



RESERVE BANK OF MALAWI

**MICROFINANCE AND CAPITAL
MARKETS FINANCIAL SECTOR
REPORT 2010**

**MICROFINANCE AND CAPITAL MARKETS
SUPERVISION DEPARTMENT**

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1.0 LETTER TO THE MINISTER OF FINANCE



RESERVE BANK OF MALAWI

GOVERNOR'S OFFICE

TEL: (265) 1 770 600

FAX: (265) 1 773 142/ 772 752

WEBSITE: <http://www.rbm.mw>

EMAIL: reserve-bank@rbm.mw

**CONVENTION DRIVE
RESERVE BANK OF MALAWI
P O BOX 30063
LILONGWE
MALAWI**

06 December 2011

Honourable Ken Lipenga
Minister of Finance
Private Bag 30049
Capital City
LILONGWE 3

Microfinance and Capital Markets Financial Sector Report 2010

I have the honour to submit to you the Microfinance and Capital Markets Financial Sector Report in regard to the regulation and supervision of capital markets and microfinance businesses in Malawi during the year ended 31 December 2010 in accordance with the provisions of the Financial Services Act, 2010.

Yours Sincerely

Dr Perks M Ligoya

REGISTRAR OF FINANCIAL INSTITUTIONS

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2.0 REGISTRAR'S FOREWORD

I am pleased to present the 2010 annual report of the Microfinance and Capital Markets Supervision Department, which highlights the developments in the microfinance industry and performance of the capital markets sector in Malawi in the year ended 31st December 2010. This is a new department that has been recently formed following the restructuring of the Non Bank Financial Institutions department in July of the year under review into: Microfinance and Capital Markets Supervision Department, and Pensions and Insurance Supervision Department. The Department is responsible for licensing, regulating and supervising operators in microfinance, fund managers and stock brokers and investment advisors.

The microfinance industry continued to operate under a weak regulatory environment as a good number of microfinance institutions were conducting their business un-supervised. Despite the fact that the Financial Services Act and the Microfinance Act were promulgated in 2010; regulations and directives to support the Acts were still in draft form as at 31st December, 2010. It is expected that these subsidiary laws will be gazetted and may come into effect in the course of the coming year. The microfinance industry will be categorised into Deposit Taking Microfinance Institutions, Non-Deposit Taking Microfinance Institutions, Microcredit Lenders and Financial Cooperatives. It can be said that although unsupervised, the country has seen an increase in the number of operators in the microfinance industry in 2010 and expects to see more in the coming year.

On the capital markets front, the stock market experienced stagnancy due to the uncertainty that arose from the global financial crisis. Trading on the Malawi bourse saw a decrease in volume of 59.1 percent and 33.6 percent in terms of value. Other intermediaries were no exception and were similarly negatively affected by the crisis. There were no new listings on the Malawi Stock Exchange (MSE).

In terms of policy, consultations and drafting of the Microfinance Bill was completed and was later endorsed by Cabinet and passed by Parliament. As at 31st December, the final drafting of the Financial Cooperatives Bill was done.

Apart from the strides made on the Bills, a new directive on Securities (Establishment and Operation of Collective Investment Schemes) was introduced. The directive will ensure that collective investment schemes (CIS) comply with provisions of the Securities Act; protect the interests of the public and investors; and ensure maintenance of professional standards in the management of CIS. In the course of the year drafting of other directives for capital markets and microfinance entities commenced.

In a related development I am also pleased to report that during the year, the Reserve Bank established a Consumer Education and Complaints Handling Unit. This Unit will be responsible for consumer empowerment and market conduct for the entire financial services industry. This in turn should improve transparency in the industry, lead to better pricing of products and help consumers of financial products make better informed decisions. I trust that you will find the information contained in this report useful.

3.0 ECONOMIC OVERVIEW¹

Real gross domestic product (GDP) grew by 6.7 percent, compared to a growth rate of 8.9 percent in 2009. The deceleration in growth is attributed to a slowdown in agricultural activity to 2.0 percent in 2010 from 13.9 percent in 2009 caused by a dry spell that some parts of the country experienced. However, the effects of the slowdown in agriculture were partly offset by significant aggregate expansion in mining, manufacturing, financial activities and wholesale and retail trade activities. Tobacco production in 2010 declined by 10.6 percent to 220.2 million kilograms due to relatively lower prices fetched in 2009. Correspondingly sales declined by 5.0 percent in 2010. Average tobacco prices rose by 1.0 percent to US\$1.89/kg on account of reduced supply of the leaf. Hence, total tobacco proceeds increased by 4.1 percent to US\$416.4 million in 2010.

The manufacturing sector grew by 4.3 percent. The increase in production was on account of scaling up of sugar production capacity at Dwangwa and Nchalo and the “Buy Malawian Campaign” that has increased demand for the locally manufactured goods on the market. Mining and quarrying grew by 80.2 percent in the review year compared to 4.9 percent in 2009. The impressive performance is attributed to increased production at Kayelekera uranium mine. Growth for this sector is projected at 33.1 percent in 2011 as fuel supply outages may adversely affect the operations in this highly energy dependant sector.

The Construction industry grew at 16.5 percent compared to 7.4 percent in 2009. The expansion is a result of major construction of hotels across the country, construction of roads and private construction of up market houses in the major cities. The information and communication sector registered growth of 9.2 percent in 2010 compared to 10.5 percent in 2009. This was explained by the massive promotions and marketing by the mobile phone companies and a new mobile service provider, Access Communications Limited.

The financial services industry grew by 10.6 percent in 2010 against recorded growth of 7.8 percent in 2009. This growth was attributed to expansion in branch networks across the country and introduction of new products such as mobile banking, and internationally accepted visa cards. Enactment of the Microfinance legislation and implementation of the financial sector strategic plan are expected to contribute towards the industry’s projected growth of 9.2 percent in 2011.

¹ Mainly derived from the Reserve Bank of Malawi Report and Accounts for the year ended 31st December 2010

Monetary developments during the review year were expansionary as money supply rose by K30.8 billion (17.8 percent) to K203.9 billion in 2010. The growth in money supply was buoyed by successful implementation of the first review of the Extended Credit Facility (ECF) arrangement with the International Monetary Fund and subdued inflationary pressures which allowed the Monetary Policy Committee to adopt an easier monetary policy stance in the course of 2010. Credit to the private sector accelerated by K26.6 billion which was almost equivalent to the increase recorded in 2009 albeit the August 2010 downward adjustment in interest rates. The delayed and slow adjustment of bank credit to more accommodative monetary policy was hampered by the already high level of debt. The expansionary effect was however partly counteracted by a K20.4 billion reduction of Government's indebtedness following foreign inflows catalysed by the ECF review as well as a net recovery of K1.6 billion in statutory corporations' loans to the banking system.

Central government operations for the year 2010 resulted into a fiscal surplus after grants of K13.2 billion compared to a deficit after grants of K36.5 billion in 2009. This improvement was attributed to increases in domestic revenues and foreign grants that outpaced the increases in expenditure. Total government revenues increased remarkably by K98.3 billion (49.7 percent) to K296.1 billion in the year under review. Government used the surplus for repaying part of its domestic debt up to K30.4 billion. Government repaid foreign loans up to K2.2 billion in 2010 compared to K1.0 billion in 2009. However foreign borrowing rose to K17.0 billion from K3.1 billion recorded during the preceding year.

Annual headline inflation in 2010 decelerated by 1.0 percent from 8.4 percent in 2009, led by a deceleration in food inflation to 5.0 percent from 7.3 percent in 2009. On the other hand, non-food inflation rose to 9.9 percent from an average of 9.6 percent in 2009 due to increase in transportation costs following a fuel pump price hike in February 2010 and an increase in housing costs.

During the year 2010 there was an expansion of capital market operations. However, the intermediary business remained stagnant following uncertainty that arose due to the global financial crisis. The insurance industry assets increased by 21.3 percent totalling K82.5 billion in assets whilst the banking sector grew by 21.6 percent with total assets at K282.4 billion.

The year under review saw the enactment of several financial laws. The Financial Services Act, Banking Act, the Credit Reference Bureau (CRB) Act, the Securities Act, the Microfinance Act and Insurance Act were enacted by Parliament in 2010. Draft laws governing operations of SACCOs and pensions were finalised and presented to Cabinet for approval and onward

submission to Parliament. These laws are expected to enhance growth and stability in the financial system. However, economic challenges are expected to revolve around the global crisis through less financing to local firms and depressed commodity prices for Malawi's exports.

The general improvement in the country's macroeconomic condition has been instrumental to improvements in many of the sectors that contribute to the country's GDP. However, the global financial crisis has been a constant offsetting factor to Malawi's economic growth leading to reduced and intermittent donor aid and stagnation of some of the country's industries. Despite this, as well as fuel and foreign exchange shortages, the country is still expected to make headway in the next economic year.

4.0 MISSION STATEMENT

The Microfinance and Capital Markets Supervision (MCSU) Department of Reserve Bank of Malawi (RBM) has an overall mission of *ensuring the existence of a fair, safe, sound and stable microfinance and capital markets in Malawi in line with international supervisory standards.*

In pursuance of the mission statement outlined above, the department will perform its work with professionalism, integrity, impartiality, and in a friendly and cooperative manner but without compromising its authority or mandate.

The department has the following core strategic objectives representing essential elements of the mission statement:

- a) ensuring the existence of an all inclusive and regulated microfinance and capital market sectors;
- b) developing the microfinance and capital market sectors and enhancing stakeholder confidence in the microfinance and capital markets services in order to broaden and deepen the market;
- c) safeguarding depositors, and investors from undue loss;
- d) fostering a competitive, cost effective environment in the microfinance and capital markets through provision of prudential directives and regulations; and
- e) providing quality, professional supervisory and regulatory service.

In conformity with internationally accepted supervisory standards, this report is compiled in partial fulfilment of these objectives and aimed at informing the public on the overall outlook of the performance of the microfinance and capital markets in Malawi for the year ended 31st December 2010. The report gives a summary of activities of the Department in terms of its regulatory responsibilities by providing a synopsis of the year's accomplishments and a variety of financial information on the state of the microfinance and capital markets sectors in Malawi.

The department has six key result areas namely; Entry control, On-going supervision, Policy development, Enhancement of competition, Consumer education and protection and Exit administration (See appendix for departmental structure).

5.0 CAPITAL MARKETS

5.1 Industry Overview

The capital market plays an important role in promoting the development of the private sector and creating new investment opportunities in the economy. The market offers an alternative source of capital funding to companies and facilitates financing of public investments.

The general improvement in the country's macroeconomic condition has been instrumental in spearheading the expansion of capital market operations. However, during the year, the intermediary business remained stagnant following uncertainty that arose due to the global financial crisis.

Looking ahead, the pension sector reforms are expected to further boost the capital market activities.

5.2 Market structure

5.2.1 The Reserve Bank of Malawi

The Reserve Bank of Malawi is a quasi-government authority responsible for the regulation and supervision of capital markets under the Securities Act of 2010. It is the primary authority responsible for licensing all capital market entities, supervising their activities, providing guidelines on market conduct and promoting the development of capital markets in Malawi.

5.2.2 The Malawi Stock Exchange (MSE)

The MSE, a limited company guaranteed by the Reserve Bank of Malawi, is responsible for operating the stock exchange. It also governs the market conduct aspect of its registered members (brokers and dealers) as a self regulating organisation (SRO).

As at year end 2010, the total number of listed companies on the Stock Exchange stood at fifteen (See Chart 1), fourteen of which are domestic and one is foreign and dual listed. There was no new listing during the year under review.

Trading at the MSE is done manually. However, in May 2010, the MSE introduced on pilot basis a Central Order System, a web based system which requires brokers to place their orders ahead of the call over session. The orders are placed on a portal on the MSE website. The system allows only placed orders to be executed in the dealing session. Only the MSE has rights to access all the orders in the system.

On 22nd September 2010, the MSE temporarily suspended trading in TNM shares following corporate action within the company. The suspension was lifted a week later after the company clarified negotiations that were taking place.

During the year ended 2010, NBS Bank issued bonus shares to its members in the ratio of 1 ordinary share for 18 ordinary shares held as at 24th December 2010. The additional bonus shares added to 26,191,909 and were listed on the exchange on 4th January, 2011.

5.2.3 Market Intermediaries

These comprise portfolio/asset managers, stock brokerage firms, collective investment schemes and investment trusts operating on the capital market. Their duty is to facilitate transfer of funds from surplus units to deficit units on the capital market (see appendices for list of all market intermediaries).

5.3 Regulation and Supervision

5.3.1 Statutory Powers

During the year under review, the Financial Services Act (FSA), 2010 and the Securities Act 2010 were promulgated. Under the new legislation, the Governor of the Reserve Bank of Malawi is appointed Registrar of Financial Institutions and is responsible for the regulation and supervision of the capital markets. The FSA and the Securities Act specifically mandates the Reserve Bank of Malawi as a primary authority, to license market participants, supervise their activities, grant approval for offering of securities, promote internal and external confidence in the integrity and proper functioning of the capital and securities markets, provide guidelines on market conduct and promote the development of the capital market in Malawi (See Box A: Main Provisions of the Securities Act, 2010). The Securities Act, 2010 repealed the Capital Market Development Act (CMDA), 1990. Directives promulgated by the Bank under the Securities Act are gazetted prior to coming into effect. Apart from the Securities (Establishment and Operation of Collective Investment Schemes) Directive 2010, which was gazetted during the year, the following drafts were submitted for gazetting as at end December 2010.

- Securities Act (Operation of Brokers/ Dealers) Directive
- Securities Act (Investment Advisors) Directive
- Securities Act (Transfer Secretaries) Directive
- Securities Act (Securities Representative) Directive
- Securities Act (Portfolio Managers) Directive

The objective of Securities Act (Establishment and Operation of Collective Investment Schemes) Directive is to ensure that collective investment schemes comply with the provisions of the Securities Act; protect the interests of investors and the public interest in general; and ensure maintenance of professional standards in the management of collective investment schemes.

Box A: Main Provisions of the Securities Act, 2010

The Securities Act, 2010, repeals the Capital Market Development Act (CMDA) and introduces new legislation that has adapted the developments that have occurred in the capital market sector in Malawi over the years. The main objection of the Act is to provide for the regulation of capital and securities markets, persons transacting business thereto, and the conduct of capital and securities markets in Malawi.

The Act gives the Registrar, who is the Governor of the Reserve Bank of Malawi, powers to ensure that the Act is complied with. It further gives the Registrar powers to license and supervise the activities of stock exchanges, brokers, dealers, investment advisers, portfolio managers, collective investment schemes and securities market intermediaries and their respective securities representatives and to direct the licensing of depositories. Carrying on business as any of the above without a license is prohibited, and amounts to an offence. In addition, the Registrar may issue directives necessary for the implementation of the Act.

Persons seeking to establish and operate a stock exchange should make an application in writing in accordance with the provisions of the Financial Services Act. The application will be accompanied by a fee specified by the Registrar. Management of the stock exchange shall comprise of a board whose members shall be elected in accordance with the articles of association of the stock exchange. The Registrar may issue directives to a stock exchange where it deems necessary and may order its closure, after consultation with the Minister of Finance. The stock exchange shall work in liaison with the Registrar in order to protect the interests of investors and for the fair administration of the activities of the stock exchange.

An applicant for a license to operate as a broker, dealer, investment advisor, portfolio manager or a securities representative and securities market intermediary shall send an application form, accompanied by a fee, to the Registrar. The Registrar may refuse to grant, revoke or suspend a license if an applicant or holder provides insufficient information or is not operating in accordance with the provisions of the Act. Licensees are required to maintain accounting records and records of securities in their beneficial ownership and to supply the Registrar with information on the same.

Securities of companies listed on the stock exchange are to be registered with the Registrar, by submitting a registration statement accompanied by a prospectus and prescribed fee. The content of the registration statement may be specified by the Registrar by way of written notice or directive. Issuers of securities shall keep the public well informed at all times, of matters which affect the value of the securities.

Pertaining to the conduct of securities business, every licensee and any other person licensed under the Act, shall effect transactions only in compliance with it, and no trading shall take place outside the stock exchange. They are required to maintain at all times such capital, liquid assets and reserves in the manner and amounts that the Registrar specifies. All persons who might have an interest in or be part of the activity in the trading of any securities are prohibited from false trading and manipulations, use of deceptive statements, fraudulent activities, giving misleading statements and insider trading. Penalties are in order for anyone who contravenes the sections that provide for the above prohibitions.

A Securities Stabilisation Fund shall be established which shall consist of monies recovered from penalties and all other monies accruing thereto. The purpose of the fund is to compensate persons who suffer loss as a result of default by licensees. Subsequently a Stabilisation Fund Committee will be established and will be responsible for the administration and operation of the stabilisation fund as regards settlement of claims made against it, however with liability limited to such amount as the Registrar may issue. The committee's membership composition is stated in the Act.

5.3.2 Entry Control/Licensing

There were no new entrants during the year under review. However, one operator has made an application for a Collective Investment Scheme licence (Unit Trust) as at end December 2010.

5.4 Supervision Methodology

5.4.1 Off-site Supervision

As a continuous licence operating requirement, all licensed capital market entities are required to prepare and timely submit prudential returns to the Bank on a quarterly basis and audited financial statements annually. The returns aid in surveillance of the reporting institutions and the industry as a whole in order to ensure safety and financial soundness of the institutions as well as the industry. Timely submission of these returns assists the regulator to quickly identify lapses and weaknesses in the operations of the institutions and appropriately effect corrective action. Essentially the effectiveness of off-site surveillance largely depends on the quality and timeliness of financial information submitted by the institutions.

During the year 2010, a small number of registered capital market professionals did not timely submit quarterly returns compared to the year 2009. As a way of encouraging compliance the new directives provide for penalties in case of late submission of returns.

5.4.2 On-site Inspections

In line with Section 4 of the Securities Act of 2010, three routine inspections were conducted at Stock Brokerage firms during the year ended December 2010. The focus of the on-site examinations was to assess the overall financial condition of the institutions, capital adequacy, effectiveness of internal control systems and Management Information Systems and to evaluate the institution's compliance with prevailing rules, regulations and requirements under the Securities Act, 2010. The findings were generally satisfactory with some deficiencies that were later addressed.

5.5 Exit Administration

No exits were administered in the market during the year under review. However, two stockbrokerage firms were on a liquidity watch list due to under capitalization, which could result in withdrawal of their current licence and further denial of the 2011 licence renewal application should the shareholders fail to recapitalize the institutions within the given deadline.

5.6 International Relations

5.6.1 International Organisation of Securities Commission (IOSCO)

IOSCO is an international standard setting body for the securities market. The Reserve Bank of Malawi is a signatory to Appendix B of IOSCO Multilateral Memorandum of Understanding (MMOU). During the year under review, the Reserve Bank of Malawi was working towards application to become a signatory under Appendix A of the IOSCO MMOU. It is envisaged that the Bank will benefit by being a member of the international network as this would assist in effective prevention of cross-border securities market breaches and market fraud.

5.6.2 Committee of Insurance, Securities and Non-Banking Financial Authorities (CISNA)

At regional level, the Bank is an active member of CISNA which is a regional grouping of insurance and capital market supervisors. Its main objectives are to enhance regulatory capacity and harmonise regulations and regulatory processes in the non bank financial sector of the Southern Africa Development Community (SADC).

During the year under review, the Reserve Bank of Malawi participated at bi-annual meetings which were held in Mozambique and Lesotho during April and December 2010, respectively. The main issues discussed at the forum included deliberations on consideration for regulation of unregulated entities in particular Credit Rating Agencies (CRAs); developments of collective investment schemes, regulation of secondary markets; regulation of market intermediaries and enforcement and exchange of information. The Lesotho meeting focused on review of Strategic Direction of CISNA from 2011 to 2015.

5.7 Performance of the Stock Market

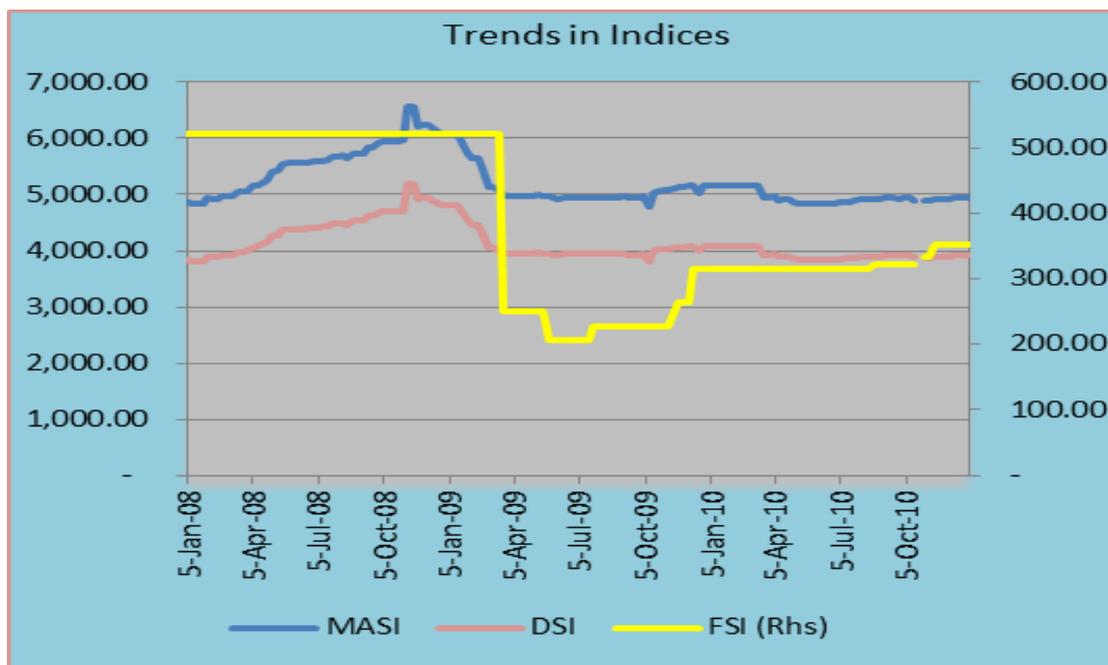
5.7.1 Stock Market Trading

The stock market remained in the doldrums following failure to fully recover from the effects of the global financial crisis. The Malawi Stock Exchange registered 242.2 million shares traded at a total turnover of K1, 911.8 million (US\$12.7 million) in 1561 deals compared to 592.4 million shares at a total turnover of K2, 877.6 million (US\$20.3 million) in 1795 deals in the previous year. This reflects a decrease in volume by 59.1 percent and 33.6 percent in terms of value.

The Malawi All Share Index (MASI), the barometer that measures the average price movement of all counters at the Exchange, declined by 3.9 percent to close off the year at 4,953.09 points from 5,154.95 points recorded in the previous period. The dismal performance was attributed to a decrease in the Domestic Share Index (DSI) which lost 4.03 percent from 4,087.19 points to 3,922.61 points during the period under review (See Chart 1). However, the Foreign Share Index (FSI) gained 12.0 percent during the review period from 314.21 points to 351.92 points.

The total market capitalization² closed off higher at K1, 278.5 billion (US\$8,478.11 million) from K1, 172.1 billion (US\$8,028.92 million) generally due to an increase in the share prices of MPICO and OML (a foreign dual listed company). In the corresponding year, the market capitalization stood at K1, 838.3 billion.

Chart 1: Malawi Stock Exchange Indices Trend

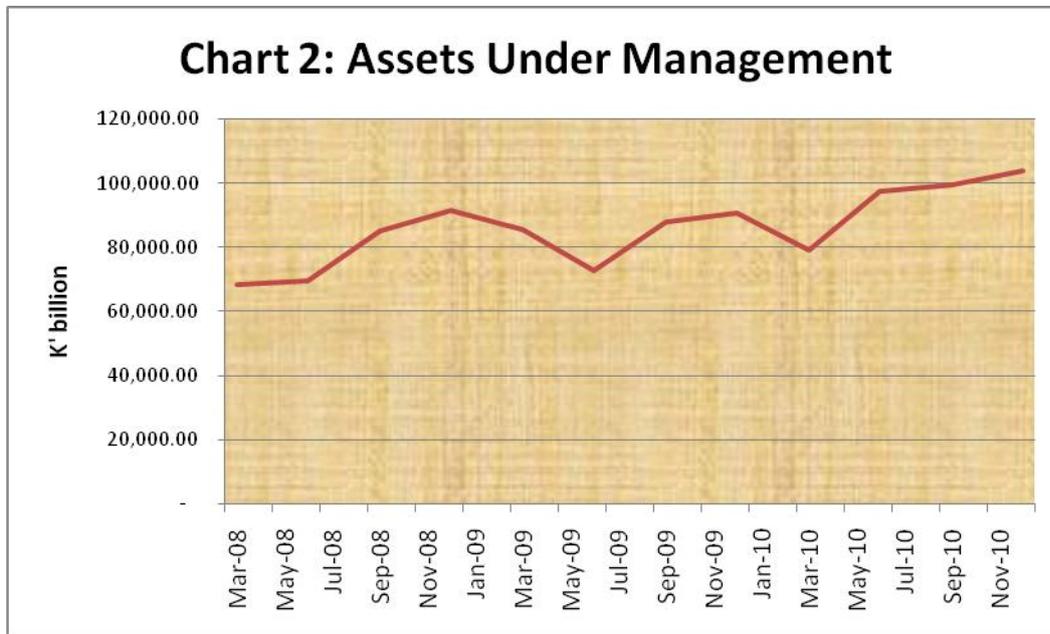


² Includes Old Mutual Plc shares

5.7.2 Fund Managers Operations

During the period under review, total assets under management stood at K103.8 billion compared to K93.9 billion as at end of December 2009 (See Chart 2 below).

Chart 2: Assets under Management



Overall, pension funds and life insurance companies remained the major sources of the funds under management each contributing 53.9 percent and 23.3 percent of the total funds respectively (See Table 1 below).

Table 1: Sources of Investment Funds

Category	Dec-09 (MK'bn)	Percentage of total funds	Dec-10 (MK'bn)	Percentage of total funds
Pension funds	48,289.57	51.4	24,014.12	23.3
General/Non Life Insurance Cos (Short term)	2,280.50	2.4	2,780.16	2.7
Life Insurance Companies (Long term)	22,950.77	24.4	55,581.98	53.9
Unit Trust Schemes	3,619.61	3.9	1,260.57	1.2
Companies	12,272.66	13.1	9,365.54	9.0
Other	4,524.08	4.8	10,190.67	9.9
Total	93,937.48	100	103,193.04	100

5.8 Future Plans

In view of regulatory developments and in particular pension sector reforms, it is anticipated that following the introduction of mandatory pension schemes in the country, fund managers acting on behalf of the pension funds will stimulate demand for long term instruments on the market in search of competitive returns. This is also expected to drive the introduction of more long term financial instruments.

On an international level, there continues to be uncertainties about the future shape of the global financial markets and the opportunities and challenges they present for sustainable global economic growth. The debt crisis in Europe, rising commodity and oil prices, and slow recovery across the globe continue to be a challenge for global financial markets. As a country, it is expected that Malawi will pursue sound regulatory approaches including adoption of international principles of securities regulation including the introduction of risk based supervision in order to play a significant role in promoting the country's growth.

6.0 MICROFINANCE

6.1 Industry Overview

The microfinance industry continued to operate under four different arrays of legislative instruments, namely the Banking, Trustees Incorporation, Cooperative Societies, and Companies Acts. This regulatory environment continued to create unlevel playing field to the different categories of microfinance services providers (MSPs). Banks with microfinance operations remained the only category subject to prudential supervision since they offer savings deposit services. The savings and credit cooperatives (SACCOs) were largely supervised by the Malawi Union of Savings and Credit Cooperatives (MUSCCO). The other categories of MSPs remained unsupervised.

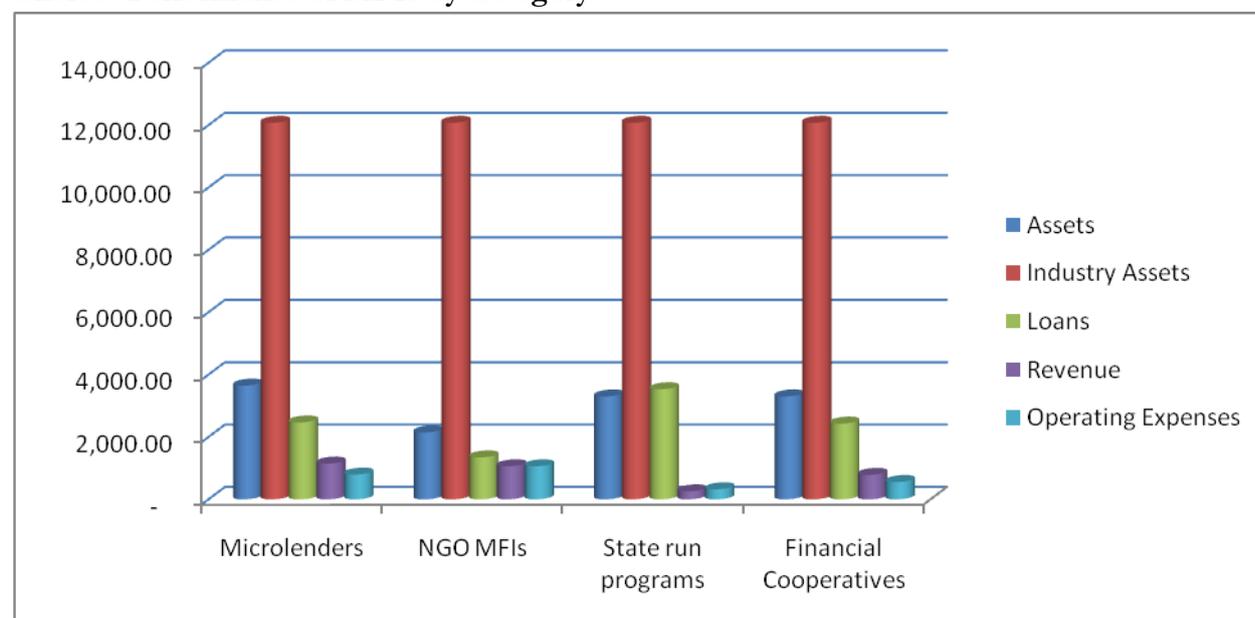
The microfinance industry was characterised by government-run programs, non-governmental organizations (NGO), private moneylenders, banks, and cooperatives in the year under review. The government-run programs regained dominance of the loan market share as the moneylenders slowed lending on account of Government's decision to stop effecting loan deductions from its payroll in 2009. The moneylenders largely offer payroll-based loan facilities to low and medium-income employees. Banks, on the other hand, also continued to explore channels to downscale to the bottom of the pyramid. One of the channels was wholesale credit to MFIs which, in turn, on-lend to clients. Two banks, namely Opportunity International Bank of Malawi (OIBM) and Malawi Savings Bank (MSB), maintained their grip in loan market share by directly offering financial services to the clients. The rest of the banks however limited their downscale to serving largely registered small and medium enterprises. Lastly, member-based financial SACCOs played a pivotal role in mobilizing share capital and savings deposits to members.

6.2 Industry Performance

The microfinance industry registered a total of MK12,073.9 million in assets. Out of these assets, about MK11,965.4 million was in form of outstanding loans. The outstanding loan portfolio represented a sharp decrease of 11.5 percent on the previous year's figure. The decrease was a result of the private moneylenders stand to slow down disbursement of new loan facilities in the wake of the Government's decision to stop effecting loan deductions from its payroll in 2009. Accordingly, the number of loans disbursed in the year under review reduced by 11.2 percent and closed at 892,598.

Table 2: Loan Market Share by Category (2010-2009)

Category	2010	2009	%(+)/(-) in loan share
Moneylenders	21%	33%	-36%
State-owned Programs	30%	29%	+3%
NGO-MFIs	11%	8%	+38%
Banks	18%	14%	+29%
Cooperatives	20%	16%	+25%

Chart 3: Performance of MFIs by Category

6.2.1 Moneylenders

Payroll-based money lending targets salaried employees who are largely civil servants. The total loans outstanding closed the year at MK2, 466.0 million from MK4,340.2 million recorded in 2009, representing a year-on-year decrease of 43.0 percent. As explained above, the sharp decrease is attributed to Government's stand to stop effecting loan deductions on its payroll on behalf of money lenders. The money lenders therefore reduced lending while seeking alternative means of loan collection. This means that the moneylenders lost grip of loan market share from 33.0 percent in the previous reporting period to 25.0 percent in 2010. This represents a decrease of 36 percent in loan market share (refer to Table 2 above).

In terms of revenue, the money lenders reported a total of MK1,146.9 million, (Chart 3) representing 35.0 percent of total industry revenue.

The operating expenses for the money lenders increased in 2010 from an average MK284.5 million to MK488.1 million. The operating expenses shot up largely due to high costs on loan recovery. The sharp increase in operating costs, coupled with reduced lending, led to reduced profitability for money-lenders. The profits for the moneylenders were also dampened by non-performing loans which averaged MK358.9 million, representing 14.6 percent of loans outstanding.

6.2.2 NGO - Microfinance Institutions

The NGO-microfinance institutions continued to provide loans using a combination of methodologies including group lending, individual lending, village banking, and self-help groups. Their operations continued to rely on largely donor support in form of loans with soft terms and grants. However, most NGO-microfinance institutions are complimenting donor support with loans from banks.

As at close of 2010, the NGO-microfinance institutions reported a total of MK1,345.8 million in outstanding loans from MK1,075.20 million in the previous year, representing 25.0 percent increase. The loans outstanding in 2010 represented 11.0 percent of the loan market share, up from 8.0 percent in the preceding year, representing an increase of 38 percent (Table 2). The NGO-MFIs steadily increased their loan market share in the year. These institutions continued to enjoy donor support in capacity building in form of provision of loan funds, information technology and financial management. Notwithstanding the remarkable increasing trend in loans outstanding, operating expenses registered an increase of 5.0 percent and closed the year at an average of MK222.6 million. The slow increase in operating expenses can be explained by the use of appropriate lending technologies by the NGO-MFIs.

Overall, the NGO-MFIs reported an average net profit of MK12.5 million in the year under review. Adjusting the profits to cost of funds and inflation reverses the profit outcome. This category also reported a non-performing loan amounting to MK63.2 million, translating into 4.7 percent of outstanding loans.

6.2.3 Banks with Microfinance Window

Opportunity International Bank of Malawi (OIBM), and Malawi Savings Bank (MSB) remained the only banks with microfinance component in their operations in the year under review. The

other banks only provided wholesale loans to other MFIs for on-lending. OIBM continued to establish a firm grip in microfinance with its microfinance portfolio accounting for 40.0 percent of its total loans portfolio of MK4,739.3 million in 2010. MSB, on the other hand, recorded about MK296.2 million in microloans, representing 2.0 percent of its total portfolio. The bulk of these microloans were seasonal loans disbursed to farmers. Overall, the bank microfinance loan operations went up by 25.0 percent and closed the year under review at 20.0 percent of loan market share (Table 2).

6.2.4 State-owned and Government Programs

During the year under review, state-owned or government programs remained active in issuing new loans. Malawi Rural Development Fund (MARDEF), and Malawi Rural Finance Company (MRFC) together accounted for MK3,531.5 million, MK316.0 million or 8.2 percent lower on the previous amount, in outstanding loans in the year under review. This outturn meant that Government intervention in the industry remained dominant with a loan market share of 30.0 percent, representing a marginal increase of 3.0 percent on the preceding year (Table 2). The assets in 2011 are expected to increase due to the commencement of loans disbursements under the program.

6.2.5 SACCOs

SACCOs are institutions registered under Cooperative Societies Act, 2000 to accept deposits, advance loans and provide other financial services to its members. During the year under review, the total number of active SACCOS affiliated to Malawi Union of Savings and Credit Cooperatives (MUSCCO) remained constant at forty five (45). Nine (9) cooperative affiliates remained dormant. Membership, however, registered a year-on-year increase of 24.5 percent and closed at 113, 884 members. Financial Cooperative Malawi Limited (FINCOOP) remains the largest cooperative affiliate accounting for 34.2 percent of the movement.

	2004	2005	2006	2007	2008	2009	2010
Assets	736.78	935.88	1,064.35	1,476.81	2,295.81	2,610.02	3,302.58
Loans	470.87	595.17	710.73	1,036.69	1,826.29	2,021.41	2,430.19
Savings	53.40	61.23	76.70	111.57	163.97	159.66	215.13
Shares	535.75	650.67	810.68	1,090.61	1,577.83	1,818.87	2,196.18

Income	205.71	232.94	276.83	373.92	485.89	505.87	785.92
Expenses	131.66	168.96	172.36	235.89	317.09	295.23	566.05
Surplus	56.55	39.04	93.97	125.16	144.36	175.28	164.19

Total assets of MUSCCO affiliates grew by 26.5 percent from MK2, 610.9 million recorded in 2009 to MK3, 302.6 million in 2010 (refer to Table 3). The growth in assets was largely due to the increase in loans by MK408.8 million or 20.2 percent as at December 2010. The loans outstanding closed the year at MK2, 430.2 million, constituting 73.5 percent of total assets. Despite the growth in membership and loan portfolio, the cooperative affiliates' loan delinquency level dropped to 2.0 or MK51.2 million in 2010 from 3.0 percent or MK58.6 million reported in the previous year. The movement continued to increase its grip on lending market having registered outstanding loans constituting 20 percent of total microcredit, representing 25.0 percent increase on the previous year (Table 3).

The movement also registered improvement in mobilisation of member shares and savings deposits during the year. As at December 2010, member shares stood at MK2, 196.2 million, up from MK1, 818.9 million (Table 3), representing 21.0 percent or MK377.3 million increase. In terms of savings, members placed a total of MK215.1 million in 2010, an increase of 34.8 percent or MK55.5 million on the preceding amount. Members prefer to hold more shares than savings in order to increase their capacity to borrow. Financial cooperatives largely lend basing on shares.

In terms of expenses, the cooperatives managed to keep operating expenses within their means. However, the expenses recorded an upsurge of 88.1 percent to close the year at MK555.4 million. The increase can be attributed to recruitment of competitive staff and acquisition of operational infrastructure such as computers in readiness for licensing by the Reserve Bank. The revenue side, on the other hand, recorded an increase of 55.3 percent and closed at MK785.9 million. Consequently, the movement recorded surpluses amounting to MK163.7 million, a decrease of MK11.6 million or 6.6 percent on the preceding period.

6.3 Legal and Regulatory Developments

After undergoing rigorous consultations with the industry, the Microfinance Bill was endorsed by Cabinet and presented in Parliament. The Bill was consequently passed into law during the September 2010 Parliamentary session. Work on formulation of regulations, directives and

guidelines to accompany the law took the centre stage with technical assistance from Financial Sector Reform and Strengthening Initiative (FIRST). Registration and licensing would not commence until the regulations, directives and guidelines are published. It is therefore expected that registration and licensing would start in 2011.

Box B: Highlights of the Microfinance Act, 2010

The Act provides for the regulation and supervision of commercial microfinance operations in Malawi. The Act gives the Registrar, who is the Governor of the Reserve Bank, powers to regulate and supervise the sector. The Act provides for progression in the conduct of microfinance business through registration of micro-lending; and licensing of non-deposit taking, and deposit-taking microfinance institutions.

The Act provides for a two-pronged approach: market conduct for micro-lending institutions with periodic reporting requirements to the Registrar; and prudential regulation for large non-deposit taking MFIs, and all deposit-taking MFIs. The prudentially regulated shall comply with capital, lending and liquidity requirements in addition to being subject to conventional governance standards and internal controls. The prudential regulation also calls for comprehensive periodic reporting.

The Act, alongside the Financial Services Act, introduces administrative penalties, punishment, and winding up procedures for all categories.

In another development, the Financial Cooperatives Bill was also presented and endorsed by Cabinet in November 2010. The Bill was therefore ready and slated for presentation to and consideration of Parliament in 2011. Work on formulation and consultation on draft regulations, directives and guidelines for cooperatives stalled until the Bill is passed into law.

6.4 International Relations and other Developments

6.4.1 International Relations

In order to leverage on worldwide experiences on increasing access to financial services to the larger segment of the Malawi population, the Reserve Bank joined membership of Alliance for Financial Inclusion (AFI). AFI is a global network of central banks and other policymaking bodies from developing countries only. AFI provides tools and resources to its members for sharing, developing, and implementing their own knowledge of policies that increase access to formal financial services.

The Reserve Bank also joined MF-Transparency initiative. MF-Transparency is an international institution working with microfinance institutions, central banks and investors to bring pricing transparency to the industry. MF-Transparency was established to promote the welfare of poor micro-entrepreneurs, and to promote the integrity of microfinance as a poverty alleviation practice.

6.4.2 Capacity Building

During the year under review, the Reserve Bank undertook a number of initiatives aimed at improving its service delivery and building capacity. Key among the initiatives was the reorganization of the Bank's corporate structure which resulted into the then Supervision of Non-Bank Financial Institution department split into two departments, namely the Pension and Insurance Supervision; and the Microfinance and Capital Markets Supervision. This was meant to give prominence and proper focus of the areas the Reserve Bank regulates.

In addition, the Bank continued to consolidate its supervisory capacity in microfinance through recruitment and training. Three new members of staff joined the Microfinance Division through recruitment and redeployment, bringing the Microfinance staff compliment to nine (9). Further to this, two members attended a three-week specialised Boulder Microfinance Program in Italy with funding from the United Nations Capital Development Fund. Other members also attended training and workshops organised and offered by Macroeconomic and Financial Management Institute of Eastern and Southern Africa (MEFMI) in the region.

6.5 Future Plans

The Department will continue to finalize work on formulation of regulations, directives and guidelines that will work alongside the Microfinance and Financial Cooperatives Acts. Registration and licensing of market players will not commence until the regulations and directives are published. Nonetheless, call report templates will be circulated to market players for familiarity prior to gazetting.

Capacity building, in terms of staffing and skills, remains critical for effective regulation of the microfinance industry. The Department will therefore endeavour to urge Management of the Reserve Bank of Malawi to recruit additional staff. In addition, the Department will continue using available resources to build capacity of staff through specialised long-term and short-term training. The Department will also endeavour to incorporate risk-based approach to supervision of the microfinance industry in order to ensure effective supervision from limited supervision

resources. In a related development, the Department plans to delegate some supervision to Malawi Union of Savings and Credit Cooperatives and Malawi Microfinance Network for the self-regulation of cooperative movement and microfinance industry, respectively. The Department therefore, in collaboration with stakeholders like FIMA project, Malawi Government, UNDP, UNCDF, among others, commits itself to develop capacities at the two institutions.

At international level, the Department will continue collaborating with its stakeholders in order to leverage on existing worldwide experiences and best practices.

7.0 CONSUMER FINANCIAL EDUCATION (CFE) AND CONSUMER PROTECTION (CP)

7.1 Introduction

This year saw several developments in the financial landscape of Malawi, chief of which was enactment of several financial laws. Worth mentioning is the Financial Services Act which was enacted in July 2010. This Act is an umbrella law for all financial activities in Malawi and it provides for the Reserve Bank of Malawi (RBM) to undertake or promote consumer awareness for the public in financial matters. With the passing of this Act, the Bank re-organized itself to re-align its supervisory functions with the new law and its subsidiary laws. CFE and CP are thus viewed as one way of protecting and safeguarding the interests of depositors, policyholders and the investing public.

7.2 Developments at the Reserve Bank of Malawi

The RBM, as part of re-organization, and effective July 2010, created a division within its supervisory function to be solely responsible for consumer education and consumer protection. The Bank also embarked on the process of recruiting suitable staff to fill the vacancies in the division. The following are therefore set as the goals for consumer education and consumer protection in Malawi:

- Creating awareness and educating consumers on access to financial services.
- Making consumers understand their rights and responsibilities as clients of financial services.
- Changing attitudes of the general public to translate knowledge into behaviour.
- Enhancing arrangements for consumer complaints redress mechanism.
- Ensuring fair treatment of consumers through good market practices.

The RBM, as a policy, decided not to undertake the task of educating the nation alone and as such, the strategy was to involve other stakeholders. To this end, a meeting of stakeholders was convened in July 2010 with funding support from United Nations Development Program (UNDP). The core objective of the meeting was to lay a foundation for the development of a National Framework for Financial Literacy and Consumer Protection in Malawi. The forum,

which converted into a National Committee on Financial Literacy and Consumer Protection³, comprises key stakeholders drawn from the financial sector, line Government ministries, academia, civil society, and donor/development partners. In order to achieve the objectives, the stakeholders will spearhead processes of formulation, sensitization and implementation of the Strategy. The UNDP, through Financial Inclusion in Malawi (FIMA) Project, would finance all costs associated with developing the National Strategy on CFE and CP.

7.3 The National Committee on CFE and CP

The National Committee has the ultimate responsibility to formulate a Financial Literacy and Consumer Protection Framework. A Technical Committee, which is a think-tank for the National Committee, was appointed to handle technical activities. The RBM chairs the Technical Committee and also provides secretarial services.

The Technical Committee, among other tasks, will be:

- Advising the National Committee on specific activities to be carried out in order to achieve the goals of the financial literacy and consumer protection initiative;
- Facilitating the drafting of the National Strategy;
- Making recommendations on implementation plan of the National Strategy;
- Facilitating development of a consumer awareness curricula;

The Technical Committee agreed that the target group for the CFE should be threefold:

- Existing users of financial services,
- The unbanked i.e. those not currently accessing financial services; and
- Pre-users, including students in secondary schools and tertiary education institutions.

³ The National Committee comprises the Reserve Bank of Malawi, Ministry of Finance, FIMA Project, Ministry of Education, Ministry of Industry and Trade, Ministry of Gender, Women and Children Welfare, FEDOMA, Capital Market Players, Bankers Association of Malawi, Insurance Association of Malawi, Malawi Microfinance Network, CRB-Africa, Malawi College of Accountancy, Bunda College, Chancellor College, Mzuzu University, the Polytechnic, National Association of Small and Medium Enterprises, Consumers Association of Malawi, Media Council of Malawi, and UNCDF.

The Technical Committee met three times in the year since its creation in July 2010. The aim is for the committee to meet twice in every quarter; whilst the national committee will meet once every quarter. The following table lays down activities of the National Committee and Technical Committee for a period of twelve months.

NO	ACTIVITY	TIMELINE
1	Consultative stakeholders' workshop to lay foundation for financial literacy and consumer protection initiative.	June 2010
2	Development of TORs for: (i) National Committee (ii) Technical Committee	July 2010
3	Meetings of: (i) National Committee (ii) Technical Committee	Quarterly Twice, Quarterly
4	Study visits to any of neighbouring or African countries where CFE and/or CP have already taken root.	Quarter 1 - 2011
5	Desk review of financial literacy needs assessment	March 2011
6	Drafting of National Financial Literacy and Consumer Protection Framework	Mar – April 2011
7	Consultative workshop for stakeholders to discuss Draft Framework	April 2011
8	Submission of Framework to Minister of Finance for Cabinet approval	May 2011
9	Development of financial literacy curricula and material	May 2011
10	Training of trainers workshop	June 2011
11	Official launch of approved National Financial Literacy and Consumer Protection Framework	July 2011

8.0 APPENDICES

8.1 List of Tables and Charts

8.1.1 Capital Markets

Table 1: [Malawi All Share Index](#) (1999=100)

Period	Indices			Market Capitalisation	
	Domestic Share Index	Foreign Share Index	Malawi share Index	All	(in billion Kwacha)
2000	270.1	213.7	518.4		613.8
2001	280.2	188.5	458.7		543.2
2002	233.4	128.2	313.4		395.2
2003	229.6	188.5	457.3		584.1
2004	426.0	238.8	583.5		745.3
2005	687.0	358.2	906.9		1,120.3
2006	1,793.4	521.6	2,310.0		1,672.1
2007	3,823.5	521.6	4,849.8		1,769.2
2008	4806.9	521.6	6080.4		1,838.3
2009	4,087.2	314.2	5,154.9		1,172.1
2010	3922.6	351.9	4953.1		1,278.5

Table 2: Allocation of Funds under Management by Source (MK'billion)-2010

Source of Funds	1 st Quarter	2 nd Quarter	3 rd Quarter	4 th Quarter
Life Insurance Companies	19.3	16.7	21.8	23.0
Pension Funds	29.2	43.6	44.6	48.3
General Insurance Co	4.3	2.7	2.2	2.3
Unit Trust Schemes	3.4	2.5	3.5	3.6
Companies	4.6	5.6	11.3	12.3
Other Sources	1.6	2.1	4.5	4.5
Total Funds	62.4	73.2	87.9	94.0

8.2 Licensed Market Players in 2010

8.2.1 Capital Markets

8.2.1.1 Stock Exchange

1. Malawi Stock Exchange

8.2.1.2 Portfolio/Investment Managers

1. Alliance Capital Limited
2. CDH Asset Management Limited
3. First Merchant Bank-Asset Management Division
4. INDETrust Limited
5. NBM-Financial Management Services
6. NICO Holdings Limited
7. Old Mutual Life Assurance Company Mw Ltd-Asset Management

8.2.1.3 Brokers

1. African Alliance Securities Limited

2. CDH Stockbrokers Limited
3. FDH Stockbrokers Limited
4. Stockbrokers Malawi Limited

8.2.1.4 Investment Trust

1. National Investment Trust Limited

8.2.2 Microfinance

8.2.2.1 List of microfinance service providers

1. Blue Financial Services
2. CARE
3. CISP
4. Concern Universal Microfinance Operations (CUMO)
5. Development of Malawi Entrepreneurs Trust (DEMAT)
6. Ecumenical Church Loan Fund (ECLOF)
7. Foundation for International Community Assistance (FINCA)
8. Finance Trust for the Self Employed (FITSE)
9. Greenwing Capital
10. Izwe Loans
11. Malawi Rural Finance Company (MRFC)
12. Malawi Savings Bank (MSB)

13. Malawi Union of Savings and Credit Cooperatives (MUSCCO)
14. Malawi Rural Development Fund (MARDEF)
15. Microloan Foundation
16. National Association for Business Women (NABW)
17. Opportunity International Bank of Malawi (OIBM)
18. Participatory Rural Development Organization
19. Pelton Finance
20. PRIDE Malawi
21. Project Hope
22. Small and Medium Enterprises Development Organization of Malawi (SEDOM)
23. Touching Lives Fund
24. The Hunger Project

8.2.2.2 List of savings and credit cooperatives (SACCOs) affiliated to MUSCCO

Southern Region

1. ADMARC Employees
 2. Blantyre ADD
 3. Blantyre City Teachers
 4. Blantyre Water Board
 5. Bvumbwe
 6. Chiradzulu Community
 7. Chithandizo SACCO
 8. Kasinthula
 9. Malawi Broadcasting
 10. Mudi
 11. Mulanje Teachers
 12. Mwanza Community
 13. Nsanje Community
 14. Oilcom
 15. Polymed
 16. PTC
 17. Sucoma
 18. Sunbird Tourism
 19. Thyolo Teachers
 20. Zomba teachers
- Central Region**
21. Auction Holdings
 22. Chitukuko
 23. Dedza
 24. DWASCO
 25. FINCOOP Malawi Ltd
 26. Kandiya
 27. Kasungu ADD
 28. Kasungu community
 29. LADD
 30. Lilongwe Urban Teachers
 31. Mchinji Teachers
 32. Ministry of Transport
 33. Mzinda
 34. QM
 35. RBM
 36. Regional Surveys
 37. Salima Teachers
 38. TPLL
 39. Ulimi
 40. UNDP
 41. University
 42. Veterinary
- Northern region**
43. Chikangawa
 44. Karonga Teachers
 45. Mzimba Teachers
 46. Rumphi Community
 47. Rumphi Teachers
 48. Umoza Community

9.0 DEPARTMENTAL STRUCTURE OF MICROFINANCE AND CAPITAL MARKETS SUPERVISION

