, all of which contribute to rising production costs. The scarcity of foreign currency has indeed been a significant challenge for the private sector in Malawi. According to Reserve Bank of Malawi (RBM) data, Malawi's foreign exchange reserves have been consistently below the recommended three months of import cover, averaging less than two months. This situation has been exacerbated by trade imbalances, with higher import bills and low export earnings. The RBM data highlight that these factors have severely impacted private sector performance, making it difficult for businesses to access the foreign currency needed for importing raw materials and engaging in international transactions

Consequently, businesses reliant on importing essential raw materials, machinery, and fuel face significant challenges. Over 80 percent of businesses have reported access to forex as one of the key challenges in operating leading to operating levels of 50 to 75 percent below optimal levels. Furthermore, the scarcity of foreign exchange has led to delays in processing payments to international suppliers, eroding trust and damaging business relationships therefore increasing the risk index for Malawi.

IMPACT OF FOREIGN CURRENCY SCARCITY ON THE PRIVATE SECTOR

The 2024 Malawi Business Climate Survey revealed that the scarcity of foreign currency and exchange rate volatility were the top challenges, scoring 9.43 out of 10. This highlights the critical nature of foreign exchange issues in facilitating effective business operations. Without access to adequate foreign currency, businesses face operational disruptions and production delays, leading to increased costs and heightened price volatility.

The foreign currency scarcity also disrupted the supply chain of essential commodities, such as fertilizer for the 2024/2025 agricultural season and fuel, particularly petrol and diesel. Fuel shortages severely impacted business operations by delaying the movement of raw materials and finished goods, increasing transportation costs, and hindering workers' mobility.

As a result of these challenges, only 34.8 percent of businesses reported positive performance in 2024, compared to 42 percent in the 2023 survey. Meanwhile, 35 percent of businesses rated their performance as fair, and 29.4 percent indicated poor performance, an increase from the 23 percent recorded in 2023. Additionally, the survey revealed that 82.8 percent of businesses operated with a capacity utilization rate of 75 percent or below, underscoring the significant constraints facing the private sector.

GOVERNMENT INTERVENTIONS

The supply-demand imbalance in the domestic foreign exchange market has manifested in various ways, including low foreign exchange reserves, declining official foreign reserves, and widening spreads between ADBs TT and Bureaux Cash exchange rates. In response to the forex liquidity and pricing challenges, and their effects on exchange rate developments, the Reserve Bank of Malawi (RBM) has instituted several short-term measures to support the importation of strategic commodities. These measures include the introduction of foreign exchange auctions and the reintroduction of the mandatory sale of 30 percent of export proceeds instituted in August 2021, among others.

The reintroduction of the requirement to sell 30 percent of export proceeds mandates that all exporters sell a minimum of 30 percent of their export earnings to Authorized Dealer Banks (ADBs) while retaining no more than 70 percent in their Foreign Currency Denominated Accounts (FCDAs). This measure has reduced the availability of foreign exchange for businesses to import raw materials essential for their operations. Businesses that generate foreign exchange have faced challenges accessing the forex they help generate.

In December 2024, the government introduced a new foreign exchange control regulation that requires public institutions to hold foreign currency reserves at the Reserve Bank of Malawi (RBM) with a mandatory conversion of 80 percent. Additionally, it mandates commercial banks to convert, within 48 hours, 70 percent of NGOs' foreign exchange receipts into Malawi kwacha and immediately transfer the proceeds to the RBM. This measure aims to ensure the availability of forex for strategic purchases, such as fuel imports, and to reduce the proliferation of forex to the parallel market.

MCCCI POSITION ON THE NEW FOREIGN EXCHANGE CONTROL MEASURES

The Confederation has noted with concern that, in addition to the mandatory requirement for all exporters to sell 30 percent of their export proceeds, the government has introduced the Foreign Exchange Control (2024) regulation. This regulation is likely to have negative implications for the private sector's access to foreign currency and the economy. While these policy measures demonstrate the government's acknowledgment of the challenges, their implementation is likely to result in unintended negative consequences, including a further decline in exports and, consequently, reduced foreign currency inflows. These measures could also disrupt the planning and implementation of projects by NGOs, particularly in the volatile environment the country is currently facing. This may discourage regional NGOs from carrying out their projects in Malawi, as the risk of foreign exchange losses would render Malawi a high-risk country.

Although the measures aim to curb illegal forex trading, they fail to address how businesses will access foreign exchange once it is directed to the Reserve Bank of Malawi (RBM). The principles being promoted contradict policies of a market economy and would likely increase the perception of instability in the policy regime and discourage investments. The Confederation believes that the Exchange Rate (Repatriation of Exports Proceeds and Operations of Foreign Currency Denominated Accounts) Regulations of 2022 are sufficient to curb illegal forex activities, and efforts should instead focus on ensuring compliance with these regulations.

The Confederation is of the view that addressing forex scarcity requires a forward-looking approach that focuses on boosting export diversification and enhancing local production capacity for import substitution. However, these proposed changes will likely create the desire to hedge further, promoting parallel trading, which will result in the escalation of parallel rates, continuing to fuel increases in production costs and price instability for basic goods and services. This trend is likely to enhance speculation and motivation to declare Malawi as a country operating in a hyperinflationary status, further impacting its attractiveness as an investment destination.

The Confederation urges the government to maintain the role of the RBM as the regulator and enable commercial banks to continue operating as expected whilst prioritizing the allocation of the available foreign exchange to productive sectors, which can generate additional forex and thereby support both the private sector and the broader economy.

Furthermore, given the limited availability of forex, the Confederation encourages the government to implement measures that prioritize export-driven industries, as they have the potential to generate more forex, which is vital for economic stability. To achieve the intended goals of fostering adherence to existing regulations and curbing illegal activities, the government should engage banks and other stakeholders in the sector for consultation.

CALL FOR ACTION

The Confederation urges the government to reconsider its approach to foreign exchange and adopt holistic measures that prioritize the private sector as a critical driver of economic growth. Policies should focus on enhancing forex availability for businesses, improving infrastructure, and fostering a competitive and sustainable business environment. Addressing these challenges is essential to strengthening the private sector's resilience and unlocking Malawi's economic potential.

Additionally, the government should strengthen existing regulatory frameworks and enforcement mechanisms to combat illicit currency trading, with adequate penalties to deter participation in the parallel market. Collaboration with financial institutions to increase forex availability for the private sector is vital, especially for prioritizing essential imports and businesses with export potential. Lastly, fostering public confidence in the banking system by ensuring stability, transparency, and accessibility to foreign currency will help shift demand from the parallel market to formal channels, effectively curbing its prevalence. The confederation therefore calls for urgent and immediate dialogue mechanism to identify workable solution to stimulate private sector investment in strategic value chains.