don't just want culprits caught and punished. They also want their stolen goods returned, or other restitution made. People resort to mob justice because they lose confidence in the processes employed by the police and the courts.

10.1.2 Increased recruitment and better training for the Police Service is needed, and police must be equipped for effective service. The cost of adequate policing can be reduced, and relationships between police and citizens can be improved, by a greater emphasis on supplementing regular police services with community policing.

10.1.3 This should be accompanied by a concentrated effort to improve efficiency and consideration for complainants and informers. The Committee agrees with the recommendations of a Justice of the Supreme Court of Appeal made during PRSP consultations to improve the delivery of justice, and to integrate traditional courts with statutory courts. Funding must be increased for justice delivery overall.

> Recommendation 21: Substantially increase the budgets for training and employment for the Police Service (to increase the number of trained officers), and for instituting community policing, particularly in rural areas. Include in the budgets adequate funds for equipment and other materials, and designate the same as Priority Poverty Expenditures.

11. Macroeconomic Review

11.0.1 Growth in the economy is absolutely necessary in order to reduce poverty, yet the macroeconomic situation in the country has generally deteriorated during the past twelve months. The cost of living as reflected in the inflation rate has gone up, interest rates have been consistently high, and the Malawi Kwacha has lost value against major trading currencies by a large margin. Weakening of the Kwacha has contributed to higher local prices through costly imports. The Kwacha depreciation is itself a direct reflection of the country's weak export base, which is overdependent on tobacco.

11.0.2 Government has taken major steps under the Ten Point Plan to improve management of public funds. However, the benefits of the fiscal reforms have only become manifest in the last few months meaning that the general population has yet to feel a positive impact on their lives. This has led to widespread calls for Government to further tighten expenditure controls.

11.1 Economic Outlook

11.1.1 The economy's poor performance has resulted in an economic growth rate inconsistent with the government's poverty reduction goal. Economic growth during 2001 is expected to be below 3%. This compares poorly with last year's 3.4% growth in Real GDP and with 6% growth which is required for significant poverty reduction. The poor growth expectation stems from below average performance in agriculture and a declining manufacturing sector. In particular, the recent heavy rains are expected to dampen agricultural production, especially of maize. This will have negative consequences for food prices and could lead to an increase in inflation.

11.1.2 Government may be able to counter this by reducing expenditures, and maintaining low borrowing levels. These measures could reduce inflationary pressures emanating from growth in the money supply. Similarly, the stability of the Kwacha and its recent appreciation against other currencies will reduce inflationary pressures from imports. The final outcome on inflation this year will therefore depend a great deal on the harvest and government's interventions in the food market. Meanwhile, interest rates are expected to decline steadily given the current downward trend in treasury bill yields. This should reduce the cost of credit to the private sector and possibly allow some resurgence in this sector. Only through much higher levels of private investment will economic growth rebound to levels necessary for meaningful poverty reduction.

11.2 Inflation

11.2.1 Malawians are concerned with the rising cost of living; the need for more stable prices for domestic goods and services was one of the key findings in PRSP district consultations. The annual inflation rate is the best indicator of changes in the cost of living because it measures changes in the general price level from year to year. In June 2000, annual inflation was 22.2%, and this was close to the 19% average over the past thirty years. By December 2000 inflation had risen as high as 35.4% partly due to the weakening Kwacha. Since then, inflation has gradually declined to 27.4% in April 2001. This is still too high, especially considering the 10% inflation target for December 2001. The Committee has in the past been skeptical of Government's inflation targets.

11.3 Monetary Policy

11.3.1 Monetary policy involves managing the country's money stock through various instruments including treasury bills, central bank bills, and interest rate adjustments. Since 1999, the Reserve Bank of Malawi has been following a tight monetary policy by limiting the growth of money held in the Bank. A tight monetary policy helps to reduce inflation that results from allowing too much money to circulate in the economy. In spite of the Bank's policy, growth in total money supply (M2) increased rapidly between August and November 2000, peaking at 48% in November, compared to 12% in June 2000. This loosening of monetary policy was related to increased Government borrowing during the second half of calendar year 2000 (the first half of financial year 2000/2001).

11.3.2 Growth in M2 began to slow down in December 2000 falling to 35% in February 2001. The contraction in the money supply follows a reduction in net domestic credit. This reflects Government's aggressive repayment programme to the Reserve Bank and to the banking system in general. In fact, since the beginning of 2001, Government has stopped borrowing on the Bank's overdraft facility.

11.4 Interest Rates

11.4.1 Reduced Government borrowing has resulted in a steady decline in treasury bill yields and is expected to bring down interest rates which have been persistently high this year. The bank rate has been above 60% for most of 2001 and even reached 75.3% in February. This contrasts sharply with the 47% rate that prevailed during 2000. The increased volatility in the bank rate is related to RBM's new formula for determining this variable by tying it to the 271-day treasury bill yield. The suitability of this approach has been questioned.

11.5 Fiscal Policy

11.5.1 Fiscal policy represents Government's attempts to influence the economy by changes in expenditure or taxes in order to achieve particular goals. A good indicator of fiscal policy is the government deficit that shows the shortfall between Government revenues and expenditures. During the first few months of the 2000/01 fiscal year, the deficit widened significantly when compared to the previous quarter. That is, expenditures increased faster than revenues.

11.5.2 Increases occurred mainly in recurrent expenditures (other expenditures, wages and salaries, and domestic interest payments) and extrabudgetary items *(RBM, Financial Economic Review, No. 2, 2000)*. Government revenues during this period were lower than projected due to the Kwacha depreciation that affected import volumes and therefore taxes collected from this source. Furthermore, there were delays in donor funding during 2000, meaning that both local and foreign sources of revenue were down.

11.5.3 The budget deficit incurred during this period was mainly financed through borrowing on the domestic market leading to higher interest rates as noted above. More recently, total expenditure has begun to decline in part due to reduced loan repayments on treasury bills, as well as to cost savings arising from the Ten Point Plan, 70% of which has been implemented according to Government. Nonetheless, the overall deficit (before grants) remains a worrying 14% of GDP, compared to an overall deficit of 9.3% of GDP in 1999. A widening deficit points to the need for tighter expenditure control, especially as government revenues are expected to decline once the new regional trade protocols are fully implemented.

12. The Private Sector

12.0.1 Growth in the private sector is the key to diversifying the economy and increasing employment in agro-processing and other manufacturing, tourism, and other industries. While much is said about encouraging private business, little seems to be happening on the ground. The Private Sector Development Project funded by the World Bank, for example, has been stalled for several years. The Committee heard testimony from the private sector highlighting constraints to business development. Among other things, private businesses are concerned about the level of taxes imposed on them, a function of the limited economic base from which the Government can raise revenues.

12.1 The Surtax

12.1.1 Government has gazetted legislation (Bill No. 2, 2001) to extend the surtax to wholesale and retail trade. This is a commendable effort by government to broaden the tax base, particularly important since international trade agreements to which Malawi is a party will reduce revenue from duty on imports, the largest single source of domestic revenue. Properly conceived, extension of the surtax should lead to significant increases in government revenue as well as benefits for local manufacturers.

12.1.2 Representatives from the private sector who testified before the Committee raised significant questions about Bill No. 2. Some concerns relate to provisions that are unclear and/or place excessive discretionary powers in the hands of implementing authorities. The concerns of the private sector seem to the Committee to be too serious to be adequately addressed by amendments to the Bill during plenary debate in Parliament or by subsidiary legislation after enactment.

12.1.3 The surtax is essentially a value-added tax, and such taxes tend to be regressive in nature, i.e., poorer individuals pay higher percentages of their