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APRA Policy Brief

Issue No. 26 July 2020

Inducing agribusiness investment in Malawi: Insights from investors

Key messages

- Fiscal incentives that are designed to increase investment in agriculture in Malawi rarely motivated initial investments. They were, however, taken advantage of by existing enterprises to increase their operational capacities and profit margins.
- Limited access to finance and poor information on available funding sources constrains agro-investment. The government should support the creation of a tailored financial institution – or enable an existing institution to introduce a tailored service that would ease access to business finance for investments in agriculture and agribusiness.
- The most potent business investment incentives are those that support inclusive business models that bring smallholder farmers into high value agricultural value chains and connect them to structured markets that offer decent prices for agricultural produce and labour.
- The administration of incentives needs streamlining, particularly of processes, clarity of entitlements and eligibility criteria, and a robust monitoring and evaluation framework that supports evidence-based incentive schemes.

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Introduction

Agriculture is the bedrock of Malawi's development strategy. It absorbs more than 80 per cent of the labour force, with most engaged in seasonal subsistence agriculture (World Bank, 2017). However, government investment in agricultural commercialisation has been low, national financial institutions do not have agribusiness-friendly policies, and access to large tracts of land necessary for commercial agriculture has been a challenge. A lack of infrastructure, such as roads and electricity, also constrain business operations, increase the cost of doing business, and undermine the competitiveness of Malawi's agribusiness sector.

To increase investment in agriculture in Malawi, the government and donors provide a variety of incentives, targeting both local and foreign agribusinesses. The effectiveness of the incentives is dependent on several factors, including how they are administered or accessed.

Incentives for agricultural investment

Government and development partners provide fiscal and non-fiscal incentives to private enterprises to encourage and support investment in agricultural commercialisation. Many government fiscal incentives are in the form of tax incentives (Table 1).

The government also provides a range of non-fiscal incentives administered by several Ministries, Departments and Agencies (MDAs). The incentives include facilitation of registration and licensing of businesses, access to investment resources and business finance, provision of business and export market information, creation of linkages between local and foreign investors, and facilitation of joint ventures, among others.

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Table 1: Overview of tax incentives relevant to agribusiness

Incentive type	Incentive description
Customs and excise tax incentives	Exemption from income tax for up to 10 years. Exemption from import tax (duty) on capital goods and building materials, exemption from import duty and Value Added Tax (VAT) on importation of livestock meant for breeding, and exemption from import duty, import excise and VAT for goods directly used in irrigation.
Industrial rebate scheme	Import and excise duty exemption for raw materials designated for manufacturing industries, but VAT is payable.
Export Processing Zone (EPZ) – established to attract export-oriented industries by offering them more favourable investment incentives than the rest of the manufacturing industry in Malawi	Duty free relief on goods to be used in government-approved factories located in the EPZ under certain conditions. However, it excludes tobacco, tea, sugar and coffee.
Capital allowances – initial capital allowances offered on capital expenditures during the year of acquisition	5% on industrial buildings and improvements to farm buildings; 10% on farm fencing; 15% on heavy machinery and installation; 10% on light machinery; 33.33% on trucks and tractors; 20% on light commercial vehicles; and 2.5% on commercial building costing more than MK100 million (US\$135,000).
Investment allowances – given to tax payers who are also manufacturers	For unused industrial buildings, plant or machinery, the allowances equal 100% of the cost of used industrial buildings and/or a plot or machinery.
Export allowances	Income tax allowance of 25% of taxable income derived from export sales.
Transport allowances	Additional allowance of up to 25% of international transport costs incurred by a tax payer for their exports.

Despite having a wide range of investment incentives, the government’s administration of these is fragmented and overseen by multiple MDAs. Tax incentives, for example, are primarily administered by the Ministries responsible for finance, trade and private sector development, in collaboration with the Malawi Revenue Authority. The administration of non-fiscal incentives involves line Ministries, the Malawi Investment and Trade Centre, the Greenbelt Authority, and the Export Development Fund, among others.

Development partner incentives

While most of the government’s incentives relate to large-scale capital investments, donor incentives usually target investments that engage small-scale farmers, or are willing to implement inclusive business models that increase farmers’ access to a structured market for their produce. International development agencies that have actively supported business investments in agricultural commercialisation include the United States Agency for International Development, the European Union, the UK’s Department for International Development, the United Nations Development Programme, the German development bank, KfW, and the World Bank.

Factors driving investment decisions and implementation of incentives

Four in-depth case studies of agribusinesses in the coffee, rice, fruit, and bio-energy value chains explored factors driving investment decisions from 2005 to 2015 (Chingaipe, Thombozi and Chingaipe, 2019). The case studies are based on primary data collected through in-depth interviews with agribusiness leaders and key informants carried out under the Agricultural Policy Research in Africa (APRA) consortium.

The findings show that investment decisions were primarily motivated by the investors’ need to, and prospects of, making a decent return. While a general conducive business and investment environment were also extremely important, some investors still risked their capital in sub-optimal environments as long as they could see a real prospect of making money. Some agribusiness investments, especially by established agribusiness enterprises, were primarily motivated by the ambition to increase market share and revenues and achieve economies of scale in production, thereby improving efficiency and returns on investment. Another factor driving investment in new business activities (start-ups) was the desire to diversify in order to spread risk, given the precarious nature of the policy and political environment in Malawi, and volatility of produce or commodity markets.



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Demonstrating vegetative propagation



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Irrigating greenhouse crops

Policy incentives identified as positively improving the investment and business environment include access to finance and other investment resources, particularly land. These were found to be a motivation for both initial investments as well as for existing investors.

Fiscal incentives were not found to motivate initial investments in new agribusinesses (start-ups). Investors across value chains stated that they would have invested even if there had been no such incentive. However, these incentives are used by existing enterprises to expand their production and processing capacities and to develop new business models.

The study also found that incentives that support inclusive business models and the creation or provision of access to structured farm produce markets for smallholder farmers were more transformative and economically empowering for smallholder farmers.

When agribusinesses attempted to take up incentives, many found their administration to be cumbersome, because so many different institutions were involved. The problem was compounded by insufficient and sub-optimal public sector coordination mechanisms, which resulted in delays and high transaction costs

for businesses applying for the incentives. There was also a lack of clarity on entitlements associated with specific incentives, and on processes and administrative requirements in order to access these incentives. There also exists a latitude of discretion for administrators of the incentives that is unhealthy and inimical to investment logic, and provides opportunities for extortion and bribery. Some politically-inclined bureaucrats, for example, bring in irrelevant considerations such as whether the investor is supportive of the party in government or not.

Monitoring and review of the uptake and effectiveness of incentives is also almost non-existent, meaning that there is little potential for learning or for improving policy impact.

Incentives and commercialisation pathways

There are multiple pathways through which agribusiness investment can enable agricultural commercialisation, which are subject to the growth strategies adopted by agricultural enterprises. Access to, or availability of, finance and land, and the economic and development priorities of policymakers and development partners, also shape these emergent pathways.

The design and implementation of government-led fiscal and non-fiscal incentives in Malawi tend to favour large-scale capital investments, i.e. estate/plantation/large-scale commercial farming and medium-scale enterprises, mostly focussing on the processing aspects of the businesses. Thus, they prop up more vertically integrated commercialisation pathways. Donor incentives, however, due to their emphasis on inclusive and developmentally-transformative business models, tend to support outgrowing or contract farming pathways.

Policy recommendations

So what can or should be done from a policy point of view to induce business investment in agricultural commercialisation?

- i. Government investment policy should address structural factors, rules and policies that negatively affect the business environment to make the climate for investment in agriculture and agribusiness generally conducive and enabling, instead of providing largely ineffective fiscal incentives.
- ii. The government, through its MDAs, should begin to design incentives that serve clear, monitorable purposes for economic and industrial transformation of the country.



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Grain storage facility

- iii. The government, through its MDAs, must develop and implement a consolidated communication strategy about investment incentives, to explain the incentives, and outline eligibility criteria and processes for accessing them in a way that reduces transaction costs. Such communication should also include all sectoral programmes run by development partners and the range of incentives offered under those programmes.
- iv. In order to spearhead transformational agricultural commercialisation, the government must streamline its business incentives to focus on and encourage private sector enterprises to adopt inclusive business models that connect a large number of smallholder farmers to reliable markets that pay decent prices for farm produce.
- v. The government should undertake reforms to increase certainty and predictability in the administration of business incentives by reducing the latitude of discretion of bureaucratic and political executives in the granting of incentives.
- vi. The government should support the creation of a tailored financial institution that would ease access to business finance for investments in agriculture and agribusiness.
- vii. The government should review, develop and enforce one way through which foreign investors acquire agricultural land for agribusinesses.
- viii. The government should work out and implement a joint monitoring and evaluation framework for agribusiness

- investment incentives to systematically capture data on investment uptake and effectiveness, moving decision-making away from economic theory and towards pragmatic and evidence-based policy.
- ix. The government should rationalise and streamline the mandates of the MDAs involved in the design and implementation of investment incentives to shorten processes, cut down on red tape and reduce transaction costs of accessing incentives.

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Citation

Chingaape, H.; Thombozi, J. and Chingaape, H. (2020) *Inducing Agribusiness Investment in Malawi: Insights from Investors*, APRA Brief 26, Brighton: Future Agricultures Consortium

ISBN: 978-1-78118-666-4



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All APRA Working Papers go through a review process before publication.

The Agricultural Policy Research in Africa (APRA) programme is a five-year research consortium. APRA is funded with UK aid from the UK government and will run from 2016-2021.

The programme is based at the Institute of Development Studies (IDS), UK (www.ids.ac.uk), with regional hubs at the Centre for African Bio-Entrepreneurship (CABE), Kenya, the Institute for Poverty, Land and Agrarian Studies (PLAAS), South Africa, and the University of Ghana, Legon. It builds on more than a decade of research and policy engagement work by the Future Agricultures Consortium (www.future-agricultures.org) and involves new partners at Lund University, Sweden, and Michigan State University and Tufts University, USA.



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