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AGRIBUSINESS SMES IN MALAWI

**ASSESSMENT OF SMALL AND MEDIUM ENTERPRISES IN THE
AGRICULTURE SECTOR AND IMPROVED ACCESS TO FINANCE IN
MALAWI**

LEO

Leveraging Economic
Opportunities

REPORT #5

AUGUST 2014

This publication was produced for review by the United States Agency for International Development. It was prepared by Jason Agar, Kadale Consultants of Malawi, for ACDI/VOCA with funding from USAID's Leveraging Economic Opportunity (LEO) project.

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FOREWORD

This report has been prepared by Jason Agar of Kadale Consultants with the support of Tione Kaonga, Frank Mkumba, Louis Jalakasi and Ndankhonza Munlo, with quantitative analysis by Taonga Chipeta of Kadale. Geoffrey Chalmers of ACIDI/VOCA provided overall guidance for the assessment, for which the author is grateful.

The views expressed in the report are those of the author, based on the available secondary documents and primary research, and do not represent, or purport to represent, the views of the United States Agency for International Development (USAID).

The team would like to express its gratitude to Mr. Christopher Chibwana, Private Sector Development Specialist, in the Sustainable Economic Growth Team at USAID, for his guidance and support. In addition, the team would like to recognize the role of the Private Sector Development team at the Ministry of Industry and Trade, in particular inputs from Alexander MTsendero, Principal Development Officer, SME Department, and McCartney Gift Lora, Enterprise Development Officer, SME Department.

The field research team met with over seventy small and medium enterprise (SME) owners and managers, who took time out of running their businesses to discuss the challenges and opportunities that they faced. In addition, banks, other financial institutions, development partners and other stakeholders gave their time generously in order to provide their views. We are grateful to all those who provided information for this study. Any misstatement or misrepresentation of that information is the responsibility of the consultants.

Jason Agar,
Kadale Consultants, Malawi

ACRONYM LIST

AfDB	African Development Bank
AGRA	Alliance for a Green Revolution in Africa
AI	Artificial insemination
ASME	Agri-business small and medium enterprise
A2F	Access to finance
BCA	Business Consult Africa
BDS	Business development services
BESTAP	Business Environment Strengthening Technical Assistance Program
BIF2	Business Innovation Facility (Phase 2)
BMO	Business membership organization
C&C	Collaboration and clustering
CoF	Certificate of Fitness (for a vehicle)
DCA	Development Credit Authority
DEMAT	Development of Malawian Enterprise Trust
DFID	Department for International Development
DRC	Democratic Republic of Congo
EEAG	Economic Empowerment Action Group
EIB	European Investment Bank
EU	European Union
FI	Financial Institution
FISP	Farm Input Subsidy Program
FSTAP	Financial Sector Technical Assistance Program
FTF	Feed the Future
GDP	Gross Domestic Product
GoM	Government of Malawi
GTPA	Grain Traders and Processors Association
IBAM	Indigenous Business Association of Malawi
IFC	International Finance Corporation
ICT	Investment Climate Assessment
INVC	Integrating Nutrition in Value Chains
IT	Information technology
LDF	Local Development Fund
LLC	Limited Liability Company
MBG	Milk Bulking Group
MBS	Malawi Bureau of Standards
MCCCI	Malawi Confederated Chambers of Commerce and Industry
MCJCSP	Malawi Competitiveness and Job Creation Support Project
MDDA	Malawi Dairy Development Alliance
MDI	Malawi Dairy Industries
ME	Microenterprise
MEPC	Malawi Export Promotion Council
MES	Medium Enterprise Survey

MFI	Micro finance institution
MGDS2	Malawi Growth and Development Strategy 2
MICF	Malawi Innovation Challenge Fund
MIM	Malawi Institute of Management
MIPA	Malawi Investment Promotion Council
MIRTDC	Malawi Industrial Training and Research Center
MITC	Malawi Investment and Trade Centre
MK	Malawi Kwacha
MNO	Mobile Network Operator
MoIT	Ministry of Industry and Trade
MRA	Malawi Revenue Authority
MRFC	Malawi Rural Finance Company
MSE	Micro and small enterprise
MSME	Micro, small & medium enterprise
MT	(metric) ton
NASME	National Association of Small and Medium Enterprises
NBFIs	Non-bank financial institutions
NBM	National Bank of Malawi
NCIC	National Construction Industry Council
NES	National Export Strategy
NGO	Nongovernmental organization
NPL	Non-Performing Loans
NSO	National Statistical Office
OBM	Opportunity Bank of Malawi
OVOP	One Village, One Product
PASS	Private Agriculture Sector Support (Trust)
PAYE	Pay as you earn
PDM	Pest and disease management
PIPHR	Presidential Initiative on Poverty and Hunger Reduction
PSD	Private sector development
RBM	Reserve Bank of Malawi
RLEEP	Rural Livelihoods Economic Empowerment Program
SEDOM	Small Enterprise Development Organization of Malawi
SME	Small & medium enterprise
SMEA	Small & Medium Enterprise Association
SMEDI	Small and Medium Entrepreneurship Development Institute
SQAM	Standards, Quality Assurance and Metrology
TIP SWAp	Trade, Industry and Private Sector, Sector Wide Approach
TEECS	Tools for Enterprise and Education Training Consultants
TEVETA	Technical, Entrepreneurial, and Vocational Education and Training Authority
UNDP	United Nations Development Program
USAID	United States Agency for International Development
VAT	Value added tax
WRS	Warehouse receipt system
ZoI	Zone of influence

EXECUTIVE SUMMARY

This assessment of agri-business small and medium enterprises (ASMEs) in Malawi found a sector with diversified business ownership, in which owners commonly operate multiple businesses and can be classed as ‘portfolio’ owner-managers spanning both agri-business and non-agri-businesses. A portfolio enables them to move resources to address cashflow shortages and seasonality in each business, manage uncontrollable downside risks by moving resources from businesses affected by such a risk, and manage growth opportunities by investing in businesses that are making most progress. A key implication is that it is difficult for public sector and donors to invest in specific value chains, as owners move resources within a portfolio of businesses that span more than one value chain and may include non-agri-businesses. The analysis is particularly focused on ASME access to finance (A2F), use of business development services (BDS), use of information and communication technology (ICT), collaborating and clustering (C&C) and the enabling environment (EE).

The study findings are set out in Section 1. An explanation of the characteristics of SMEs¹ is set out in section 1.1, highlighting that seasonal and part-time employees are common, as well as high numbers of unpaid employees who are typically members of the family. According to FinScope 2012, around 75% of SMEs were owned by men (section 1.2.4), though the primary research found even higher proportions of male ownership of ASMEs. The issue of male/female ownership is blurred by traditional attitudes with the man as the identified head, yet potentially having his wife’s participation in the enterprise portfolio.

Details of ASMEs found in the Feed the Future (FTF) Zones of Influence (ZOI) are set out in section 1.2. The value chain functions at district level are agri-input supply, trading, transport and retail sale. There are few agri-service providers and agri-processors, but no SME owned and rented out warehousing. Value chain functions at district level primarily support or aggregate production, which is moved to the urban areas for processing and marketing.

Details of the soybean, groundnut and dairy value chains are set in section 1.4. There was little specialization in groundnut or soybean with input suppliers, traders and transporters handling both crops and other district specific crops. The exception was a concentration of medium traders in groundnuts in Mchinji, due to high levels of production in this district which attracts many large buyers from other African countries. There were relatively few dairy players at district level other than producers and the Milk Bulking Groups which act as aggregators and input/service suppliers. This is due to the need to integrate production with (urban-based) processors which eliminates the scope for traders to intermediate between producers and processors, leading to more direct relationships between these.

Very limited BDS are used by the ASMEs surveyed with no specialist BDS providers located in the districts (section 1.5), though there are a few business (accountants) and technical (mechanics/technicians) service providers providing some business services. National level private, public and NGO BDS providers depend on subsidy for service provision. The relevance of BDS is currently low, so a more demand-side driven approach would be needed that responds to the needs of owner-managed ASME rather than treating ASMEs as if they were small ‘corporates’. More attention is needed to meeting the challenges of managing a portfolio of ASMEs.

¹ Micro, small and medium enterprises (MSMEs) are defined using Ministry of Industry and Trade’s (MoIT) categories. Micro is 1-4, small is 5-20 and medium is 21-100 employees.

There is low adoption of financial services (section 1.6) other than **bank accounts**, which are primarily used for managing transactions and the safe storage of cash. ASMEs tend to have multiple accounts if they have multiple outlets/businesses. ASMEs reported limited saving; rather cash is invested in different enterprises, with temporary saving used to manage cashflow. ASMEs identified risks relating to theft/robbery, premises (flood/fire) and operations (inflation, transport), with 34.5% of small and 87.5% of medium enterprises having suffered a loss in the previous year. ASMEs managed these risks by taking preventive measures, rather than buying **insurance**.

Around 40% of SMEs surveyed in FinScope 2012 were **borrowing**. However, as also found in the primary research, borrowing from 'business friends' was much more likely than from a formal Financial Institution (FI) as finance was immediately available and often interest free. Potential borrowers need the title for a property, which is hard to provide. Lending of stock and transport was also common. There is a core of ASME owners that will not take formal finance from fear of losing their assets.

All FIs defined their SME portfolios differently, so data could not be aggregated. All FIs have SME Sections/Departments, but with limited actual product tailoring to SME needs; mostly these are re-branded personal banking products. FI staff have limited training and understanding of SMEs; often FI staff are frustrated with SME owner behaviors, such as diverting funds, lack of records, poor finance management skills, etc. FIs are risk averse in their ASME lending, relying on collateral rather than analysis of capacity or willingness to pay; due to the absence of land/property title, many ASMEs therefore cannot access bank finance. Adoption of financial services increases with size, but financial services are not well adapted for ASMEs, limiting overall uptake.

Cellphone was the most common form of **ICT** used by far; half of ASME owners had a smartphone which they used for email and web-access (section 1.7). This provides a potential access point for BDS and financial services.

Examples of **collaboration** (section 1.8) include sharing of stock and transport. ASME owners find others to trust, where there is a mutual benefit in doing so. **Clustering** as a strategic choice was not found, other than a groundnut cluster in Mchinji where there is a high level of production which supported many related businesses.

Details on the **enabling environment (EE)** are set out in section 1.9. Licensing is common as it raises revenue for District Assemblies and so is generally enforced. However, registration is only required if bidding for contracts or raising finance; it is difficult to access but also poorly enforced. There are few EE opportunities not being addressed.

Section 2 sets out the way forward, summarizing the challenges for BDS, A2F, ICT, C&C and EE for ASMEs, setting out possible interventions for addressing these and makes recommendations.

For BDS, the major challenges are: low uptake of BDS by ASMEs; poor co-ordination between providers; high degree of subsidy to make BDS affordable to ASMEs; low service relevance of BDS to ASMEs; low appreciation of the nature of owner-managed enterprises by BDS providers; and low BDS outreach in districts. The possible interventions for USAID include: (1) assist BDS providers to refocus their services for ASMEs; (2) embed BDS provision in value chain players; (3) work with FIs to support BDS to ASMEs underpinned by a credit guarantee package; and (4) research, develop and support the implementation of low cost delivery models for business information and advice/advisory service. **It is recommended that USAID should pursue a combination of the above interventions, combining intervention 4 with any or all of interventions 1, 2 and 3.**

For A2F, the major challenges are: weak financial management skills of ASME owners; low appreciation of ASME operating conditions by FI staff; insufficient information and capacity by FIs to assess ASME lending risk; and titles not available on district properties, limiting collateral. The possible interventions for USAID support in A2F include: (1) support demand-led financial innovations targeting ASMEs; (2) support ASME financial education; (3) support initiatives to improve ASME borrower identification and credit status; and (4) support a wider range of bank guarantee mechanisms targeting ASMEs. Capacity building for FI staff could be integrated into all the above options. **It is recommended that USAID should prioritize interventions 1 and 2, including capacity building of FI staff; interventions 3 and 4 could also be integrated into a program.**

For ICT, the major challenges are: low use of ICT by ASMEs other than cellphones, though smart phone use is increasing; low current use by ASMEs of m-money options for payments and receipts; and low use by ASMEs for email and web activities. The possible interventions for USAID support in ICT are: (1) support development of smartphone-based access to BDS, including financial education; support development and access to tailored ASME ‘Apps’ and access to ‘cloud-based’ storage. **It is recommended that USAID should prioritize interventions 1 and 2; interventions 3 and 4 could also be integrated.**

For C&C, the major challenges are: collaboration is not widely used by ASMEs, with low trust levels and poor experiences; and clustering is not adopted as a conscious strategy. The possible intervention for USAID in C&C is: (1) support research and promotion of ASME collaboration and clustering. **It is recommended that USAID does not prioritize C&C over BDS, A2F and ICT interventions; rather it should seek to encourage greater C&C through the other recommended interventions.**

For the EE, the major challenges are: registration is practically difficult and time consuming for ASMEs that want to register, and there is low understanding of enabling environment and compliance with rules among ASME owners. The possible intervention for USAID support in the EE is: (1) support enabling environment education activities utilizing ICT mechanisms, such as smart-phone access to downloadable materials. **It is recommended that USAID does not prioritize an EE education intervention over other options, as it is of less immediate importance.**

I KEY FINDINGS

The key findings in this assessment are set out in this section, responding directly to the scope of work (see Annex I). This assessment combines a quantitative analysis of the FinScope Micro, Small and Medium Enterprise (MSME) 2012 study ('FinScope 2012') with primary qualitative research covering 68 agri-business SMEs (ASMEs), nine financial institutions (FIs), 12 agri-business value chain larger firms and 10 other ASME stakeholders. The SMEs² within the FinScope 2013 study are a sub-set of the overall nationally representative MSME sample. The qualitative interviews were designed to bring insights that are not captured by quantitative data; however care needs to be taken in generalizing from these. Using a mixed methods approach enabled data and findings to be triangulated, thereby increasing their robustness. The findings that follow in this section are based on quantitative data, supported and extended by the qualitative data and insights. The narrative sets out where data is from FinScope (2012) and where it is from the qualitative interviews. Details of the methodology are set out in Annex II: Methodology.

In this section, an overview of the nature of SMEs in Malawi is followed by a review of ASMEs in the Zone of Influence (ZoI) and of ASMEs in the three target value chains. Finally, there are sections on BDS, Access to Finance (A2F), Collaboration and Clustering (C&C), Information and Communications Technologies (ICT) and the Enabling Environment (EE).

I.1 SMALL & MEDIUM ENTERPRISES

This section provides an overview of SMEs in Malawi, looking at SME definitions, employment in SMEs, the portfolio nature of SME ownership, ASMEs and ownership by men/women.

I.2 SME DEFINITION AND CATEGORIZATION

Definitions of SMEs vary, but using employment criteria of 5-20 employees (small) and 21-100 employees (medium) there are an estimated 61,000 SMEs in Malawi.

The Ministry of Industry and Trade (MoIT) categorizes businesses into 'micro', 'small', 'medium' and 'large' based on employment, defining 'micro' as having 1-4 employees, and thus excluding the self-employed. For this assessment, the best way to profile MSMEs is to define micros as 0-4 employees, since there are very many micros with no employees other than the owner. A revised breakdown of the FinScope 2012 representative sample is as follows in Table 1.

Table 1: FinScope MSME Sample by Business Category, 2012

Sample	Frequency	%
Micro (0-4 employees)	1,772	93.9
Small (5-20 employees)	108	5.7
Medium (21-100 employees)	8	0.4
Total	1,888	100.0

Source: FinScope (2012) database – consultant's analysis

According to FinScope (2012), 93.9% of MSMEs are micro, 5.7% are small and 0.4% are medium-enterprises (MEs). Extrapolating from these proportions gives an estimate of 61,000 SMEs, which is in line with previous

² Note that the term 'SME' is used for all SMEs, whereas 'ASME' is used where the focus is specifically on agri-business SMEs.

estimates.³ However, the small proportion of the SMEs in the FinScope (2012) sample means it is unreliable to disaggregate SME data further by sex or by location of respondents. These differences are drawn from the qualitative study were relevant.

1.2.1 EMPLOYMENT IN SMES

SMEs more commonly employ temporary and unpaid family members, than full time employees. As enterprises grow, the nature of employment becomes more full-time and paid.

Employment is the key determining factor for classifying MSMEs in Malawi. Several important findings follow from the observation that employment in the SME owners' related businesses is not captured in most surveys; by not considering these related businesses as part of a single business portfolio, enterprises appear smaller and more single-purpose than they are in reality. This raises questions of how employment is counted:

1. Whether to count the owner as 'employed'?
2. Whether to count family members (spouses, adult children, siblings, etc.) working in the business?
3. Whether to count workers if there is no pay or formal contract, perhaps with payment in kind?
4. Whether to use a counting method based on full-time only, full-time equivalent or head count, which would include part-time and seasonal/temporary employees

Each method has definitional and data collection challenges. As noted, MoIT uses 1-4 employees, but it is unclear if this includes working owners and if this is full-time, full-time equivalent or a simple headcount basis. Although inclusion of owners is not crucial for this assessment,⁴ the basis of calculation being full-time, full-time equivalent or headcount does make a large difference, as many SMEs employ seasonal and part-time staff.

Table 2: Status of Employees in Small Enterprises, 2012

Employee status (excluding owner)	Employee status as % of all employees - small enterprises	Employee status as % of all employees - medium enterprises
Full-time paid	16.0	47.5
Part-time paid	12.2	13.4
Temporary paid	31.6	14.6
Paid in kind	11.1	6.7
Both Paid /Paid in kind	6.3	9.6
Unpaid	22.2	8.3
Other	0.6	0.0
Total	100.0	100.0

Source: FinScope (2012) database – consultant's analysis, n=108 (small) & n=8 (medium)

The above data highlight that SMEs combine different forms of employment. For small enterprises, the most common form of employment is temporary (paid) at 31.6% of employees, reflecting the seasonal nature of

³ FinScope (2012) does not explain how the total number of businesses was calculated and the method to split micro, small and medium enterprises. This calculated figure should be read with caution as it is lower than previous estimates. E.g. the Assessment of the SME Sector in Malawi (USAID, 2007) combined data from the Gemini and the Medium Enterprise surveys, estimating 66,900 to 83,625 SMEs (2006). Without access to the method for calculating 987,480 businesses, it is not possible to determine the validity of the FinScope estimate of 60,671 SMEs.

⁴ A micro-enterprise with four employees plus owner becomes a small enterprise; one with 19 employees and owner is a medium-enterprise.

many businesses, including agri-businesses. This is followed by unpaid employees (22.2%) including family members, and full-time (paid) employees (16.0%). Those paid in kind are likely to be family members and temporary task-based workers paid with food ('ganyu'), which is a common arrangement. Across small enterprises, the pattern is one full-time and one part-time paid employee, two temporary paid, one paid in kind and two unpaid.

For medium enterprises, the structure of employment is very different with full-time (paid) by far the most common form of employment (47.5%), followed by temporary (paid) (14.6%) and part-time (paid) (13.4%). For medium enterprises, the pattern is approximately 15 full-time, nine part-time or temporary and approximately eight others paid partly/fully in-kind. This suggests that medium enterprises have more formalized employment and less predominance of family members within their overall workforce.

In the primary research, 38 (59%)⁵ of ASMEs had temporary/seasonal employees, while 50 (75.7%) employed family members, typically with flexible payment. This could result in no payment in certain periods for family members.

An important issue is whether to count employees in businesses with the same ownership. FinScope (2012), respondents answered only for the business in which they spent most time, thereby excluding employees for other businesses under common ownership. This method results in understating the employment in that owner's related businesses; by not considering them as a unified business portfolio, enterprises appear smaller than they are in practice. Although this issue of 'portfolio' business ownership does not answer the question of Malawi's 'missing middle',⁶ it may be part of the explanation.

1.2.2 PORTFOLIO OWNERSHIP

Multiple business ownership as a 'portfolio' is common; it enables owners to manage cashflow, manage risk and manage growth between the different businesses.

FinScope (2012) found multiple enterprise ownership, with an estimated 987,480 MSMEs⁷ owned by 760,000 owners.

Table 3: Number of Businesses Owned by SME Owners, 2012

How many businesses with less than 100 employees do you own? (A1a) ⁸	% of small enterprise owners owning....	% of medium enterprise owners owning.....	% of all SME owners owning....
1 business	65.7	62.5	65.5
2 businesses	29.6	25.0	29.3
3 businesses	4.6	12.5	5.2
4+ businesses	0.0	0.0	0.0
Total	100.0	100.0	100.0

Source: FinScope (2012) database – consultant's analysis

⁵ Percentages are of total respondents (68) for each primary research question, excluding did not know/respond and not applicable. Percentages are to help comparisons, rather than for extrapolating to the whole ASME population.

⁶ This refers to a perceived large gap in firm numbers in the small/medium sized category, between the micro and large enterprises categories.

⁷ The FinScope (2012) report does not provide the basis for these estimates, so the split for SME ownership cannot be extracted.

⁸ FinScope requires that over 50% of what the business makes or does should be sold to exclude subsistence farmers.

Across all SMEs, 34.5% of respondents said they owned more than one business (FinScope 2012). The primary research found that 41 (62.1%) of ASME owners had more than one business, with eight owners identifying that they owned six businesses or more. The operation of multiple businesses as a ‘portfolio’ was not only common, but a deliberate strategy for *managing cashflow*, *managing risk* and *managing growth*. These three sub-purposes⁹ fit a strategy of dealing with the immediate (cashflow), limiting the ‘downside’ (risk) and taking the ‘upside’ (growth).

As a strategy for *managing cashflow*, 32 owners with more than one business moved capital (cash) from one business to another according to business needs and to avoid borrowing from formal or informal sources. Sometimes the need *related to a particular business problem*, for example a feed manufacturer (Dedza) had problems getting paid by Milk Bulking Groups (MBGs), which in turn were not being paid by the processor they were supplying. In other cases, owners were moving cash between businesses *to take advantage of different seasonal demand in different businesses*. For example a trader (Dedza) who buys soybean, groundnut and other crops (April to September), moves his cash from crop trading into cement sales from October to December, which is the peak period for small-scale construction. At this time, he also transfers capital into farm inputs for the planting season, which peaks at the onset of the rains. From January to March (the ‘hungry season’), he focuses his cash on stock for retail sales of food crops when prices peak, and shifts into grocery from April onwards when farmers receive cash from crop sales and want to buy groceries. This seasonal synchronizing of business activities is supported by the movement of cash to buy stock. This business owner has found a seasonal formula to utilize his scarce cash resources through a portfolio business approach.

A second reason for a portfolio of businesses was to **manage downside** risks. ASME owners gave examples in which one of their businesses was affected by an external factor beyond their control, such as government intervention on pricing or low production resulting in insufficient volumes for processing and trading. For example, GoM offered an attractive forward soybean price, making it difficult to buy at market rates for trading. In such situations, the owner moves capital and effort to other businesses not directly affected. 30 respondent ASMEs with more than one business were assessed to be managing risk in this way.

Finally, in the primary research, 27 owners used their portfolio to invest where growth was strongest. In this case, the portfolio was a means to test and try different businesses and markets to determine which were most attractive. For example, one trader (Dedza) disposed of a mini-bus to add capital in his trading business. Finding the best business was often trial and error, with owners making choices more based on the owner’s knowledge and ‘gut-feelings’, than on a more systematic analysis of the market and opportunity (or ‘business plan’). There was no evidence of formal market appraisals being undertaken;¹⁰ rather maintaining a range of businesses meant that owners could respond rapidly to new situations.

1.2.3 AGRI-BUSINESS SMES

ASMEs include the supply of inputs, services to farming/agri-businesses, trading produce, storing and transporting, processing and retailing farm produce. It is not possible to extract ASMEs from the FinScope categories.

Six categories of agri-business were identified through discussions with key informants:

1. Supplying inputs for farming and agri-business
2. Providing services for farming and agri-business

⁹ These were not necessarily explicitly stated, but were also discerned by the consultants from owner’s comments about their behaviors.

¹⁰ As noted in the lack of demand for Business Development Services. See 1.5.

3. Trading of farm produce in its original or partly transformed state (wholesale)
4. Storing and transport of agricultural produce in originally, partly or fully transformed state
5. Processing of farm produce into intermediate or finished products
6. Retailing of farm produce for consumption

FinScope (2012) categorized MSMEs into four economic sectors: Agriculture (44%), Wholesale/Retail (40%), Manufacturing and Construction (12%) and Services, including Transport (4%). However, it is not possible to disaggregate agri-businesses within these categories in the database, as the necessary information is not recorded. Agri-businesses could be in all four of these economic sectors. The consultants extracted categories from the FinScope (2012) data that were likely to be predominantly agri-businesses as follows:

Table 4: Categories of Agri-Business, 2012

Main Business activity	Micro	Small	Medium	%
Grow something and sell	14.0	43.9	9.7	15.4
Rear livestock/poultry and sell	1.7	1.9	1.8	1.7
Sub-total farming	15.7	45.8	11.5	17.1
Sell something in the same form that I buy from someone else	35.3	23.4	29.2	34.3
Sell something that I buy and resell in a different form by repackaging, re-grading or cooking	15.3	4.7	21.2	15.1
Process an agricultural product and sell it in a new form	2.3	0.9	0.9	2.2
Sell by-products of animals	1.8	0.9	2.7	1.8
Process an agricultural product	0.7	2.8	4.4	1.1
Sub-total – agri-business activities	55.4	32.7	58.4	54.4
Other	28.9	21.5	30.1	28.6
Total	100.0	100.0	100.0	100.0

Source: FinScope MSME (2012) database – consultant’s analysis

Based on the above five FinScope (2012) categories, 54.4% of SMEs were potentially agri-businesses. However, some of the categories such as ‘sell something in the same form that I buy from someone else’ cover trading in agricultural and non-farm goods, so not all enterprises in this category would be classed as agri-businesses. In addition, ASME owners in the primary interviews gave a combination of farming, trading, transporting and processing business activities under their ownership. Therefore the categories of ‘grow something and sell’ and ‘rear livestock/poultry and sell’ could also be run by owners with agri-business interests. It is difficult to extract the ASMEs total from the FinScope (2012) database in a reliable manner.

1.2.4 OWNERSHIP BY MEN/WOMEN

Men are more likely to own ASMEs than women. Ownership issues are to some extent blurred, as there are examples of female co-ownership of and co-operation in ASME portfolios.

The split of male/female respondents across MSMEs is set out in the table below.

Table 5: Proportion of Male/Female Respondents by Size of Business

Sample	Type of business			Total
	Micro	Small	Medium	
Male	50.0	76.9	75.0	51.6
Female	49.8	23.1	25.0	48.1
Missing (Male/Female)	0.2	-	-	0.2
Total	100.0	100.0	100.0	100.0

Source: FinScope MSME (2012) database – consultant’s analysis

In FinScope (2012), the proportion of male and female respondents for SMEs is similar to that for micro-enterprises; however male respondents were more common in small (76.9%) and medium (75.0%) enterprise categories. This is unsurprising and was supported by the difficulty in the primary research of identifying female-owned ASMEs. Only four (5.9%) out of 68 ASMEs interviewed were owned by women or husband and wife in equal co-ownership.

There were other examples where wives were actively involved, but short of equal co-ownership. FinScope (2012) recorded that 26.7% of businesses are jointly run, but without clarifying the exact nature of the joint operation and if it amounted to equal co-ownership. The primary research therefore found fewer female owned or co-owned ASMEs than FinScope, but this could be a function of the nature of the enterprises, such that female ownership and co-ownership is higher in non-ASME categories.

There are large-scale female wholesale traders, particularly in Lilongwe, who buy in some of the districts visited with (Mchinji and Mangochi were mentioned) through dealing with the mainly male district-level traders. One key informant indicated that there are smaller female traders, beyond the main centers, and the research team identified female representation in retail micro-trading at district markets, but not in district-wide trading.

1.3 SMES IN THE ZONE OF INFLUENCE

The seven target districts accounted for 25-30% of the FinScope (2012) MSME sample, with Lilongwe Rural and Mangochi more important and Balaka least important in proportions of SMEs. There were gaps/limited numbers of ASMEs offering warehousing/storage, services and processing in the districts, while agri-input supplying, trading, transporting and retail selling ASMEs were common. ASMEs rarely specialized in one crop, but tended to operate across several crops, as well as operating vertically across farming, inputs, transport and trading, as well as a mix of agri-business and non-agri-business.

This section provides a review of SMEs in the Zone of Influence (ZoI). The breakdown of MSMEs by district is shown in the table below.

Table 6: Proportion of MSMEs in the Target Districts, as % of National Sample

Target District	Micro %	Small %	Medium %	Total MSMEs %
Balaka	2.3	-	-	2.1
Mangochi	5.6	4.6	-	5.5
Machinga	3.6	1.9	-	3.5
Dedza	3.0	5.6	-	3.1
Ntcheu	3.7	0.9	-	3.5
Lilongwe Rural	8.7	6.5	-	8.6
Mchinji	2.7	9.3	25.0	3.1
All 7 Districts (% of the total)	29.6	28.7	25.0	29.5
All Districts	100.0	100.0	100.0	100.0

Source: FinScope (2012) database – consultant’s analysis

In total, the seven target districts accounted for 29.5% of the FinScope (2012) sample, 28.7% of small enterprises and 25.0% of medium enterprises. Lilongwe Rural and Mangochi have a higher proportion of MSMEs than the other five districts, reflecting their size and population densities. As FinScope (2012) was a MSME study and as micros are by far the most common category of enterprise in Malawi, then the representation of medium and, to a lesser extent, of small enterprises in the sample is inevitably limited.

The primary research on SMEs in the seven ZoI districts resulted in interviews being conducted as shown in the table below.

Table 7: Sample of SMEs in Qualitative Research, 2014

Target District	Small	Medium	Total
Balaka	9	-	9
Mangochi	6	3	9
Machinga	5	2	7
Dedza	8	-	8
Ntcheu	10	1	11
LL Rural	8	2	10
Mchinji	11	2	13
All 7 Districts (% of the total)	57	10	67

Source: Consultants' primary research

A total of 58 small- and 10 medium-enterprises were interviewed across a range of value chain functions, including input supplying, trading (wholesale), transporting, processing and trading (retail).¹¹ The total for medium enterprises exceeded the total in the FinScope (2012) sample, while the number of small enterprises was over 50% of the FinScope (2012) sample. As FinScope (2012) covered all types of businesses, including non-agricultural/agri-business, and other agricultural value chains, the primary research sample is more comprehensive in its ASME coverage. In addition to the ASMEs, 68 micro-enterprises were interviewed to find those with 2-4 employees in order to shed some light on the transition from micro- to small-enterprise as well as to understand target chain activities.¹²

Gaps in the categories of ASMEs interviewed in the primary research were identified as: no SMEs renting out warehousing were found; only four SME processors; and, one service provider to agriculture and agri-business identified in the three target value chains. The most commonly identified ASMEs were transporters and traders, followed by agro-input dealers, though these were commonly part of a portfolio of businesses under common ownership.

From the primary research, certain value chain functions are concentrated in the Districts, while others are more concentrated in the urban areas. District activity is focused on farming, supply of farm inputs¹³ to support production, as well as buying, aggregating and transporting farm produce to urban areas. There is also retailing of farm produce to District consumers. By contrast, processing is concentrated in urban areas for domestic and export sales.

There were many combinations of businesses within and outside the target value chains. For example, traders not only traded in both groundnut and soybean, but they traded in other common crops for that locality, such as maize, pigeon peas and/or beans. The combination of crops depended on the locality due to different production patterns. In addition, traders often sold or had related businesses for farm inputs and transport.¹⁴ Finally, 31 (52.5%) ASME owners had completely unrelated businesses, e.g. a dairy farmer, who packages his milk for retail sale, also has a fuel station and a grocery shop (Mangochi); a transporter of crops had a clothes

¹¹ The totals of each are provided in each section, with the caveat that there was a pattern of ownership of multiple agri-businesses (see 1.2.2).

¹² These were not in-depth interviews compared to the main target group of ASMEs and are therefore not reported directly.

¹³ Such as seed, fertilizer, chemicals and veterinary drugs.

¹⁴ These were sometimes sold from the same premises, but also through other related businesses.

shop, a stationery shop, a chicken feed shop and was farming soybean (Mangochi). The key point is that there are many combinations of businesses.¹⁵

Because of the business portfolio approach that is adopted, it is not helpful to think of a groundnut, soybean or dairy SME; rather it is more useful to think of a SME owner with a portfolio of businesses some of which handle soybean, groundnut and/or dairy products. This has implications for modeling impact from Feed the Future (FTF) supported increases in production, as there are few SMEs that specialize in only one function in one of the three value chains.

1.4 TARGET VALUE CHAINS

The three FTF value chains are reviewed in turn, with groundnut and soybean grouped together, followed by dairy:

1.4.1 GROUNDNUT AND SOYBEAN VALUE CHAINS

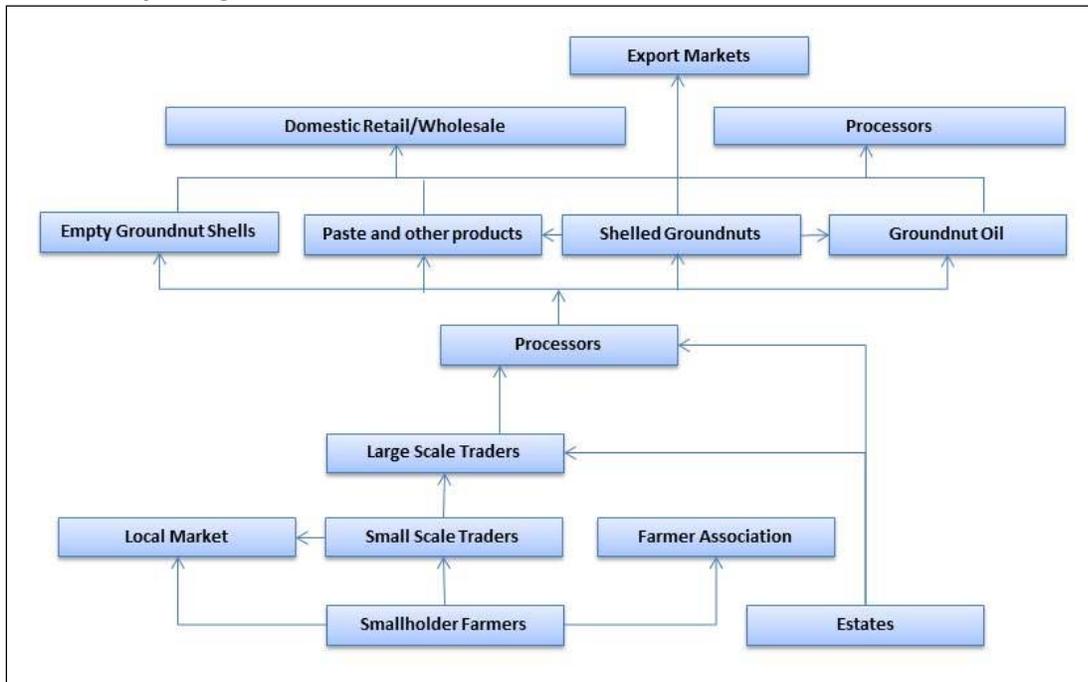
Specialization in groundnuts or soybean was not common, except among traders in Mchinji. ASMEs respond to market and environmental factors moving into and out of these and other crops according to circumstances. Soybean and groundnut were less common in hotter dryer districts for agronomic reasons (Balaka, Machinga (parts) and Mangochi). Demand for warehousing is very seasonal and there is plenty of available space, even if most is not purpose built for storage. Processing of these crops tends to require more investment in more complex equipment, than some other crops e.g. sunflower, so it is mostly absent. The groundnut trade in Mchinji is international and traders and related suppliers have grown relatively large and specialized compared to crops in other Districts. The groundnut trade is more stable than soybean, partly due to absence of GoM interventions in the former compared to the latter.

The information on ASMEs with groundnut and soybean related business activities is combined, as the primary research found that value chain participants deal in both commodities without specializing. Their decision to trade either or both crops depends more on availability and the owner's assessment of market potential, which varies from year to year. As a result, they move into and out of groundnut and soybean as circumstances dictate, particularly soybean due to price volatility partly caused by GoM interventions.

Groundnut and soybean grow in similar agro-ecological zones, so farmers can and do substitute them when making their planting choices. These are widely grown crops, particularly across Central Region. Mchinji is the main groundnut producing district in Malawi, while Dedza is more important for soybean. Production of soybean and groundnut is more limited in the lower, hotter and dryer districts such as Balaka, Mangochi and low lying areas of Machinga. In these districts, more drought tolerant crops like cotton and pigeon peas are more common. Simplified value chains for groundnut and soybean are set out below.

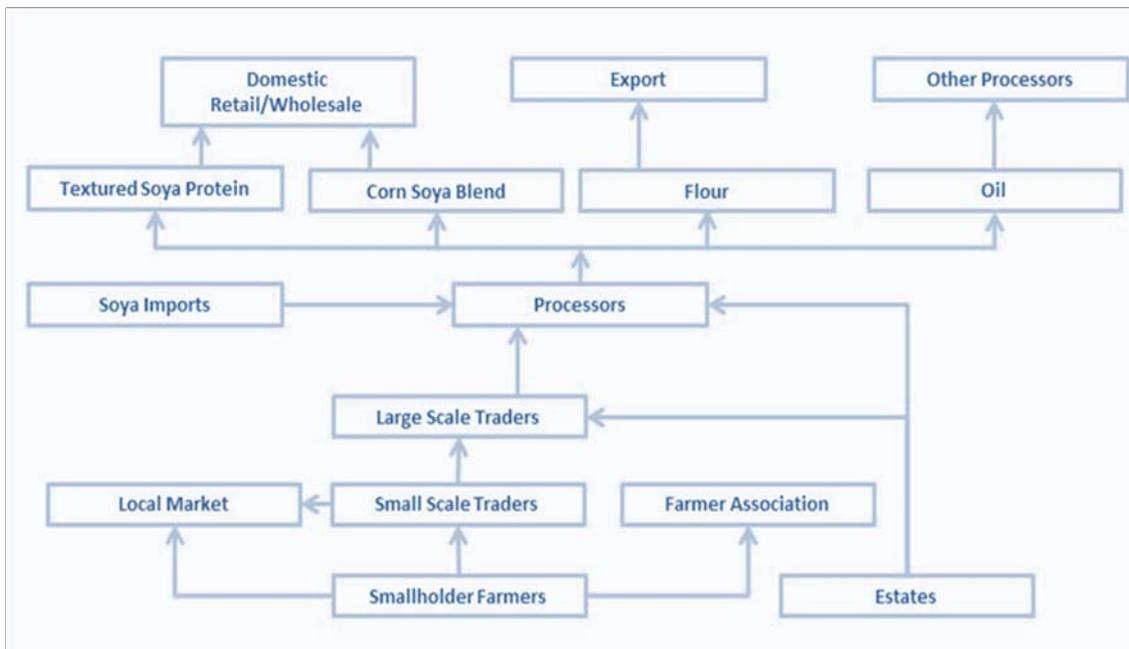
¹⁵ Complimentary products were often integrated, like farm inputs and buying produce, while those that were very different were in different premises/outlets, like grocery and wholesale trading.

Table 8: Simplified groundnut value chain



Source: Kadale/Imani/Tetra-Tech ARD, Malawi Vulnerability Assessment, Groundnut Value Chain Analysis (2013)

Table 9: Simplified soybean value chain



Source: Kadale/Imani/Tetra-Tech ARD, Malawi Vulnerability Assessment, Groundnut Value Chain Analysis (2013)

Both chains are similar at the district level, as input suppliers, traders (wholesale) and transporters supply, buy and transport groundnut and soybean, as well as the other crops prominent in each district, without clear specialization. Although the inputs differ to some extent,¹⁶ there are no special facilities required for trading and transporting either crop, which makes it easy to move into and out of these crops. The only specialization was in Mchinji where the traders focus primarily on groundnuts as the trade is strong, attracting international traders. Groundnut has generated consistently good returns for these traders and is less prone to interventions by GoM, such as the export restriction and purchasing initiatives that have disrupted the soybean market.¹⁷

Before discussing the categories of value chain players that were present in the districts, missing or scarce value chain functions are reviewed being warehouse providers, service providers and oil processors.

Warehousing providers – The field research team searched for SMEs that had invested in warehousing¹⁸ to rent out as a business. Three medium sized groundnut traders had invested in large¹⁹ warehouses in Waliranji (Mchinji) for their own exclusive use and one trader in Ntcheu had built a relatively small warehouse (50MT) for its own use. There are two large houses in Mangochi that the (SME) owners aim to rent out for storage, such as to seed companies. One medium animal feed processor (Dedza) had rented out spare warehouse space to a NGO, but this arrangement had ended. However, no purpose-built SME-owned warehousing for rent was identified in any ZoI District.

There were a few NGO and large enterprise investments in warehousing identified as:

1. Save the Children built five warehouses in Mangochi (100MT+ each) which are currently not used
2. CADECOM is building a warehouse in Dedza, but it is not complete and presumed to be for its own use
3. A large company (MANICA) (Balaka) had a warehouse for rent to other businesses

All the traders interviewed had access to storage space, typically at the rear of their shops. Traders stated that when they needed extra storage, it was possible to rent empty business premises or even private houses in District centers. Traders also store on their verandahs and at home. In Balaka, Mangochi and Machinga, traders reported storing produce in the open under a tarpaulin, relying on the low risk of rains. Traders said that they only need additional storage for 1-3 months after the peak buying time when their own space is insufficient; renting was more efficient than investing in a bigger space that would be under-utilized for three quarters of the year. Although traders do continue to buy and sell produce into December, they manage this within their existing space, as that is more cost efficient than renting more space. These factors explain why traders do not want to take leases beyond a few months and why there is therefore limited attraction to invest in warehousing for renting out, as the market is highly seasonal and space is not difficult to find. The conclusion is that storage space is not a constraint to agri-businesses.

¹⁶ Obviously on seed, but also soybean needs inoculum to improve its productivity.

¹⁷ An example of this has been the impact of the PIPHR announcing it would buy soybean at MK600/kg in the 2013 buying season, but failing to do so. This confused the market, as traders could not buy from farmers at such a high price, and if they were able to secure supply, then they were unwilling to sell it waiting for the promised purchases at MK600/kg, only to eventually realize that it was not going to happen and have to sell their stock at around MK170/kg. This has led many traders to avoid soybean for the last season. One farmer met during the research summed it up by stating his disappointment at the prices and that he was not growing soybean again.

¹⁸ Warehousing refers to any storage space, whether purpose designed or otherwise. Often trading outlets had a retail frontage and a large back room which was in effect the storage space for the enterprise.

¹⁹ Greater than 1,000 MT.

Service providers within the value chain²⁰ – These could include engineering and vehicle mechanic services, as well as business services such as accounting. Engineering services were not identified in the Districts, as processing is not generally present. There were accountants in some District centers, but these do not focus on the target value chains or even agri-business more generally. The only service providers identified were vehicle mechanics operating in District centers; however, the transporters with multiple vehicles stated that they take their vehicles to the city or bring a mechanic from the city if they need complex work doing, such as on diesel engines, as this was beyond the capacity of District level service providers. There are missing higher level vehicle mechanic services in ZoI Districts.

Processors – Oil processing can utilize different legumes such as soybean, cotton seed and sunflower. Groundnut can also be pressed for oil, but there is strong demand for whole groundnut so oil from groundnut is relatively expensive and less attractive. Soybean is more difficult to process than cotton and especially sunflower, so it requires more specialized plant, such as exists at Sunseed and BERL in Lilongwe. As a result, most oil processing takes place in Blantyre/Limbe and Lilongwe. One oil processing plant was identified in Mangochi, owned by Italians and mainly buying sunflower not soybean/groundnut. There is a sunflower oil processing plant in Mchinji District (Mkanda).

There was one animal feed processor in Dedza which buys soybean. Groundnut is processed into flour and cooked for retail sale at a micro-enterprise scale, but was not identified at SME level. Overall, processing is a relatively scarce function in the Districts and mainly small scale if it exists. This may be a function of economies of scale due to access to bigger markets for urban-based processors. Where there are opportunities, these could be for poorly served markets for oil, but mainly from sunflower, which is cheaper than soybean and groundnut, and is limited to the areas where it is grown and easiest to process.

Turning to enterprises that were found, ASMEs were identified as undertaking the following chain functions:

1. Supplying seed, pest and disease management (PDM) chemicals²¹ and equipment²², tools, fertilizer and packaging material, mainly sacking (*Input suppliers*).
2. Buying and aggregating stock for sale to larger traders, processors and exporters (*Wholesale traders*)
3. Moving produce from rural areas to the district/trading centers (hired by farmers), and transporting aggregated stock from trading centers to large (urban) buyers for trading, processing or export (*Transporters*)
4. Supplying produce for consumption by District-level consumers (*Retail traders*)

Input suppliers – A total of 28 input suppliers were identified across the seven Districts, with high concentrations in Mchinji and Mangochi, but few in Lilongwe Rural and Dedza. It is important to note that input supplies are also available from the branches of national companies like Farmers World, Kulima Gold and Export Trading; these were excluded from the research as they are not SMEs, even if they are commonly present and significant players in the District level value chain. Of the 28 input suppliers, two were seed producers/multipliers (Funwe and Pindulani, both in Mangochi) and the rest were agri-input dealers selling a mixture of seed, PDM chemicals, tools and fertilizer.

Three agri-input dealers in the primary research (two in Mchinji and one in Balaka) had multiple outlets. The majority of agri-input dealers were also traders, buying commodities (wholesale) and engaging in seasonal retail sales. These had a complimentary set of activities that enabled them to change focus depending on the

²⁰ Excluding Business Development Service providers – see later.

²¹ Pesticides, fungicides and herbicides.

²² Sprayers and protective wear/equipment.

season. These agri-input dealers/traders saw the supply of inputs as a means to persuade farmers to sell their produce to them, as ensuring farmers get inputs creates loyalty and an obligation to sell the produce to the input provider. There are issues with the availability of inputs, so a 'loyalty loop' involving more assured access to inputs in return for supplying produce is a credible strategy. This was reinforced by some input suppliers stating that they provide loyal farmers with credit for inputs. More evidence would be needed through farmer interviews to verify this.

One major complaint of agri-input dealers was that the larger national firms were able to import inputs directly and sell at more competitive prices, making it more difficult for SME agri-input dealers. This was linked to statements about large foreign firms and small Malawian firms, with a plea to GoM to restrict larger suppliers. This suggests that agri-input SMEs find it difficult to compete with larger firms. In Mitundu, the agri-input SMEs were organizing into an area based association to lobby GoM on this type of issue. Such competition issues are beyond the scope and to note that this is the view from one perspective and did not include that of farmers or the larger firms.

Agri-input dealers highlighted that low demand can result in stock going out of date, particularly at the end of the planting and growing season. This may also be a function of poor purchasing (over-stocking) and/or poor stock control (poor rotation). The incentive for agri-input dealers is to under-stock and so never to be left with out of date stock that cannot be sold, even if this meant loss of sales if they had been more optimistic in stocking. There is out of date stock in the system and this is commonly sold, rather than write it off and dispose of it.

There was a linked issue of poorly performing inputs due to agri-input dealer sales to micro-vendors who then tampered with the contents, through dilution or substitution; the blame for poor performance can come back to the agri-input dealer as the local agent of the firm that originally supplied the product. There was a reported problem of counterfeit goods and fake seed that was undermining the market.

It was interesting to discover, particularly in Mchinji, that there are many more varieties of PDM chemicals available than are approved in Malawi. Zambia and Tanzania are a source of these imported chemicals, as is South Africa. Tanzania was stated to be the source of many counterfeit chemicals. Chemicals were transported on minibuses, as the physical volume is small, so dedicated transport would be too expensive and unnecessary.

One source referred to buying over 10 types of herbicide from Zambia, presumably unapproved for use in Malawi. These are approved for use in the other countries, but Malawi reportedly takes a relatively restrictive view in approving/licensing chemicals for use. That may benefit the few suppliers with approved products, but it limits farmer' choices, so some people have identified the opportunities for 'informal' imports to satisfy demand.

There is informal cross-border trade in fertilizer with Mozambique especially at Ntcheu and Mangochi. Mozambican traders bring fertilizer to the border, and sell to Malawian agri-input traders at wholesale prices. This is a better alternative than travelling to Limbe/Blantyre or Lilongwe to buy fertilizer at wholesale rates due to lower transport costs

Agri-input SMEs highlighted distortions in the fertilizer and seed markets over recent years, due to the Farm Input Subsidy Program (FISP), which has undermined the private sector input supply market, making it less attractive and concentrating outlets in more central locations. This is an example of the downside risks that reinforce the need to have more than one business activity to cope with changes in the market or business environment that are beyond the business' control. FISP has led to diversification out of agri-input supply.

Wholesale traders – ASMEs in this category buy a range of crops from individual farmers and from micro/small traders who consolidate at village and smaller market levels. The driver over which crops to buy is whether the trader has a market for the crop. Typically, the traders in the ZoI sell to bigger traders in the same locality (small to medium and medium to large/national), or to a processor, national trader or exporter in Lilongwe or Blantyre/Limbe.

37 ASME traders were identified in the primary research, of which three had more than one outlet (Mchinji and Balaka). This is unlikely to be all the ASME traders as not all the centers in the Districts were visited, but through asking identified ASME traders who their main competitors were, most of the ASME traders were identified. Most were trading both groundnut and soybean.

The key to successful trading is to build stock quickly to a size that is economic to transport (20-30 MT) or attractive to buyers at the next level in the value chain. The aim is to sell the stock, get paid and build stock again as quickly as possible. This way a trader turns over its limited capital quickly, making a margin each time, with the incentive is to turn it over as many times in the season as possible.

To achieve this, the ASME traders establish buying points in high potential rural areas to attract farmers through making it convenient to sell, as well as opening outlets in other trading centers. One trader has two outlets in the same location, explaining that the one on the periphery is there to catch farmers as they come into town, since having cycled or walked with a heavy load, it tempts them to sell at the first place they reach. Other traders talked about creating loyalty through supply of inputs. Another area of claimed advantage was being fairer with the scales. Cheating on scales by traders is common, as is farmers wetting produce, hiding poor quality and adding other matter to make up the weight. Traders get different reputations, but many claimed to be offering a fairer deal by not manipulating scales. Some traders suggested that electronic scales gave them an advantage, as they were tamper proof.

Traders were quick to change tack by buying different commodities if they could not match prices offered by a large trader or GoM supported body, or due to some other dislocation in the market, including oversupply and falling prices. Therefore, although there were specialist traders in groundnuts in Mchinji, due to its particular dominant position, in all other locations the traders did not specialize in a crop. The implication is that it is difficult to invest specifically in 'groundnut traders' or 'soybean traders' as the traders move in and out of crops.

As well as traders building a portfolio of agri-inputs, trading and retail sales of food commodities, (maize and beans), two common investments by traders were in their own premises and in their own transport. The rationale behind these complementary investments is for cost and business control. Premises and transport are major costs other than stock; therefore, the trader wants to control these and capture any margin that is in the rent and the transport. In addition, if the premises are not its own, the trader does not want to invest in improvements, such as security bars, lighting or ventilation which are important for risk reduction.

On transport, not having control of a vehicle can mean that transport is not available at the time and convenience of the trader, resulting in missed opportunities. Also, the risk of theft of produce en route means the trader has to put his own people on the vehicle anyway, which is an additional costs compared to employing his own transport team. If the vehicle is not owned by the trader, he is unsure how well maintained it is and breakdowns can be costly in terms of hiring alternative transport and collecting goods from a broken down

vehicle. Controlling premises and transport therefore enable the trader to reduce business operation risks, and capture any profit in these business functions.²³

There is a very active groundnut export trade from Mchinji. Traders are coming from all over Southern and Central Africa to source Malawi's groundnuts, which are highly valued.²⁴ One trader was sending out six trucks (30MT) per month to a customer in the Democratic Republic of Congo (DRC). It is unclear how much is formal or informal trade, but larger vehicles are difficult to move informally. It is this volume of trade that supports specialization by traders in Mchinji in groundnuts, in a way that specialization is not seen elsewhere. Although there are risks in specializing, the returns are presumably too good to pass up compared to diversifying into other business activities.

Transporters – Transporters were relatively easy to identify and count, as the practice is to have vehicles on a transport rank at visible locations. Due to the sheer numbers of vehicles, some assumptions had to be made about ownership and employment based on a discussion with drivers and identified owners for their estimates of how many owners had more than one vehicle. As each vehicle has a driver and a driver's mate, then the owner of two vehicles could be classified as a small enterprise. In total, an estimated 188 small and 6 medium transport enterprises were identified, spread across all seven districts, with 15 interviewed in the primary research.

Transport owners usually had farming or trading businesses that had led them to want to have their own transport to capture the margin in transport and to get greater business control. In the transport 'ranks',²⁵ the sizes of vehicles varied. They owned different sized vehicles so that if they got a contract, they could send the smallest necessary vehicle to be efficient.

There were specialized transport operators who had built a fleet of six or more vehicles. To get to this level requires an ongoing contract with one of the large buyers/processors to keep such a fleet busy, as it is not viable to carry such a high level of capital tied up and rely on picking up contracts day by day at the transport rank. One transporter in Mangochi had six 20/30 MT trucks that were contracted by a tobacco company, giving him a core contract. For the more specialized transporters, as well as having more vehicles, these had to be of a much better standard than those on the transport rank and generally were larger vehicles for efficient national carriage. These transporters also need to ensure compliance, as their vehicles are regularly stopped on major roads and in the city, whereas the trucks hired day by day get by with lower compliance standards and missing licenses. Finally, specialized transporters go to Lilongwe or Blantyre²⁶ for non-routine vehicle maintenance, as the skill base of mechanics in the districts is insufficient to maintain the higher standard of vehicles.

Traders and farmers that also own vehicles put them on the rank to pick up occasional contracts to utilize the vehicle. Vehicles were rarely designated for a particular use; rather they could carry any type of crop or non-agricultural goods. Transporters did not specialize by goods carried, unless they had a long term contract.

Transporters were concerned about fuel prices as they had to quote in advance, but could find a major increase overnight, as the fuel price is linked to the MK:US \$ rate. Fuel shortages were not mentioned, as the

²³ The use of premises for collateral is discussed in the section on access to finance.

²⁴ Angola, Zambia, Democratic Republic of Congo were mentioned as places where buyers come from. Groundnut is also going to Tanzania.

²⁵ All the centers visited had at least one location where trucks for rent were waiting for customers, in a 'rank'.

²⁶ Or get a mechanic from the city to come out to them.

period where this was an intense problem has passed. For the specialized transporters, getting a Certificate of Fitness was a major issue, as delays at the Road Traffic Department meant vehicles were off the road and losing money for the business.

Traders (retail) – Most of the wholesale traders also engaged in retail trading, selling to any consumers who came to purchase. This is not their main business, but an easy addition, as the stock is on hand and the margins for consumer sales are higher when sold in small quantities. In addition, to retail sales throughout the buying season, they also use stock bought at the end of the main buying season (around November) to sell in the hungry months of January to March. Although there are large potential price gains to be made by buying early in the season (April/May) and holding stock for sale in January to March, there are price risks in doing so. Prices do generally rise through the season and rise more sharply as produce is exhausted in January/February, but prices are not guaranteed to rise.

For the trader, although the margin on stock purchased early season for sale in late season appears large, there are incremental costs with storage, notably financing costs, labor/security, the need for chemical treatment and losses through additional drying, losses to pests that increase progressively with time, compared to selling stock as soon as possible, then replenishing with fresh stock. Overall, the margins from turning stock over quickly compared to buying and holding stock, appear to be more attractive and less risky.²⁷ Turning over stock also gives the trader flexibility to invest in other opportunities that arise and that might be more attractive, compared to tying up the trader's capital in stock for 8-10 months at a time.

One trader in Dedza also had an outlet in a major township in Blantyre as a separate business, which he supplied with stock from his trading business. Demand for commodities is stronger in urban areas, as is the amount of available cash for purchases; so even with the transport cost, the trader makes a better return than retail sales in Dedza. This district-urban link also created another opportunity, as this trader received stock from other traders, who recognized that he could get far better prices than they could in Dedza. So even though they compete for buying and selling in Dedza, the other (small) traders would deposit their stock with the trader for him to sell.

Of additional interest, the first trader gives the other traders a commitment on forward selling price and the depositing traders agree to be paid in March at the end of the season. The first trader therefore had more stock to sell with potential economies of scale in transport, as well as credit for 3-4 months. In return, he gave the depositing traders a better price than they would have got by local sales and he assumed all the price risk (and gains). This was a sophisticated trading arrangement, financing, risk management and collaboration for mutual gain. It is not a Warehouse Receipt Scheme (WRS), but it is a form of stock futures management requiring considerable trust and calculated risk.

Some traders had reached stock sharing arrangements with other traders, so if one had an order to fulfill but insufficient stock, the others could supply it and share some of the profit. In Mchinji traders share stock, which has to be returned as stock. Collaboration also extended to transport for buying inputs and moving goods to urban markets.

²⁷ If selling prices fall, then the buying price can also be brought down, so the trader always makes a margin compared to buying at one price and not being able to change buying prices according to the market changes.

1.4.2 DAIRY

Dairy was a much smaller value chain than soybean and groundnut. The main ZOI activities were inputs to dairy farming (breeding, feeding and servicing) and consolidation through MBGs. Transport was managed by the urban based processors. The selling of milk by commercial farmers in district centers has become more common, due to the good prices compared to the formal chain via MBGs. There have been problems at MBGs due to the collapse of MDI resulting in loss of payments, and from poor management at some MBGs, such that ancillary suppliers, such as feed producers have had to scale back or change their business focus.

The data from this section is drawn from the interviews in the districts as well as meetings with milk producer associations and other value chain players in Lilongwe.

Milk Production

The dairy sector is built on milk production, much of which occurs in the districts. There are higher concentrations of milk producers and related MBGs around Lilongwe City, which is a ready market for all the milk produced in Lilongwe Rural District. MBG producing members typically have one or two cows, making them farming micro-enterprises. In addition to MBGs and micro-producers, there are some commercial-scale farmers with at least 10 pure or cross-bred dairy cows in all seven districts. Five of those interviewed were involved in agri-business activities, such as breeding, feed production and retail sale of milk, including a commercial farmer in Mangochi who was bottling unpasteurized milk for sale in the town.

The commercial farmers in Ntcheu, Balaka, Machinga and Mangochi reported shortages of milk supply relative to demand in the Bomas of their districts. One commercial farmer expressed bewilderment as to why others had not invested in milk production due to the high level of demand. However, he also discussed the many challenges of running a dairy herd, particularly the access to good services (veterinary, artificial insemination (AI)), drugs and feed.

Dairy farming needs good support and a ready local market. For micro-producers, a well-functioning MBG provides this access to services, drugs/feed, training and a market; but without a MBG or if it does not function well, then micro-producers face considerable difficulties with the risk of losing valuable dairy cows if not properly supported. The commercial dairy farmers have more experience and resources to access inputs without a MBG. All the commercial farmers reported demand for all the milk they can produce in the Districts, as there is little competition from micro-producers or other commercial dairy farmers. Although packaged milk from city-based processors is available in district centers, the prices are much higher, due to processing, packaging and distributing costs, compared to the sale of raw unpasteurized milk²⁸ delivered directly by local commercial dairy farmers to users.

Value Chain Players

The value chain functions in dairy were identified at district level as:

1. Providing services for farming, notably veterinary and AI, accessed mainly through MBGs by small producers and directly by commercial producers
2. Dairy cow breeders are present, but due to the research focus, only one breeder was identified (Dedza)
3. Supplying inputs for production, such as drugs, dips/sprays and feed through MBGs and agri-vets

²⁸ Sales of unpasteurized milk are banned in urban areas, but not outside the four cities.

4. Wholesaling/trading as a function is undertaken by MBGs
5. Selling milk for consumption at home and to institutions was identified in all districts apart from Lilongwe Rural, being undertaken by commercial farmers
6. The following functions were limited or absent:
7. Transporting milk was absent, as collection of milk is organized by the urban processors
8. Processing milk into packaged processed milk as a consumer product was only found in one (catholic mission related) cheese-maker in Balaka.²⁹ The other was the bottling of unpasteurized milk for retail sale (Mangochi)
9. Processing feed – one feed processor was identified (Dedza), with another just within Lilongwe City boundary

In terms of the *missing and limited functions*:

Transporting milk – This was absent, other than by commercial farmers who use their own transport to reach District-based customers. Commercial farmers control transport, to avoid reliance on another party's transport with a higher risk of loss if that vehicle was allocated to some other task or was not well maintained and broke down.

Processing milk – Milk is a versatile raw material that can be processed into liquid milk (pasteurize/heat treat/fermented/buttermilk/flavored etc.), yogurt, cheese, butter, ice-cream and combined milk/non-milk products. However, as a perishable product, it requires immediate processing and quick sale. The demand for liquid milk is mainly met from unprocessed 'raw' milk direct from producers to consumers and demand for milk products beyond liquid milk is limited. The sale of unprocessed liquid milk is banned in urban areas, but not beyond the cities, so unprocessed liquid milk is available in District centers and is much cheaper than packaged processed milk. The market for District-level processed milk is likely to remain limited with competition from the large urban processors.

Processing animal feeds – There is one dairy feed processor operating from Dedza and another just within the Lilongwe City boundary. Both received support from USAID through the Malawi Dairy Development Alliance (MDDA) project and one through the USADF program to support processing and capacity development. In both cases, the processors reported that their dairy feed business had deteriorated due to payment problems with MBGs which in turn partly stem from poor payment by the now closed Malawi Dairy Industries (MDI) factory in Lilongwe. The latter had failed to pay on time for milk from MBGs for several years, ceasing around December 2013. As a result MBGs supplying MDI have not paid members in full or to pay suppliers, like the animal feed processors.

There are still MBGs that buy dairy feed, particularly those supplying Lilongwe Dairies. However, feed processors also noted that some MBGs had considerable arrears due to poor management. The feed processors stopped supplying these MBGs or required cash payment, but supplied other MBGs on credit due to their good payment records.

In response to the fall in demand from MBGs, one feed processors had laid-off workers and was focusing more on related businesses, such as an abattoir/meat processing and breeding, while the other focused on poultry feeds which were growing well and had vertically integrated into producing oilseed cake as a raw material source. The bi-product of this was vegetable oil that was being packaged and sold to consumers. This

²⁹ The Balaka Best Company primarily produces cheeses (100kg to 150kg per day) and buys milk from Toleza farm (commercial dairy farm).

diversification into alternative businesses illustrates the earlier points about portfolio businesses and how owners respond to uncontrollable risks.

Turning to the value chain *functions present in the districts*:

Services to farmers – Small producers access AI and para-vet technicians through MBGs. Veterinary services beyond very basic work are mostly provided by government officers doing private jobs. The challenges with AI services and related semen and liquid nitrogen supplies are documented in secondary sources.³⁰ Following a period of disruption, these services are now more available, but still with supply gaps.

Higher level veterinary services come from a Lilongwe based qualified vet, who travels to districts on request, primarily for commercial farmers. The absence of higher level service in the district adds cost and increases vulnerability to loss of animals.

For the commercial farmers, who sometimes have cooling facilities/refrigerators, there is a need for electrical technicians, who are generally available. Usually farmers manage their own transport.

Dairy cow breeders – The supply of dairy animals constitutes a key input for the dairy sector, which currently constrains growth. Two dairy cow breeders (Dedza³¹ and Mangochi) were identified and interviewed. The Dedza breeder buys supplementary animals in, but the cost of formal loans means that they do not borrow for this which constrains the number of animals they can buy. As well as breeding, the business sells milk, which provides regular income compared to the irregular large sums from sale of calves. Commercial dairy farming and breeding are integrated for this cashflow reason and that the opportunity for milk sales in district centers is good.

USAID has supported breeders in the target districts through the MDDA program that were not interviewed.

Supplying inputs – MBGs act as a source of some inputs for their members, including feed and bull semen though their affiliated AI technicians. Some inputs are also available through the district agricultural offices. In addition, there are input suppliers in the district centers, notably Lilongwe Livestock Center (LLC) which has outlets in many districts (Mchinji, Ntcheu, Machinga) providing agri-vet supplies of drugs, sprays and other animal health products. Other than LLC, one pharmacy was selling animal health products alongside its human health range as a diversification (Mchinji). Animal health suppliers provide animal health products for a range of livestock and poultry and do not specialize in dairy animals, as demand is too small.

Interviews with one MBG and commercial farmers note that some drugs are not stocked by agri-vets as the level of business is low and Agri-vets are concerned to sell products within their shelf life than to overstock and risk high stock losses, due to the high unit cost of items.

Wholesaling/trading of milk – Bulking of milk is a key function in the value chain, as it is not economically feasible to collect from the farmgate, due to the very small average production of most producers, their dispersed nature and the poor quality of roads particularly in the rainy season. Therefore, producers need to bring the milk to a central point where the buyer can collect it from, and where it can be kept cooler through milk cooling facilities. 16 MBGs were identified and one other dairy farmer group.

With the support of GoM and development partners, farmer managed MBGs have evolved as the predominant model. These have a bulking tank(s) and in some cases, facilities to cool, such as through connection to

³⁰ Kadale, (2011) Land O'Lakes End of Project Review.

³¹ This is related to the animal feed business, also in Dedza, through the same co-owner.

electricity supply or a generator. The MBG agrees a contract with a processor, who collects the milk and pays the MBG monthly. Without a bulking center, it would not be viable for processors to collect milk from small farmers, and potentially not from commercial farmers unless there was a sufficient concentration of supply. Beyond MBGs, there is no scope for wholesaling of milk as the economics dictate that guaranteed off-take is required of all the milk and further handling at wholesale level risks significant losses through perishing.

Since 2011, the milk price paid by processors have been kept at MK 100-110/liter, yet inflation has been over 20%/year. The result is that farmers have been less able to buy feed and other inputs, and the declining real returns from dairy has led to reduced purchase of inputs and lower production. This reduction in inputs has affected the feed processors and input suppliers. Dairy value chain players gave the effects of inflation and devaluation as risk factors for their businesses (see section on insurance below). The effective real reduction in price paid to producers has been damaging for the MBGs and their producer members. It also led one commercial farmer to stop supplying his MBG and start direct sales to consumers in Dedza, for which he gets MK 200/liter. Pressure from low producer prices creates an incentive to sell outside the MBG through informal channels and further undermine the MBG.

As well as collection points, MBGs act as a mechanism for service provision to farmers, such as accessing AI services, para-vets and training. MBGs are also a source of dairy inputs, including dairy heifers through pass-on schemes and distribution of animals gifted by development partners, and feed. From interviews with dairy stakeholders, there are significant limits on the number of dairy heifers that are being passed on/distributed. The challenges with feed supply have also been noted, attributable to MDI ceasing to pay, but also to poor management in some MBGs.

From a SME classification perspective, the MBGs are farmer-owned groups, with some registered as Co-operatives, such as Chitsanzo in Dedza District. They are unlike the other SMEs in this study as they are collectively owned with most of the capital from GoM and development partners. Each MBG is run by an elected committee and function to varying degrees, often with governance and management problems. There is a lack of capital from members. In practice, the MBGs look to development partners and processors for ongoing support with investment. Development partners have also provided support for training of members in husbandry and some business skills.

Retail selling of milk – Most commercial farmers sold their milk direct to consumers or institutions. Some commercial farmers had gone beyond bulk supply by opening retail outlets and in one case, bottling unprocessed milk for convenient sale. These farmer-retailers wanted the benefit of the retail margins from the sale of their milk. In two district centers, the retail price for unprocessed milk was MK 200 (\$0.50)/liter, double the price paid by processors via the MBGs. The higher prices were a function of a relative undersupply in district centers; even at MK 200/liter retail, this was half the price of the packaged processed milk through normal grocery stores. With the high margins, it appears that retailing of unprocessed milk in bulk or packaged is likely to grow, due to its relative profitability.

Although not specifically identified, as they would fall into micro-enterprises, vending of raw milk by farmers and micro-vendors (‘hawkers’) is common in many trading centers. These provide competition to the commercial farmers and other retailers, but they are limited due to the poor reputation of hawkers for adulterating milk.

Overall, dairy is much smaller than soybean and groundnut value chains. The ZoI functions are limited, with little transport and processing, and unlikely to change, even with increased volumes of production. There are

players performing more than one function, such as commercial production, transport and retail. The perishable nature of milk incentivizes vertically integrated functions. Another reason for this is the gap between the processors' buying price and the retail price, which is exacerbated by shortfalls of supply in many of the district centers.

1.5 BUSINESS DEVELOPMENT SERVICES

Business Development Services (BDS) can include technical and business services that are part of the operational requirements of chain participants and services that are more developmental in nature. Examples of technical services are vehicle and equipment maintenance, and business services, includes accounting and taxation services and computer/information technology (IT) support. Services that are not part of the normal operational activities, but are 'developmental' in nature include one-off or relatively short-term interventions to develop/change strategic direction, build capacity, design a new product/business concept, etc. Possible services include consulting, research and training services around strategy review and development, organizational development and capacity building, design and piloting new projects, acquisitions/mergers and start-up ventures.

1.5.1 DEMAND FOR BDS

It was rare to find business, technical and developmental services in the districts, other than lower-level technicians (e.g. vehicle/equipment mechanics) and accountants, the latter serving more the medium enterprises. More developmental service use was occasionally found, such as training/capacity building and business planning (four cases in the primary research), but were only used by larger ASMEs and often with development partner support. Medium enterprises were willing to bring in providers from the city if needed rather than rely on low quality service in the districts, but even this was uncommon.

The following table from FinScope (2012) illustrates the nature of problems faced at start-up.

Table 10: Problems at Business Start-Up

<i>“What problems, if any, were faced with when you started or took over your business?” (B4)³²</i>	% Small	% Medium	% all SMEs
Sourcing money	48.1	50.0	48.3
Cash flow	0.9	-	0.9
Being owed money	4.6	12.5	5.2
Financial records	2.8	-	2.6
Registering business	0.9	-	0.9
Laws and regulations	-	12.5	0.9
Tax compliance	-	-	-
Who to sell to	3.7	12.5	4.3
Raising awareness	0.9	25.0	2.6
Too many competitors	13.9	-	12.9
Not enough customers	16.7	12.5	16.4
Problems with stock	13.0	-	12.1
Own lack of skills	7.4	-	6.9
Writing a business plan	-	-	-
Transport	17.6	12.5	17.2
Equipment	14.8	25.0	15.5

³² 'B4' refers to the question number in the original MSME questionnaire. These references are shown throughout, starting with a letter to denote the different section in the MSME questionnaire. The questions are reproduced in each table, as per the questionnaire.

Crime or theft by others	6.5	-	6.0
Other	17.6	37.5	19.0

Source: FinScope (2012), Consultant's Analysis

Sourcing finance (48.1% of SMEs) was the stand out problem; yet, writing a business plan, which is normally a requirement for bank finance, was not identified as a problem (0%). This may link to these businesses not starting with bank finance,³³ but rather trying to find start-up funds from their own, family's or friends' resources. The lack of concern about a business plan also limits the potential for such BDS providers.

Practical considerations like transport (17.6%), stock (13.0%) and equipment (14.8%) were the second most common problems, with markets (too many competitors (13.9%) and not enough customers (16.7%)) at around the same level. These statements of problems broadly fit with other surveys of business issues.

From the primary research, the only district based business services being used by ASMEs were from accountants. One accountant was providing payroll and monthly management accounts. There were two identified examples (Dedza and in Mitundu (Lilongwe Rural)) of accountants providing more than just their normal business services. In Mitundu, the accountant was offering strategic support to an agri-input business, while in Dedza the accountant had provided input to a business plan to raise finance. Both of the firms that use these services were medium businesses.

There was limited evidence of other BDS, such as training in management or other forms of capacity development. One feed manufacturer was getting support from USADF for consultancy help on a range of issues, including development of new systems alongside the investment in new plant with USADF funding. In Balaka, CNFA trained one of the agro-dealers in business management, storage, chemical application and crop management, which is a mix of technical and business training. In another case, an animal feed business supported by USADF had funds within the support package to pay for BDS help in developing accounting systems and internal controls. There were also examples of ASMEs getting accounting services from Lilongwe, such as a veterinary business (Mangochi).

More frequently, ASMEs rely on their own capacity or draw on their networks for information and advice from business 'friends' and family, as indicated by three agro-dealers in Ntcheu, Machinga and Mangochi.

It can be concluded that current demand for and use of BDS by District-level ASMEs is very limited, and that it is more likely to be used by medium than small enterprises.

1.5.2 NATURE OF BDS PROVIDERS

Providers of developmental BDS tend to be urban based and reliant on subsidy. They can be private, public or NGO sector providers. Both FinScope and the primary interviews found limited current demand for BDS. Evidence of service use was that it was low.

This section focuses on the developmental BDS providers, grouped by 'ownership' status into three broad groups: private sector BDS providers, public sector BDS providers, and development partner providers.

³³ See later. 25% of small businesses said they use money from another business.

Private Sector BDS providers

These are privately owned management or business consultancy firms that provide business advisory or development services. The majority of these firms are managed by one or two people and serve a range of clients across different sectors. For example, UMODZI Consulting, Tools for Enterprise and Education Consultants (TEECS) and Business Consult Africa (BCA) are the better known and business and management consultancy firms targeting SME development. The table below summarizes identified private sector BDS providers:

Table 11: Private Sector BDS Providers

Private BDS Provider	Business Development Services
Arch Professional	Sales and Marketing, Customer Care and Training
Business Alliance International	Training and Market Linkages
Business Consult Africa Ltd	Training, Business Strategic Plan Development, Organizational Development, Business Engineering.
Fletcher and Evans Consulting	Sales and Marketing, Research
Foodsec Consulting	Training, Food Safety and Hygiene, Value Chain Studies, Business Counseling
Invest and Reap	Trainings, Organizational Development, Monitoring and Evaluation and Research
Micro Enterprise Development Technical Assistance Centre	Capacity Building, Marketing, Branding, Public Relations & Communication, Business Start Up Advice and Business Planning, Business Mentorship and Coaching
Mlambe Consulting	Organization Assessments, Strategic Planning and Review, Team and Relationship Building, Orientation and Development of Boards Leadership Development, Resource Mobilization Support for Non Profit Organizations, Business Ethics, Learning and Knowledge Management Facilitation, Communication Strategy Development Change Management, Organization Policies, Systems & Procedures, Process Facilitation of Meetings, Workshops & Other Forums.
Tools for Enterprise and Education Consultants	Entrepreneurship, Leadership Mentoring and Skills Training, Business Diagnostics, Business Strategy Design, Business Plan Development, Market Access Training and Business Linkages, Market Research, Value Chain and Feasibility Studies.
Tradeline Corporation	Training, Market linkages, Organizational Development, Business Plan Development, Value Chain Analysis.
UMODZI Consulting	Training, Business Mentorship and Coaching, Business Diagnostics & Business/Strategic Planning, Organizational Development, Market Research, Feasibility Studies, ICT, Change Management, Performance Review, Market Linkages, Financial Management, Operations and Financial Systems, Project Management, Business Start-up Advice and Networking, Value Analysis and Workshop Facilitation.

Source: Consultants' research

Other private BDS providers for whom information could not be obtained are: Glorious Consulting, Afro-Management, MODA Consulting, Techtop Consult, Management International, and Brian and Company,

some of which are singleton consultants with other business interests. There are also individuals, often employed in the formal sector, who seek and undertake private jobs as a moonlighting activity, or sometimes in their employer's time. Finally, there are individuals who help out family and friends venturing into, or who are already in business or in formal employment³⁴, with particular problems/tasks, depending on expertise. This category is different, in that they do not seek work, like the previous categories, but rather respond to requests on an ad hoc basis and are driven by familial/friendship and social obligation reasons rather than for income potential. In practice the latter group of BDS providers may not receive any payment, other than perhaps something for expenses incurred.

These providers offer SMEs options that range in price and quality. The specialist firms are the most expensive, while some individuals offer highly discounted rates if doing a private job or do not charge at all if family/friend. In the case of the more specialized firms, these are heavily reliant on contracts from development partners³⁵ to deliver services to various target groups that they are interested in, including SMEs. There is also interest from some private sector organizations, particularly banks, in using BDS specialist firms to deliver support to SMEs through training and one to one support, mainly around business planning and financial management. Their view is that this might improve the quality of business plans and management of firms that have borrowed.

Quality of service is more difficult to determine as the tasks are so variable and much of what goes on is not visible; but the expectation is that the specialist firms, with more trained and experienced consultants offer a higher quality more professional service.

Public Sector BDS

Identified public sector BDS providers include those shown in the table below.

Table 12: Governmental BDS Providers

Provider	Description of Services, including BDS
Malawi Bureau of Standard (MBS)	Quality Standard Development, Training, Inspection and Accreditation.
Malawi Institute of Management (MIM)	Training, Organizational Development, Business & Strategic Planning.
Malawi Industrial Research & Technology Development Centre (MIRTDC)	Industrial Research, Technology development and Training and Maintenance.
Polytechnic Management Development Centre	Training, Leadership Development, Research and Coaching
Small and Medium Enterprises Development Institute (SMEDI)	Create an enabling environment for MSMEs, Support Collective and Individual entrepreneurs, Build Sustainable Malawian Enterprises, Enable Access to Financing, Improve Information Availability on and to MSMEs, Enable MSMEs to compete in new markets
Technical, Entrepreneurial, and Vocational Education and Training Authority (TEVETA)	Promote and regulate sustainable provision of Quality, Technical, Entrepreneurial & Vocational Education and Training including coordinating the delivery of Training in Occupational

³⁴ Including government employment

³⁵ Supplemented by occasional private sector contracts

	Health and Safety, Leadership, Organizational Development, Business Planning, Marketing and Research, Value Addition & Quality Standards.
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Source: Consultants' research

Some of the above are specialized in BDS, such as SMEDI and MIM. More information on SMEDI, as the most significant GoM BDS provider to SMEs, is contained in section 1.9.1. MIM operates as a relatively autonomous body offering training and conference facilities, and access to academic programs from outside Malawi. It also undertakes consultancies and runs bespoke training, but does not specifically target SMEs.

In other cases, public sector providers combine business service activities with BDS. For example, MBS enforces standards with traders/agri-input suppliers, particularly checking scales and out of date products. The focus of these public organizations is more on training and capacity building groups of MSMEs, than services to individual SMEs. This is a function of their mandates, which are more focused on micro and small, than on medium enterprises.

As public institutions, they depend to differing extents on GoM for part of their funding, with additional resources available for projects from various development partners. MBS and TEVETA benefit from statutory based levies and charges on businesses. In addition, some public BDS providers seek to provide services to the private sector on a paid for basis, such as service fees charged for testing or fees for running training programs. In some cases, SMEs have no alternative to these providers and are compelled to use the services. From this assessment, it was not possible to come to a view on the charges made or the quality of services. However, secondary sources indicate that public sector bodies struggle to understand and deliver acceptable services to private sector users, because of the different organizational cultures and operating realities between public and private sectors.

NGOs and Projects

There are NGOs and Projects that receive funding from development partners to provide support services to ASMEs. They either use staff or outsource to consultants to provide business advisory services, paying the BDS cost on behalf of ASMEs. Their services usually end on the phasing out of the project funds.

Table 13: NGO and Project BDS Providers

NGO/Project offering BDS	Development Partner	Business Development Services
Business Information and Communication Systems	CISP and Project Malawi	Microfinance, Entrepreneurship Training & Market Linkages
COMSIP	World Bank	Organizational Capacity Development, Training & Market Linkages
Farmers Union of Malawi	USAID and Swedish Government	Organizational Development, Training & Market Linkages
Local Development Fund (LDF)	World Bank, African Development Bank & GoM	Capacity building in BDS, technical support to ASMEs by identifying BDS Providers and coordinating delivery of Training, Organizational Development, ICT, Technology Development or Innovation and Market Linkages.

National Association of Small-holder Farmers of Malawi	USAID and Norwegian Government	Organizational Development, Market Linkages, Agricultural Extension Services, Communication
The Supporting Cooperative Project in Malawi	COMSIP and Scottish Govt	Organizational Capacity Development & Market Linkage Training

Source: Consultants' research

Of particular note is the LDF that aims to build the capacity of BDS providers. The first step in that process has been to build a list of providers, which will be followed by capacity building training. The focus is on national and district level providers.

FinScope (2012) asked which organizations MSMEs had used for business advice at any point. The results are shown in the table below.

Table 14: Organizations That Have 'Helped' SMEs, 2012

"Which of these organizations have you ever made use of for help with your business?" (N2)	Ever Used		% of all SMEs
	Small	Medium	
National Construction Industry Council (NCIC)	0.9	0.0	0.9
MIRTDC	2.8	0.0	2.6
MoIT	2.8	12.5	3.4
Malawi Investment Promotion Agency (MIPA)	1.9	12.5	2.6
Development of Malawian Traders Trust (DEMAT)	2.8	0.0	2.6
Small Enterprise Development Organization (SEDOM)	4.6	12.5	5.2
FINCA	12.0	0.0	11.2
Malawi Bureau of Standards (MBS)	3.7	12.5	4.3
Malawi Rural Finance Co. (MRFC)	10.2	0.0	9.5
University of Malawi	2.8	12.5	3.4
Malawi Confederation of Chambers of Commerce & Industry (MCCCI)	1.9	12.5	2.6
National Statistics Office (NSO)	6.5	0.0	6.0
Other ³⁶	17.6	25.0	18.1
None	13.0	0.0	12.1

Source: FinScope MSME (2012), Consultant's Analysis, Multiple responses possible

The above table highlights that SMEs identified a range of organizations that they stated have helped them with their businesses. The question was phrased as "help" though it followed on from a question saying "help and advice", so it is possible that some of the responses were about help and not relating to advice. This might explain why FINCA and MRFC scored highly, as both of these are Microfinance institutions (MFIs) and the help in those cases may more refer to a loan or training to support a loan. The organization ranked third was the National Statistical Office (NSO), which is not obviously involved in help or advice, but in data collection. Respondents may possibly have interpreted help as being contact with, in which case NSO may have surveyed them at some point.

In the primary research for this study, there was no mention of BDS from NGOs, other than training by CNFA in technical and business aspects of agri-input dealership.

³⁶ Details of organizations under 'other' were not available from the database.

1.5.3 CHALLENGES FACED BY BDS PROVIDERS

There is a low appreciation by ASMEs of the value of BDS and low ability to afford services. Some FIs are interested in BDS provision, but this carries challenges, including conflicting interests of advising borrowing ASME clients.

The main challenges identified by BDS providers are low appreciation by SMEs of the value of BDS, lack of knowledge of how to find an appropriate BDS provider and low willingness to pay for the BDS. SMEs have limitations on what they can afford, but they also do not readily value services. Valuing any service in advance of delivery is very difficult, and when the charges look high, the natural response is to manage without the service, even if it could yield gains for the SME. A further issue is that most BDS providers are mainly urban based focusing on larger and higher potential clients than serve dispersed smaller, lower potential SMEs in the districts.

Low educational attainment by many SME owners compared to formally educated business advisers makes interaction more difficult, as can unrealistic expectations by SME owners of what a BDS provider to achieve. According to BDS providers and banks, some SMEs want BDS providers to help them mislead banks into providing loans when the business situation does not merit it.

A further challenge is that most BDS, irrespective of provider, are subsidized to some extent. Without a subsidy, there would be little demand; but the subsidy also keeps fee rates higher than they would be and maintains supply from a wider range of mixed quality suppliers than a functioning market would sustain.

Other than business advisers and trainers delivering ‘face-to-face’, other means to deliver BDS are through access to generic information by SMS³⁷ and websites to access how to guides³⁸. An important alternative to direct provision is through *embedding* services alongside other activities in the value chain, such as equipping those that interact with SMEs with information to share alongside their normal business activity. The latter model might be something that could work through service providers like accountants and buyers/processors looking to strengthen the supply chain.

There is also scope to consider how FIs can provide or support appropriate BDS alongside financial services, since they have a direct interest in the performance and success of the business. For example, CUMO Micro-finance is providing business training to its micro-enterprise clients. Opportunity Bank of Malawi (OBM) provides a mix of business and transformational training to its rural clients, who are also mainly at micro enterprise level. In the recent past, the International Finance Corporation (IFC) supported a one week business training program for 2,000 female business owners through NBS Bank. However, the banks are mainly not offering or supporting BDS to their clients.

One challenge with FIs providing BDS to ‘borrowing clients’ is that the client may seek to avoid payment if the advice has not lead to an improvement in the business. A related risk is that clients feel obliged to undertake the actions that the bank is advising, even if it thinks or knows that these are not good ideas. Finally, running a SME is quite different from the experience base of bankers who may not be in the best position to advise SMEs, relying on more formal and corporate models of running a business that are not relevant for SMEs.

³⁷ The Zambia National Farmers Union has an interactive SMS based system for accessing advice.

³⁸ More common in developed economies

An alternative is to separate advice from the bank, even if it is delivered to a bank's SME clients. A recent FinMark study on Rural and Agricultural Financial Innovation (2013) identified the Private Agricultural Sector Support (PASS) Trust model which enables ASMEs to develop bankable proposals, supported by a guarantee fund for banks. Essentially, PASS acts as an intermediary to understand the bank's requirements and then works with the ASMEs to build their capacity and provide comfort to all parties through a range of loan guarantee packages that banks pay for. Income from the guarantee funds subsidizes PASS' BDS support to the ASMEs.³⁹

I.6 FINANCIAL SERVICES

This section reviews the use of financial services by SMEs. The FinScope MSME (2012) database contains a considerable amount of financial data, which is combined with qualitative data from the field work.

1.6.1 FINANCIAL SERVICES USAGE

Transaction services, primarily bank accounts, are the most commonly used financial service; at the other end, there is very low use of insurance. Attitudes to banks were generally positive on trust and service, but less positive about understanding, helping and charges.

The use of financial services, as identified by FinScope MSME (2012), is set out in the table below.

Table 15: Use of Financial Products/Services, 2012

<i>Which of the following do you... (F1)</i>	<i>...have now?</i>		<i>not have now but used to have?</i>		<i>not and never had?</i>	
	<i>Small</i>	<i>Medium</i>	<i>Small</i>	<i>Medium</i>	<i>Small</i>	<i>Medium</i>
Savings or transaction account	43.5	75.0	3.7	12.5	52.8	12.5
Current or cheque account	12.0	37.5	2.8	0.0	82.4	62.5
Deposit account (fixed term / notice)	3.7	12.5	2.8	0.0	91.7	50.0
ATM card or debit or visa card	16.7	37.5	3.7	0.0	77.8	62.5
Cellphone banking (check balances, transfer money)	0.0	0.0	0.0	0.0	96.3	75.0
An overdraft facility	0.9	0.0	0.0	0.0	95.4	75.0
Life insurance or cover	2.8	25.0	0.0	0.0	92.6	62.5
Medical aid/medical scheme	3.7	25.0	0.0	0.0	93.5	62.5
Hospital plan	1.9	12.5	0.0	0.0	95.4	75.0
Funeral plan or cover	1.9	25.0	0.0	0.0	95.4	75.0
Business contents insurance (office equipment)	0.0	12.5	0.0	0.0	96.3	62.5
Business contents insurance (tools & machinery)	0.0	12.5	0.0	0.0	97.2	75.0
Business premises insurance	1.9	12.5	0.0	0.0	95.4	75.0
Motor Vehicle Insurance	5.6	37.5	0.0	0.0	92.6	62.5
Pension or provident fund	0.0	12.5	0.0	0.0	97.2	62.5

Source: FinScope (2012), Consultant's Analysis, Multiple responses possible

³⁹ PASS has been supported for 12 years by a development partner, but appears to have reached viability.

As expected, the most commonly used products are savings/transaction accounts with 43.5% of small, and 75.0% of medium enterprises, having these. For medium enterprises, 37.5% had current/checking accounts. Other common products⁴⁰ for medium enterprises were vehicle insurance (37.5%), buildings/premises insurance (37.5%), life insurance (25%), medical aid (25%) and funeral cover (25%).

The explanation behind low uptake of service is partly due to SME' views about FIs and partly about access:

Table 16: Attitudes to Financial Institutions, 2012

<i>“Please tell me if you agree or disagree with each statement.....” (G1)</i>	Agree		Disagree		Don't Know	
	Small	Medium	Small	Medium	Small	Medium
It is difficult to open a bank account	29.6	37.5	60.2	62.5	10.2	0.0
Bank charges/interests are very high	40.7	62.5	31.5	25.0	27.8	12.5
FIs don't explain how things work	42.6	50.0	26.9	12.5	30.6	37.5
FIs are not understanding when you don't make your payments	56.5	50.0	17.6	0.0	25.9	50.0
FIs give too much credit and get you into financial trouble	40.7	25.0	33.3	12.5	25.9	62.5
FIs take advantage of poor people	47.2	37.5	32.4	37.5	20.4	25.0
FIs have products and services designed for people like you	59.3	62.5	14.8	12.5	25.9	25.0
You could manage fine without a bank account	50.0	50.0	45.4	50.0	4.6	0.0
Banks provide a good service	80.6	100.0	4.6	0.0	14.8	0.0
You trust banks	82.4	87.5	11.1	0.0	6.5	12.5

Source: FinScope (2012), Consultant's analysis, multiple responses possible

The data suggests that SMEs are generally positive towards FIs/banks⁴¹ with ratings at over 80% on good service and trust. There were also positive findings on the ease of opening bank accounts, which were the most common product being used, and on the design of products relevant for the respondents. However, there were less positive responses around charges/interest being high, particularly among medium enterprises, poor explanations of how things work and 'bank's not understanding' about late payments. Interestingly, responses were evenly split on managing 'fine' without a bank account; this is reflected in the proportion that actual have some form of bank account (see Table 15).

The trust in banks echo findings on low income savings in Malawi⁴² (FinMark 2013) that found high levels of trust in banks as safe places to keep funds, but concern about charges. In FinMark (2013), there was more concern about the level of charges than the rate of interest paid on deposits; but as with the data on SMEs, concerns about interest rates increased with respondent's size. For small enterprises that want to borrow, there is more concern about access than cost. For medium enterprises, which have options from more than one bank, then the concern shifts from access to 'cost', as expressed in the interest rate.

⁴⁰ ATM cards and savings books are issued with accounts, so these are not listed here as already 'counted' in the other figures.

⁴¹ Note that the wording of the questions interchanged banks and Financial Institutions, so it is not clear if responses were for banks only or FIs more generally, in some cases.

⁴² Understanding the challenges and opportunities in promoting savings among low income individuals in Lesotho, Malawi and South Africa (2013), FinMark Trust

The above rates of service penetration highlight that there is still a large gap between supply and demand of financial services. These are now reviewed in detail through a supply side categorization into bank accounts, savings, insurance and credit services.

1.6.2 BANK ACCOUNTS

What are commonly termed 'savings' accounts are often used more as transaction accounts for payments in and cashing out. Accounts are also valued for safe keeping of funds, rather than saving as an investment. ASME owners often maintain multiple accounts, which may reflect the bank branch network in the different areas in which they operate, as well as being seen as a necessary step to getting a loan from any bank that might be willing.

For small enterprises, aside from a savings/transaction account, 12% said they had a current/checking account and 3.7% had a fixed term/notice account. FinScope (2012) found that only 13.9% of small enterprises said customers normally pay by check and 9.3% by bank transfer, while for medium enterprises it was 37.5% and 12.5% respectively. It is possible that some small enterprises use other's accounts for depositing occasional check payments, but at some point it is necessary to have a bank account, as indicated by the higher levels of these means for medium enterprises.

There were differences in behavior of small compared to medium enterprises in personal and business bank accounts. The data from FinScope (2012) shows that small enterprises are much more likely to use a bank account for personal and business activities, compared to medium enterprises which predominantly separated business and personal accounts.⁴³ This may partly reflect higher charges on business accounts, such as ledger fees, which discourage establishing a separate business account, but it is also likely to be a function of poor separation of personal and business activities by small enterprise owners. Based on other FinScope (2012) responses, it may also be a factor of the limited income streams from the business that do not make it justifiable to split.

Based on the ASME interviews, bank accounts were seen as important for keeping money safe, but also for making payments to some suppliers and for receiving payments from larger businesses that they were supplying or providing a service for, such as transport. The bank accounts were also useful for those businesses with more than one outlet, as it enabled staff to deposit funds on a regular basis, so that the owner was able to utilize this for replenishing stock.

ASMEs owners with multiple businesses and/or multiple outlets often had several bank accounts despite several disadvantages. Maintaining multiple accounts increases bank charges compared to consolidating accounts in one bank, and means that funds are dispersed and may not all be usable due to requirements for minimum balances. In addition, the time and effort to maintain and manage multiple accounts is clearly greater than what is involved in maintaining a single account. The multiplicity of accounts can reflect which banks have branches in particular locations, which force ASME owners with more than one outlets and/or business in different locations to use several banks. The ability to deposit and withdraw at different locations gave the ASME owners more flexibility and great safety in handling cash, despite the inefficiencies and costs incurred.

A second reason for multiple bank accounts was that the owners thought this might help them get a loan. This fits with the common requirement among banks that the borrower should have an account and be

⁴³ A reported 67.5% of medium enterprises were using a business account for their business transactions, even though there was still a substantial residual number using their personal accounts for business.

known to the bank. In this case, the accounts were kept in the hope of future access to loans, but without a firm prospect, as there are requirements for loans other than a history of operating an account.

1.6.3 SAVINGS

Small enterprises were as likely to save in the home as at the bank, probably reflecting access and cost issues. These are often not savings for investment return (though interest), but for safe keeping until needed. Medium enterprises are more likely to be saving formally.

Savings are important for future investment and for managing working capital needs. The table below sets out the places that SMEs in the FinScope MSME (2012) study said they were saving:

Table 17: Places for SME Savings, 2012

<i>Where do you save, or put money away for business purposes? (I2a)</i>	% of all Small	% of all Medium	% of all SMEs
Bank	44.4	87.5	47.4
MFI	0.0	0.0	0.0
Chipereganyu	1.9	0.0	1.7
In the home	45.4	25.0	44.0
Other	0.9	0.0	0.9

Source: FinScope MSME (2012), Consultant’s Analysis, Multiple responses possible

For small enterprises, saving in the home is a common method of saving, almost equaled by rates of saving at the bank. The prevalence of savings in the home mirrors the findings from previous studies (FinScope 2008 and FinMark Trust 2013). For consumers, saving at home reflects the need for ready access to cash to deal with day to day and incidental expenses, plus the relatively high time and potentially travel costs to reach an FI outlet to transact. This behavior continues from consumer through micro-enterprise to small enterprises, but with higher use of bank accounts by enterprise owners than by consumers. This progression is based on size and formality of enterprise, is evidenced by medium enterprises, for which the clear choice in the sample was for bank savings. For these enterprises, the size of the operation and the need to make payments and receive payments by check, which is still common in the business community, means that a bank account eventually becomes necessary.

In the primary research, there was very little mention of savings by ASMEs; rather they spoke of bank accounts in terms of transactions. It is likely that the account is also a means to hold surplus cash until it is required for the business use or for paying the owner. The FinMark (2013) study on low income savings also found that individuals were using savings accounts more for transactions than for saving. That study also found that individuals usually saved with a ‘project’ specifically in mind, be it social or economic.⁴⁴ That is, they had a purpose for the savings, which was motivating them to try to build their savings balances.⁴⁵ For the SMEs, bank accounts, even those labeled ‘savings’ accounts were being used for transactions, though FinScope (2012) does suggest that there is some savings for investment going on, as indicated in the table below.

⁴⁴ Typically for farm inputs, housing improvements, a business, education and so on.

⁴⁵ Though in practice many of them had to withdraw savings in order to meet a mix of day to day needs (as they were low income households) and emergency/urgent needs such as medical and funeral costs.

Table 18: SMEs Reasons for Saving, 2012

<i>"...what are you saving or putting the money aside for?"</i> (I2b)	% of all Small	% of all Medium
To expand the business	46.3	37.5
Money for day to day running	24.1	37.5
To have money when I need it	33.3	37.5
For the future	25.0	25.0
Other	0.9	0.0

Source: FinScope MSME (2012), Consultant's Analysis, Multiple responses possible

1.6.4 INSURANCE

ASMEs commonly face losses through crime, fire and other hazards. ASMEs focus on taking measures to prevent loss than using insurance to mitigate the loss. ASMEs want to own, and therefore control, premises and transport which are major risk factors for them in losses and operational problems. Owning premises means the ASME can invest in prevention measures against common risks. Controlling transport is more efficient, convenient and avoids the risk of being let down. Insurance was rarely mentioned by ASMEs.

The financial service use in FinScope (2012) (Table 15) found low levels of insurance, with vehicle, medical, workman compensation and life insurances between 2.8-6.0% of small enterprises, though higher levels for medium enterprises.

SMEs face a range of risks. FinScope (2012) found the following responses on losses in the last 12 months.

Table 19: Insurable Losses Incurred in the Last Year, 2012

<i>"Has your business suffered a loss such as through theft, crime, fire, etc. in the last 12 months?"</i> (J2)	% of all Small	% of all Medium	% of all SMEs
Yes	34.3	87.5	37.9
No	65.7	12.5	62.1
Total	100.0	100.0	100.0

Source: FinScope MSME (2012), Consultant's Analysis

Just over one third of small enterprises and nearly nine out of ten medium enterprises had suffered a loss in the last year, suggesting that factors such as theft, crime, fire and other insurable events are common.

From the primary research, the question was framed as what risks the business faced and what the owner did about these risks, without mentioning insurance. The responses from businesses fell into a number of groups.

Table 20: Risks for SMEs and Mitigation Strategies

Risks identified by SMEs	Mitigation Strategy
Break-ins and robbery	ASMEs invest in security – gates, bars, walls, guards and lighting. This is more possible when the premises are owned and so the owner benefits from any investment in security measures. Cash is also deposited to the bank regularly or taken to the owner's home at night.
Theft by staff/managers	ASMEs try to make sure there is clear control of a discrete area of the business or outlet, so that if there is theft then the responsibility is clear.

	Family members were involved in the business and records kept and checked regularly. As the portfolio grows, then other members of the family can be brought in, but they have to be trusted, such as a spouse, or sibling. There was evidence of owners building trust in employees who had not been involved in petty or major thefts
Theft of goods in transit	Owners send someone with the transport to accompany the delivery of goods and avoid missing bags along the way, or short counting on arrival by the buyer's staff
Robbery of cash in transit to and from the bank, and at the owner's home	ASMEs may have to travel long distances using public transport for cash deposits or withdrawals. Owners travel at irregular times and disguise bags carrying money. Robbers target business people, especially if they are tipped off that the owner keeps money at home. The owner has to make their home as secure as they can.
Fire, flood or other damage	These are not commonly guarded against, other than precautionary measures. Where flooding is possible, they take measures to reduce water entry to store rooms, such as raised thresholds or raised storage areas.
Non-payment	This risk is managed by requiring cash payments. Where trade credit has been extended, then no future credit is given.
Inflation & MK devaluation	ASMEs have to adjust prices frequently, though it affects demand
Breakdowns in transit	Some transporter have small garages at home for maintenance before departure Transporters ensure that drivers have basic knowledge of mechanics & car repair

Source: Consultant's research

Respondents identified a range of risks, some of which are commonly insurable, while others related to broader business environment risks like inflation and devaluation. Theft and robbery were commonly mentioned. Business people are targeted by potential robbers and also suffer from theft by staff and managers.

There are steps to limit the risks. One SME owner reduced staff in each outlet so that only one person was in control and therefore if there were missing goods or money, it was clear where the responsibility lay. Another trader had clear separation for the different ranges of products in the outlet, so that each operated as a separate unit in terms of cash handling and stock, again so that responsibility for losses could be clearly assigned to an individual.

The issue of theft by staff and managers is a problem, so owners also use family members to oversee additional outlets. There was evidence that owners seek trust relations with key members of staff and managers, so honesty is a key factor in staff recruitment, retention and promotion by ASMEs.

Insurance as a means to mitigate risk was rarely mentioned, with ASMEs preferring to take preventative measures to address risks. ASMEs did not have negative views about insurance; rather it was just not something they considered. It is also possible that access in the districts is much more difficult than in urban areas. No ASME owners thought they had loan insurance, yet Credit Life Cover is commonly part of a loan package, in which case owners were not aware of having the cover rolled into the loan. It has been recommended in previous studies, such as FinScope (2008) that bundling insurance with other products could be one way to ensure that SMEs have protection, however it runs the risk of not being a transparent arrangement, as with Credit Life Cover, to the extent that the borrowers are not aware they have been charged for the cover.

There is considerable work to be done on raising understanding of insurance benefits and availability. Policies tailored to SME risks need to cover the risks highlighted above, particularly theft, in order to be attractive to SMEs. However, in the consultants' assessment, many ASMEs value premises improvements and will likely continue to prioritize this over insurance of the most common risks.

1.6.5 CREDIT

Approximately 40% of small enterprises were borrowing or had borrowed in the past year primarily for day to day needs and also for growth. Importantly, they were nearly three times as likely to borrow from a business friend as from a bank. The primary research supported this in that it was possible to borrow up to MK 500k (US \$1,250) for a month at no interest from this source, on the basis that it was reciprocal. The immediate availability of funds was the driving factor, but cost saving must also play a big part. About one third of ASMEs in the primary research would not consider borrowing from a FI for fear of losing their assets.

In terms of credit use, the following table shows the proportion of SMEs that have borrowed.

Table 21: Proportion of SMEs that have borrowed, 2012

“As a business owner, which of the following statements apply to you?” (H1)	% of all Small	% of all Medium	% of all SMEs
You have borrowed money in the past year for business purposes	29.6	12.5	28.4
You have taken good on credit for business purposes in the past year	9.3	12.5	9.5
You are currently repaying or owe money for your business	8.3	12.5	8.6
You are currently repaying or owe money for goods on credit for your business	2.8	-	2.6
None of the above	59.3	-	55.2

Source: FinScope (2012), Consultant's Analysis, Multiple responses possible, except line 5, n=104

The data show that 37.2% of small enterprises and 25.0% of medium enterprises⁴⁶ had outstanding loans or trade credit that they were paying. FinScope (2012) considered the reasons for borrowing, set out in the table below.

Table 22: SME Reasons for Borrowing, 2012

For what reasons did you borrow money? Q27 (H7)	Small	Medium	% of all SMEs borrowers
Growing my business	39.5	50.0	40.0
Day to day business needs	47.4	0.0	45.0
Finance a tender/contract	18.4	0.0	17.5
To buy property	2.6	0.0	2.5
To finance stock	10.5	0.0	10.0
To upgrade business facilities	2.6	0.0	2.5
New equipment	7.9	50.0	10.0
Personal reasons	7.9	0.0	7.5
Other	10.5	0.0	10.0
Refused	0.0	0.0	0.0

Source: FinScope (2012), Consultant's Analysis, Multiple responses possible, n=40

⁴⁶ There were missing values for both small and medium enterprises.

The reasons for borrowing were strongly oriented to meeting the *'day to day business needs'* (45.0%), which could be re-stated as working capital needs, and *'growing my business'* (40.0%) being investment in working capital and/or fixed capital. Financing a tender/contract can also be classified as financing for working capital.

The main source of finance is set out in the table below.

Table 23: Main Source of Borrowing, 2012

Which of these places did you borrow the most amount of money? Q27 (H3)	Q27b. Largest Source		% of all SMEs borrowers
	Small	Medium	
Bank	15.8	50.0	20.0
MFI	10.5	0.0	15.0
Village Bank	0.0	0.0	0.0
NGO	5.3	0.0	5.0
Government agency	7.9	0.0	7.5
Chipereganyu	0.0	0.0	0.0
Informal money lender	10.5	0.0	10.0
Friends, family friends, family or colleagues	44.7	0.0	47.5
Employer	0.0	0.0	0.0
Get goods on credit	5.3	0.0	5.0
Other	5.3	0.0	10.0

Source: FinScope MSME (2012), Consultant's Analysis

The above table highlights that *'friends, family friends, family or colleagues'* are the most common main source of loans for nearly half of those that were borrowing (42.5%). This was followed by banks (15.0%), MFIs (10.0%) and informal lenders, such as Katapila (10.0%). That almost three times as many SMEs borrowed from friends and family compared to banks, suggests that the banks have a long way to go to win over SMEs from these personal sources.

The FinScope (2012) survey asked why they chose their main source. The results are presented below.

Table 24: Reasons for Choosing a Source of Borrowing, 2012

Why did you use this source for borrowing? Q28 (H6)	Small	Medium	% of all SMEs borrowers	% of all MSMEs borrowers
Affordable cheapest instalment	7.9	50.0	10.0	0.9
Lowest interest rate	15.8	0.0	15.0	1.3
Flexible payment rate	10.5	0.0	10.0	0.9
Get money quickest	55.3	0.0	52.5	4.7
Best service	10.5	50.0	12.5	1.1
No credit checking	5.3	0.0	5.0	0.4
Familiarity	26.3	0.0	25.0	2.2
Trust	26.3	0.0	25.0	2.2
Convenient	15.8	0.0	15.0	1.3
There was no other source	23.7	0.0	22.5	2.0
Other	5.3	0.0	5.0	0.4

Source: FinScope (2012), Consultant's Analysis, multiple responses possible

The responses highlighted that ‘*get money quickest*’ was the overwhelming reason (55.3%) for small enterprises followed by ‘*familiarity*’, ‘*trust*’ and that ‘*there was no other source*’.⁴⁷ Interestingly, ‘*lowest interest rate*’ was lower ranked, and equal with, ‘*convenience*’. This data is further qualified by probing into attitudes to taking loans:

Table 25: Attitudes to Borrowing/Not Borrowing

<i>“Thinking about your business, please tell me if you agree or disagree with each statement?” (H9)</i>	Agree %		Disagree %		Don't know %	
	Small	Medium	Small	Medium	Small	Medium
You are able to turn to friends or family to provide with money for emergencies	73.1	50.0	26.9	37.5	-	12.5
You have money set aside in case of emergencies at your business	86.1	100.0	13.0	-	0.9	-
You would never borrow any money from anyone or any place for your business	20.4	12.5	77.8	87.5	0.9	-
You would only borrow and take loans for occasional valuable purchases for your business	88.0	100.0	9.3	-	1.9	-
You pay off the balance of what you owe on our business loans in full every time	48.1	25.0	40.7	50.0	10.2	25.0
You would borrow money to start another business	83.3	75.0	14.8	-	1.9	25.0

Source: FinScope (2012), Consultant’s Analysis

The above table highlights that many ASMEs have options for finance, in the form of friends and family, and money set aside. They would not rule out borrowing, but would do so for significant items for the business on an occasional basis and to start a new business. However, the responses were equally split on whether they would pay off their loans in full every time. This may partly reflect that there may not always be a requirement to clear debts from family and friends, and/or that they have not or would consider not fully paying of loans from formal sources.

Although 25 (41%) of the ASMEs were borrowing from FIs, the qualitative research found reluctance by 20 ASMEs to borrow from formal sources (36%). For some of the ASME owners, this was an absolute statement that they would never borrow from a formal FI. The common fear was that they could end up losing all that they had built up, as formal FIs would require pledging of assets, including premises and vehicles. It might be that these ASMEs would not have been able to borrow due to not being able to meet the FI’s requirements. One trader said: “*banks love businesses when they are doing well rather than helping the struggling businesses to grow*” highlighting a different issue that banks do not help those that most need finance.

In the primary research, 30 (49%) of the ASMEs talked about arrangements with ‘business friends’ meaning in this case other ASMEs in their locality that they interacted with as suppliers and even competitors. One form of borrowing that was mentioned in the section on groundnut and soybean, was lending of stock, to be returned when the borrower had been paid and could re-stock. But respondents talked about borrowing money from other businesses, with amounts up to MK 500,000 (\$1,250) frequently mentioned. One agri-input dealer does this when he needs to source fertilizer (Lilongwe Rural) The arrangements varied according to the nature of the relationship, but generally these were not loans for interest/profit, but to assist the ‘business friend’.

⁴⁷ Some data values were missing for medium enterprises

On a different basis, in Mitundu, one large trader was receiving advance funds from a large exporting group and from buyers in Tanzania to source groundnuts for them. This advancing of funds is sometimes done for small traders working on behalf of a larger trader.

There were also mentions of borrowing from family, but this was less common than from business friends. It may be that the family is normally coming to the business to borrow, rather than the other way around, as the ASME owner is likely to be, or perceived to be, relatively wealthy within his/her family, whereas in the normal course of business within a center, the ASME owner will interact with peer ASME owners who can see benefits in helping each other, such as reciprocal help when it is needed.

ASMEs were also quite inventive at getting credit. For example, transporters are often asked by traders who want to move their goods to a customer in the cities to give up to 10 days credit before paying, which enables them to receive the funds from the buyer through their accounts. However, the transporter needs to pay for fuel in cash from the normal service stations, so he negotiates with a black market supplier of fuel for a full tank of fuel, to be paid within 14 days. There is no interest charge, but the fuel is sold at a premium price.

The implications of the above is that there is a core of ASME owners who would be unlikely to borrow from formal sources, partly from 'fear' of losing their assets and businesses, and partly because they have an alternative for the amounts of finance they need for working capital and small investment in fixed assets. There are also other ASMEs, probably more medium than small, that are prepared and willing to borrow from banks in order to take business opportunities as well as support working capital and address cashflow problems.

1.6.6 FINANCIAL SERVICE PROVIDERS

The banks mainly treated SME services as an extension of personal banking, but with little/no substantive differentiation of products to be tailored to SME or agri-business needs. The main focus was on lending products, which were collateral based. Banks had problems assessing credit worthiness of ASMEs, so used collateral as a means to reduce/remove their risk. Due to problems with land titles in Districts, this effectively excludes borrowing from formal sources by ASMEs. This suggests there are both supply and demand side constraints.

The research team met six banks,⁴⁸ two MFIs and a micro-insurer to discuss SME finance, as detailed in Annex III.

Discussions with MFIs indicated that there is limited lending to SMEs, rather their lending activities are focused more on micro-enterprises. However, based on the earlier interviews with business owners and identified portfolio approach, it is possible that some of the individual micro-enterprise owners also owned other businesses directly or with a spouse/family member and so may fall within the small enterprise category. MFIs do provide a mix of credit and training to their clients. The latter is focused on loan/credit management, but does also extend into financial training more generally, and beyond in some cases e.g. CUMO Microfinance has a mobile enterprise training unit.

For the six banks interviewed, all had a dedicated SME department except OBM which stated that it targeted micro-enterprises, so that this is its main focus. The SME departments were mainly located under Personal Banking, as opposed to Corporate Banking, as SMEs are below the high value larger corporate clients and merit less direct attention. In many ways, SMEs are in fact extensions of a personal banking relationship,

⁴⁸ With a total of 102 banking outlets across Malawi.

given the importance of the owner-manager in the SME's structure and operations, so the fit within Personal Banking makes sense.

There were several bank branches in each district, principally at the District Centre, but also in some other important trading centers, such as Liwonde in Machinga, with some districts, like Lilongwe rural and Mchinji served by mobile banking units.

All six banks used different definitions of SME to classify their clients. Five used business annual turnover for classifying businesses into micro, SME and large/corporate. The upper turnover level for SMEs was generally around MK200-300million (US \$500,000-750,000), but for one bank it was MK 500m (US \$1.25m). Only one bank specified a lower turnover limit of MK24m (US \$60,000) for an SME, below which the businesses were classified as micro-enterprises. Most of the banks did not differentiate between micro, small and medium enterprises, but grouped them together.

Banks also used employment and loan size filters, though it was not clear if an enterprise had to fit all three criteria to be classified as a SME in the system or that this was more a matter of judgment by a bank officer to determine whether to include as a personal banking client, a SME client or a corporate client. The filters appeared to some extent to be guiding rather than firm boundaries. In practice, this discretion might be useful and practical given that there are challenges in getting accurate up to date data, as well as making a more rounded assessment of where the best location is, according to the servicing needs.

In relation to employment, one bank used 11-25 for small and 25-100 for medium. Another used 50 employees for SME, without splitting small and medium. In essence, there were inconsistent cut off points, but as noted, this appeared to me more of a guiding level than a definitive dividing line.

The size of loan was the key factor for one bank, with micro-enterprise loans from MK 5,000 to MK 1million (US \$12.50 to US \$2,500), and SME loans from MK1m to MK 25m (US \$ 2,500-62,500) and large/corporates above that. Another bank set a maximum of MK70m (US \$ 175,000) loan below which a business was a SME.

The banks were asked to provide details of their products for SMEs. From the discussions, it was clear that although some products were presented as specifically for SMEs, these were either standard products or standard products that had been badged/branded to be for SMEs, but with no or minimal adaptation. In some cases, such as current accounts, the main difference was that the charges were higher for SME ('business' current accounts in general) than for personal accounts. Essentially the differences were presentational and not apparently related to a specific assessment of SME needs. This suggests to the consultants that the financial services supply constraints lie in the specific loan terms and product characteristics, rather than the range of 'SME loans' they offer.

The banks were also asked if they classified agricultural/agri-business from other sectors and, if so, if they distinguished between agricultural as 'farming' from agri-business as other agricultural activity, other than farming ('off-farm'). In all cases, the banks classify enterprises as agricultural compared to other non-agricultural sectors,⁴⁹ rather than distinguishing between farm and off-farm business activity within 'agricultural'. As a result, it was not possible to identify portfolio data for agri-businesses separated from farm-related agricultural activity.

⁴⁹ These varied for each bank.

It should also be noted that a major portion of the banks' lending and MSME client base was to tobacco farmers through farming clubs. The reason that this is such a major portion is that the tobacco farming sector is one of the best organized in Malawi, with a formal market through the auction floors. Loan recovery is high, but not 100%. However, this is a much safer form of agricultural lending than lending to many other agricultural sub-sectors. Although USAID cannot support tobacco farming and agri-business, the main point is that the banks are heavily focused on tobacco with their agricultural lending portfolios, making other sub-sectors less attractive and interesting to them. The banks also target tea and sugar, which also have well-organized marketing systems and are export crops, which means borrowers are more likely to repay loans.

Two of the six banks stated that they also lend to dairy and to soybean, while one said it has some groundnut clients. These would include farmers and agri-businesses. Based on the logic of a lending where there is an organized market, then dairy has more attraction than soybean and groundnut, as the MBGs have contracts with dairy processors because the collection of the milk has to be organized and regular, unlike soybean and groundnut which can be more easily stored, transported and sold to any potential buyer. There is clearly side selling to vendors by farmers and by MBGs, but in the main they sell to a single processor who is required to pay monthly. This creates opportunities for agreeing with the MBG/members and the processor for loans to be deducted from the monthly payment.

As is clear from the above lending behavior by banks, the key to lending is the existence of a relatively orderly market structure, where loan deductions can be made. This is problematic for soybean and groundnut, as these can be classed as 'open-marketed' crops,⁵⁰ which are not perishable (like sugar, tea and milk) and so can be sold at any point in the season and easily moved, making it more difficult for processors/buyers to be sure of buying the crop. Rather, these crops are susceptible to side-selling by farmers so that any provider of inputs cannot be sure the crop will be available to buy. It is no coincidence that traders are involved in open-marketed crops and not in 'closed-marketed' crops.⁵¹ As a result, lenders are not able to finance activities in these 'open-marketed' crops, as the crop can be sold to anyone and therefore loan recovery is very uncertain. This partly explains why banks have faced such challenges in lending to crop sectors like groundnut and soybean.

Banks also identified the issues of the legal status of agri-businesses, the identification of owners and their traceability. For agri-business SMEs this presents a major obstacle as though they may have licenses to operate, typically from their District Assembly, and are checked by the Malawi Bureau of Standards (MBS) and visited by the Malawi Revenue Authority (MRA), these are operational matters that are implemented *even if* a business does not have a legal form. In legal terms, the business does not exist as an entity separate from the individual owner or from the individuals that run it, if run a husband and wife. Although names such as 'company', 'partnership' or a name that is not the owner's name are commonly used, these 'businesses' are not legally either a limited company or a formal partnership. In practice, they operate as sole traders where the owner(s) is the legal person. However, FIs are reluctant to give credit to ASME, as they have no *formal legal status* and the FIs know that it is very difficult to identify the person they are dealing with and trace them for

⁵⁰ See Contract Farming in Malawi, World Bank (2008)

⁵¹ Closed marketed are where there is an imperative or strong incentive for processors and farmers to be integrated, for example due to the perishability of the commodity. Tea, coffee, sugar-cane and milk must all be processed within 1-2 days of harvesting and so there is a need to integrate processing and farming activities, with proximate location, organised harvesting and collection and regularized payment systems. Tobacco was an exception, as it has the characteristics of an open marketed crop and is susceptible to side selling, but the overall organisation of the sector with a single official marketing channel, creates a mechanism to control side selling when combined with the leaf buyers intensive support to growers including monitoring of production and incentives for compliance. See Contract Farming in Malawi, World Bank (2008)

payment of debts/loans if the 'business' defaults. FIs reported that ASME/owners change their names and identities in order to access further loans after defaulting with one lender. The absence of a Credit Reference Bureau in Malawi contributes to the poor quality of ASMEs data maintained by financial institutions.

The FIs also highlighted that the *default rate* on loans to SMEs can be as high as 18%, and typically up to 5-10%. In response to this, FIs put in place ever more stringent credit assessment measures before issuing loans to SMEs. The consequence is that it requires more time, more information, more documents and more cost on both sides, particularly the SME to comply with the requirements.

One of the reasons for the high default rate is that some SMEs *divert* a proportion of the loan obtained from the bank for purposes other than the intended one, which includes spending on personal needs as well as diversion into another business. There is also an element of wasteful spending reported by FIs, where SMEs purchase non-productive assets, typically vehicles, or tie up the capital in a property, which does not yield an income stream to meet the debt incurred, eventually resulting in default if the loan is not serviced from other sources. One bank SME Manager estimated that only one third was used for the stated purposes, and the rest diverted.

One response to high default and inability to pursue individuals who change their identity is that FIs require *security/collateral* that covers over 100% of the loan value, typically over 150%. FIs do not accept landed property that is not registered, which tends to be confined to the urban areas and major centers in the Districts. This makes access to bank loans difficult by District-based ASMEs. FIs can take other forms of collateral such as equipment and vehicles, but not in all cases as there is concern by FIs over taking security over moveable assets. In the absence of security/collateral, then FIs generally do not lend. Unlike more developed economies, where banks have developed lending products that utilize contracts and debtors, this is not yet possible in Malawi, mainly because the FIs are reluctant to move from security/collateral lending. As an alternative, lease-purchase is available in Malawi for fixed assets like equipment and vehicles, but is not yet widely used, mainly due to concerns by lenders over the risk of movable assets.

Some SMEs offer land and properties as collateral that belong to third parties by using *fake documents* and bribing people engaged by the bank to conduct property valuations. Banks do not solely rely on the information provided by ASMEs, they have to assess the risk level and verify all the information which delays the process. On the other side, one ASME mentioned that it was necessary to give the bank manager something after getting the loan.

FIs stated that they face problems in *assessing the credit worthiness* of ASMEs, as most do not keep proper and verifiable financial records even if they have been operating a bank account with the potential lender. Banks encourage ASMEs to open accounts with them first and operate the account for at least three months so that deposit/credit can be used to assess the ability of the business to generate income to determine its credit worthiness. This approach has risks as a determined ASME fraudster can manipulate their deposits to present a more credit-worthy picture. In practice, deposit turnover is used as one indicator of credit-worthiness than a determinant of it.

Some ASMEs submit financial statements that are not consistent with their bank account statements or which are not reflective of their true situation. These need checking and this delays the process, but it also results in requests for additional information which ASMEs reported as problematic.

Banks seek to assess the *borrower's character*, particularly to identify those who have defaulted with the bank or another FI and also exclude those who are politically exposed persons, and so risky to lend to.

A further risk for FIs is that there are external risks that cannot be managed or insured against, particularly in the agricultural/agri-business sector where there are considerable weather and market based risks. This is compounded by the covariate nature of the risks, such that many ASMEs would be affected by poor weather or a fall in world prices all at the same time, resulting in a high vulnerability of lenders if their portfolio is heavily dependent on agriculture/agri-business. Although NICO and Micro-ensure have developed insurance policies for the agricultural sector, such as weather-based index insurance, dairy cow insurance, and policies that cover a range of agri-business risks, these do not adequately cover all the risks and mostly focus on production.

According to FI respondents, SMEs in general lack *financial management* and *marketing* skills. Financial management includes cashflow and working capital management, investment decisions, record keeping and understanding management accounting. One bank SME manager said: “*Even chartered accountants do not keep good financial records for their businesses.*” Marketing included researching/determining market opportunities, differentiating and competing in markets and delivering good products/services. Too many businesses were simply copying what they saw other businesses do, and then trying to cut corners to save costs and even cheat customers, such as by tampering with scales or selling sub-standard or expired products.

Based on FinScope MSME (2012) responses, 53.7% of small enterprises and 75% of medium enterprises keep financial records. Of these, half of medium enterprises keep manual records and over 90% of small enterprises. 10% of small enterprises that keep records get some external help, while 25% of medium enterprises get external help. It is surprising that 25% of medium enterprises state that they do not keep financial records. One enterprise visited pointed to a wad of papers hanging from a wire from the ceiling as the means by which it stores its financial records. There are clearly weaknesses in record keeping, but this is not simply about formalizing systems, but about finding appropriate record keeping systems that provide sufficient relevant and time information for decision making. To be able to borrow money from a formal FI is inevitably going to require a more significant change in record keeping.

In addition to the above, bankers highlighted the poor saving culture of ASMEs which turns them into persistent borrowers of working capital. One of the effects of the lack of saving culture is the failure to invest in value addition, as this requires continued and substantial investment in expensive equipment. In essence, it is difficult for SME owners to defer the benefits of being in business; rather they feel a need to show that they are being successful in the present by spending on conspicuous assets, like vehicles and property, and living a lifestyle above the current income that the business can support.

These are fundamental weaknesses in SMEs, even if bankers are generalizing and not fully appreciating the challenges of the operating environment faced by SMEs. Many of these stem from attitudes firmly based in the prevailing business culture, but also weaknesses in the business training that is available which is based on theoretical and corporate business operating models rather than embedded in a deep appreciation of how to manage and operate a SME in a chaotic and relatively risky environment. Recognizing that owners are operating a portfolio approach to their business activities, and how that impacts on decision making have to be built into more appropriate enterprise training and education approaches by BDS providers.

Banks are interested in use of mobile technologies to innovate their banking services, including money transfers. On the demand side, all of the owners use phones for communicating, and some are using smartphones for accessing the internet and emailing. Several of the ASMEs said they were looking at mobile money transfers, as they do need to move funds to pay staff, pay suppliers and to receive payments. It is possible that this could be an area of financial service that would be easier for banks, telecom companies and ASMEs to find a product/service package that is easier to provide and use than credit.

There are efforts underway by the Financial Strengthening Technical Assistance Program (FSTAP) on financial literacy, which is part of a wider recognition of the need for a better appreciation of finances in the everyday life of Malawians. This may assist over time to improve the level of financial literacy of those in businesses, but it is more likely that an extraordinary effort would be required to make a difference, and that it would need to be more focused on running enterprises, than on consumer awareness. The FinMark (2013) low income savings study highlighted that financial literacy can be overly focused on supply side views of literacy, by concentrating on financial service products like bank accounts, credit, savings and insurance. As the current study has highlighted, an enterprise can manage without ever having a bank account, savings at an FI, a loan or insurance.

One organization involved in support to the financial sector highlighted that banks in Malawi are *risk averse*, mainly because they have a ready market with large corporates, Treasury-Bills and foreign exchange that does not necessitate them taking much risk. SME lending is inherently more difficult, more risk and less efficient,⁵² so that it should not be a great surprise that it is not prioritized more and that the banks adopt a low risk approach. It may be that it is a lender with a smaller market share or a lender that is more solely focused on SMEs would be more likely to innovate and lead the market.

Banks did point out that the *Basel II guidelines* issued by Reserve Bank of Malawi requires banks to engage in secure lending which involves lending to less risky clients like corporate clients rather than non-secure lending to segments like ASMEs. Basel II has affected at least one bank's appetite for risk, as it now avoids non-secured lending. This suggests that there is a policy opportunity to provide incentives for alternatives to current secured lending models which predominate.

FIs also highlight that *the legal system* in Malawi is still slow even though the introduction of commercial courts has been an improvement. The ability to enforce security and recover debts is necessary for banks to consider more risk in their lending. An element that would support enforcement is the long awaited national identity card system and establishing functioning CRBs covering individuals and SMEs.

At this point in time, there are considerable obstacles to SME lending by formal FIs, which would require a concerted approach to address.

I.7 INFORMATION AND COMMUNICATION TECHNOLOGY

Mobile phone ownership is high and just under half of the ASMEs in the primary research had smartphones, which 87% were using to access email and the web in ways that they had not previously done for those that had a computer. A few ASMEs had begun to try mobile-money services. High smartphone ownership, use of the web and email and the advent of mobile-money services suggest there is scope for interventions that speed and extend uptake and use.

FinScope MSME (2012) asked about ownership of a number of items, some of which relate to ICT. Results are shown in the table below.

⁵² The process for assessing, disbursing and managing bigger loans is a similar to that for smaller loans, so many smaller loans to the same value of a few larger loans is more costly to delivery and operate, hence less efficient.

Table 26: Ownership of ICT Assets

<i>“Does the business own/rent/have access to the following?” (A13b)</i>	% of all Small	% of all Medium	% of all SMEs
A generator	4.6	25.0	6.0
Telephone/Landline	8.3	37.5	10.3
Cell phone	76.9	75.0	76.7
A fax machine/fax facilities	1.9	37.5	4.3
Credit card machine/Malswitch card	2.8	25.0	4.3
Computers	4.6	37.5	6.9
An email address	5.6	37.5	7.8
A website	0.9	12.5	1.7
Internet access	5.6	37.5	7.8

Source: FinScope MSME (2012), Consultants Analysis

As expected, over three quarters of ASMEs owned a cellphone followed by 10.3% with a fixed landline; all other communication equipment and means had access at less than 10%. Medium enterprises had substantially higher access on almost all items. The primary research supported the findings from FinScope. The only means of ICT that was commonly owned or accessible was a cellphone.

From the primary research, 30 respondents (45%) said they had a smartphone and of these, 26 (87%) had used their ‘smartphone’⁵³ for email and occasional internet access. The main concern for users was the slow speeds and access to signal in the districts compared to urban areas. FinScope did not differentiate smart and non-smart cellphones, and the higher usage reflects that smartphone have become more available and are being adopted by businesses in preference to getting a computer. Although the medium enterprises interviewed did own computers, these were used for keeping business records, with information sent by paper records or phoned in.⁵⁴ Computers were mainly used by finance and administration staff, and not by the owners. For ASME owners, the smartphone has many advantages in that it is portable and accessible to the owner wherever s/he is, so the smartphone enables email and internet access that previously was the preserve of the computer, but was not being utilized by owners for this. For medium enterprises, there is more need for computerized records, so they generally had both smartphones and computers, but email communication and web access for the owners is more through their phones than the enterprises’ computers.

In FinScope (2012), no businesses reported receiving payment by money transfer or internet, since the study was undertaken before the launch of mobile phone payment and transfers by TNM and Airtel. The primary research found three SME owners experimenting with making and receiving payments. Mobile phone transfers would be of use to ASMEs to make and receive payments. There is likely to be scope for mobile phone based solutions for ASMEs.

Other than the above, there was no reported use of ICT for other aspects of business operations.

⁵³ In this context, this refers to a phone that can access the internet and through the likes of Google, Yahoo and Hotmail then owners can operate an email account through the phone.

⁵⁴ One business (Mangochi) used minibus services to send paper records and stationery between its outlets.

1.8 COLLABORATION AND CLUSTERING (C&C)

There were examples of collaboration between ASMEs along the chain, and between competing ASMEs, particularly around fulfilling contracts. The only cluster found was around groundnut in parts of Mchinji District, which more reflect the high level of supply and related frequency of visits by traders from the region.

Collaboration in the context of this study is defined as when two or more separately owned enterprises in the same or complementary business areas work together to achieve a common beneficial business aim. In practice, this was likely to be around businesses working together to win contracts or new business, but it could be related to improving competitiveness through cost reduction or development of a more attractive product or integrated package, which in time would lead to addition custom and/or higher profits.

Clustering in the context of this study is defined as when two or more separately owned enterprises in the same or complementary business areas co-locate for mutual benefit, as a means to improve efficiency and/or offer an improved product or service to customers through that co-location.

This section includes Business Membership Organizations (BMOs) which are a specific type of collaboration.

There were no questions in FinScope (2012) that relate to collaboration and clustering. In the primary research, ASMEs were asked about collaboration and clustering. There were examples found of collaboration particularly traders sharing stock and transporters coming together to fulfill a large contract.

The examples on stock sharing have been covered under the section on traders (see Groundnuts and Soybean section), including the Dedza traders who were supplying the trader with stock for sale in Blantyre townships, rather than seeking a market themselves. The detail is not repeated here, other than to indicate that it is a common practice for traders to join their stock to fulfill a larger order.

The other main examples of *collaboration* related to transport.⁵⁵ One trader had formed a link with a wholesale business at Muloza on the Mozambique border. He regularly delivers produce there and has negotiated to take backloads from Muloza to Limbe/Blantyre on his way back to Ntcheu. This gives both parties a cost efficiency that is shared between them.⁵⁶ Most of the transporters indicated that they collaborate when trying to get contracts with bigger firms. The large firms do not want to negotiate with lots of transporters for multiple vehicles, but want one contract, leaving the transporter(s) to sort out their logistics. The transporters form informal groups and have informal agreements on how to fulfill the contract, including on sharing the profits. For example, the transporters in Machinga collaborate to get ADMARC contracts.

In relation to *clustering*, there were examples of where several businesses of the same type are co-located, but these were less deliberate choices to co-locate, but rather businesses clustering where there were more business opportunities.⁵⁷ For example, there is a concentration of groundnut traders in Mchinji, and this appears to attract international buyers from Southern and West-Central Africa due to high demand in their home markets. However, the traders have not deliberately clustered for mutual advantage, but rather are in centers like Waliranji where there is a high concentration of supply and proximity to the border for ease of formal

⁵⁵ Sometimes this is just about one transporter with a contract having committed his vehicles to another contract, and so needing additional vehicles. This is essentially a subcontracting arrangement rather than a true collaboration

⁵⁶ If the trader did not have a backload, it is likely that his drivers would negotiate their own deals and be transporting goods using his transport, but with the money being paid to the driver, so having certainty on backloads avoids this risk.

⁵⁷ Transporters forming a transport rank for vehicles to hire, is a form of clustering through choice, as it attracts customers through offering a wide range of choices, but this not the type of clustering that is sought in this study.

and informal access. This is clustering through competition, not as a strategic choice. Supporting services are also clustered for the same reasons, such as transport.

In terms of BMOs, there are several SMEs groupings in Malawi targeting (M)SMEs, being the National Association of Small and Medium Enterprises (NASME), the Indigenous Business Association of Malawi (IBAM) and the Economic Empowerment Action Group (EEAG). The Small and Medium Enterprise Association (SMEA) has been formed within the second quarter of 2014 and appears to have some more respected individuals on its Board, but it is too new to know if it can build a viable membership base and be effective in its operation.

According to the MoIT,⁵⁸ these BMOs do not collaborate, but rather compete with each other, seeking to gain the status of the main/lead organization with which GoM consults. Mostly, the MoIT works with NASME for historical reasons, but other key informants questioned if any of these BMOs have significant numbers of subscribing MSME members as a basis for their legitimacy. According to MoIT, it does get requests from BMOs to intervene in situations where members are having problems, but these are mostly trade disputes that are more appropriately dealt with through arbitration or legal processes if they cannot be solved by the parties. NASME reports that it does get invited to participate in trade fairs in Malawi and the region, to which it invites some members to participate, but the challenge is usually funding, so if there are no GoM funds or development partner funds, then the opportunities cannot be taken up. There are also occasionally loan funds available to SMEs through NASME, but these are reported to be very limited and sourced from GoM or development partners.

The MCCCCI has been much longer established as a BMO and has gone through several phases in which it was dominated by MSEs⁵⁹, but now focuses more on medium and large enterprises. MCCCCI has around 250 members nationally, including SMEs, but this is a relatively small proportion of SMEs and likely these will be more urban based firms. MCCCCI does offer more services to members, including access to training, access to events/speakers, information bulletins (macro-economic), and opportunities to engage with public officials and government (such as the post Budget events). MCCCCI is also invited to sit on a number of bodies, as a private sector representative, such as the National Export Strategy implementation/'task' groups and to engage with government in consultations on issues affecting private sector. MCCCCI manages a Public Private Dialogue) forum, but with little progress in recent years.

From the primary research, none of the 68 ASMEs interviewed were members of these national BMOs. This may reflect the limited activities to recruit and support district members, but also that SME owners see limited benefits from subscription to generic/national SME BMOs.

In contrast, 10 respondents (agri-input dealers) were members of the Seed Traders Association of Malawi, one was a member of the Poultry Association of Malawi (feed processor) and one was a member of the Fertilizer Association of Malawi (agri-input dealers). As noted, the traders in Mitundu were forming their own area-based traders association.

In conclusion, it appears that opportunities for representation of SMEs are more likely to be better served through trade/sector and even locally based representative organizations than national BMOs.

⁵⁸ Based on the poor reputation of these bodies with other stakeholders and the lack of awareness of them among SMEs, the consultants did not prioritize interviews with these groups.

⁵⁹ This made it susceptible to capture by politically minded individuals who could sign up members to vote for them as Chamber President. President Muluji is a former MCCCCI President.

I.9 ENABLING ENVIRONMENT

This section gives detail about the MoIT and its MSME draft policy; it reviews compliance, licensing and registration for SMEs. Interventions in the enabling environment are limited, but the implementation of the Ministry's functional review may bring forward opportunities.

1.9.1 MOIT STRUCTURE AND PSD PROJECTS

The MoIT and its key affiliates is the subject of a functional review that is awaiting implementation. This would shift MoIT to a policy and oversight role.

The MoIT is responsible for MSMEs, and has a separate department dealing with SMEs within the Private Sector Division. This is a relatively junior section of the Ministry, compared to the Department of Trade, and it is understaffed. Within the MoIT, there are various task groups operating in support of the Trade, Industry and Private Sector Wide Approach (TIP SWAp). One of the key technical working groups of relevance to SMEs in the MoIT is the Access to Finance (A2F) Group, which is supported by a technical adviser. This group is involved in research co-ordination and engages with the financial sector players on MSMEs, not just SME finance. DFID funds the TIP SWAp coordinator.

MoIT has two main affiliated organizations for which it is responsible, being the Malawi Investment and Trade Center (MITC) and the Small and Medium Enterprise Development Institute (SMEDI). A functional review of the MoIT, funded by DFID is awaiting agreement on implementation.⁶⁰ This will refocus the MoIT more on policy and regulation and less on implementation activities with a revision to the mandate covering six areas:

1. Create a conducive business environment
2. Remove trade barriers
3. Improve alignment to markets
4. Negotiate international agreements
5. Set strategic direction
6. Collaborate inter-institutionally

These reflect current trade and private sector development priorities. The functional review has not been agreed, but it already reflects changes and activities that are underway. For example, the MoIT developed a National Export Strategy (NES) in 2011 focusing on several sectors, including sugar, manufacturing and oilseeds (including groundnut and soybean). There are technical working groups supporting 'oilseeds' and the other focal area, and each technical working group is supported by an externally contracted technical advisor supported by either United Nations Development Program (UNDP) or DFID.

MITC has both an investment and trade promotion mandate, reflecting its merger out of MIPA and MEPC. In terms of investment, the mandate is split into promotion and facilitation. In the past, the focus of MIPA support was on international relatively large investors, though it was not very successful in this, due to the relatively weak investment climate.⁶¹ Malawian SMEs mostly did not seek MIPA's assistance. It is too early to say if MITC will prioritize SMEs and if it will be successful at promoting and facilitating SME investment.

⁶⁰ Presentation of Strategic and Functional Reviews for MoIT, MITC and SMEDI, Deloitte Monitor, 2013

⁶¹ Investment Climate Assessment, RPED, (2006).

MITC also has a mandate for trade promotion and facilitation, taking over from MEPC, which was ineffective in this role, particularly in relation to SMEs. It is as yet unclear how it will pursue its mandate, though a functional review has been conducted, and is waiting for MoIT to determine the way forward.

SMEDI was formed out of the Malawi Entrepreneurship Development Institute (MEDI), the Development of Malawian Traders Trust (DEMAT) and the Small Enterprise Development Organization of Malawi (SEDOM). Whereas the merger of MIPA and MEPC was for efficiency reasons and improved co-ordination between these two areas, the merger of MEDI, DEMAT and SEDOM was more to reduce overlapping mandates and address weak performance. SMEDI's proposed mandate is to:

1. Advocate for an improved SME environment
2. Develop collective and individual (start-up) entrepreneurs (though information provision and coordinating BDS)
3. Develop sustainable (established) MSMEs (though information provision and coordinating BDS)
4. Enhance access to finance (facilitate linkages, identify gaps and advocate for change)
5. Improve information available on and to MSMEs (conduct research and disseminate)
6. Enable MSMEs to compete in markets (investigate and improve standards)

DFID is committed to support for SMEDI, though the final mandate and roles are not yet settled, with some debate over SMEDI as a BDS provider, rather than BDS coordinator (points 2 and 3 above). Activities have commenced on the design of improve information flows from SMEDI through developing an information center supported by website and inter-active communication with MSMEs.

Compared to the recent past, the MoIT is now relatively well supported with technical advisors and is the focal point for several development partner funded projects, including support for the Malawi Innovation Challenge Fund (MICF) funded by DFID through UNDP, the Malawi Competitiveness and Job Creation Support Project (MCJCSPP) funded by African Development Bank) and the Malawi Oilseeds Sector Transformation (MOST) Project funded by DFID. MICF will⁶² focus on manufacturing through a challenge fund mechanism, MCJCSPP is focusing on a mix of subsidized BDS (entrepreneurship development, mentoring/counseling), standards, access to finance (FI capacity building) and value chain activities (pigeon peas and soybean),⁶³ while MOST is taking a market systems approach to facilitating development in four oilseed markets including soybean and groundnut, supported by DFID.⁶⁴

The Malawi Bureau of Standards (MBS) and TEVETA are affiliated with the MoIT. In practice these are more service than development institutions, and both use levies and charges on users and the whole business community to support their activities. In the primary research, MBS did commonly interact with district players, notably traders, checking their scales and other standards for their premises. Some of the processors indicated unexplained long delays in getting certification for their products from MBS. Because MBS certification is not accepted outside Malawi, then this is a problem for exporters that need to get a recognized certification,

⁶² MICF is mobilising as the time of this report.

⁶³ This takes on the previous role of the World Bank's Business Environment Strengthening Technical Assistance Project (BESTAP).

⁶⁴ In addition, there are other important established projects in the FTF areas of focus but not connected to the MoIT, notably the Integrating Nutrition in value chains funded by USAID and the Rural Livelihoods Economic Enhancement Project (RLEEP). INVC is focusing on all three target value chains, with initiatives primarily relating to production of these, but also with attention to improving efficiency and functioning in the value chains. RLEEP is focused on a similar mix of production and value chain enhancement activities (including soybean). More recently the African Alliance for the Greening of Africa (AGRA) has begun implementing a seed project including groundnut and soybean.

typically via testing in South Africa. To address this weakness in certification, MBS has very recently commenced a project funded through the MCJCSP to cover Standards, Quality Assurance and Metrology (SQAM), including consulting with SMEs on their requirements. TEVETA offers skills training in a range of trades that are used by the business community, funded by a levy on businesses over a threshold level. TEVETA can do firm specific training, but this is mainly benefiting larger firms.

MIRTDC operates from Blantyre and undertakes training of enterprises in its technologies, but it reaches few SMEs.

Finally, One Village, One Project (OVOP) comes under MoIT. This former Presidential initiative seeks to promote village level enterprise, but has been ineffective and appears to be low priority. In the past it has supported oil processing, including groundnut oil in Mitundu and Mchinji. According to the MoIT, OVOP groups have failed to gain MBS certification for their products as they do not have the capacity or resources to do so.

At the time of this assessment, there are many initiatives around the business enabling environment, trade and MSMEs, making the arena relatively crowded. Many of these initiatives are less than six months old and how effective they will be is yet to be seen. At this point, there are no clear gaps or opportunities to work with MoIT and other public sector affiliates to promote SME. It would be appropriate to wait for the various reviews to the mandate to be finalized to see if these might generate opportunities.

1.9.2 MSME (DRAFT) POLICY

The MSME Policy is awaiting approval, but may be changed post the election. It addresses issues of policy, value chain operation, access to finance, BDS, ICT and legal and regulatory environment.

The MoIT's draft MSME policy proposes greater coherence within GoM to support MSME development, better co-ordination between GoM bodies and development partners, and engagement with private providers and MSMEs.

The draft MSME policy and accompanying strategy proposes activities in six areas:

1. Enhance policy integration and implementation
2. Improve the operation of value chains
3. Improve access to finance
4. Improve BDS to MSMEs
5. Improve information skills, standards and technology
6. Promote an enabling legal and regulatory environment

1. Policy integration and implementation – The aim is to improve the institutional structure so as to facilitate MSME development. The focus of activities include enabling SMEDI to undertake its enhanced mandate, establishing inter-ministry coordinating body supported by task teams, engaging the President through a bi-annual MSME conference and introducing a Small Business Act.

2. Operation of value chains – The aim is to improve links between small and large enterprises and address the missing middle. There is a focus on small agricultural producers, with reference to capacity building and embedding services through large enterprises. The focus of activities is to establish the Malawi Innovation Challenge Fund (MICF)⁶⁵ so as to promote business to business, large to small linkages, establish a strong

⁶⁵ MICF has just commenced its mobilization.

value chain research facility at SMEDI and support the implementation of the National Export Strategy (NES).

3. **Access to finance** – The aim is to build sustainable financial systems to support MSME development and growth. The focus of activities is establish a venture capital fund for smaller enterprises, support a financial innovation fund to stimulate innovation by FIs that address MSMEs (particularly youth and women), review the tax regime to stimulate registration of MSME and support a national identity system.

4. **BDS** – The aim is to provide effective MSME support programs and initiatives adapted to various groups. Activities focus on support to establish SMEDI in harmony with Malawi Investment and Training Centre (MITC), support a mentoring and counseling facility for faltering businesses, support for incubation centers in the districts and artisanal sheds, co-ordinate BDS providers, association and MSME representatives, establish a national database of providers and introduce entrepreneurial training in more languages.

5. **Information, skills, standards and technology** – The aim is to bridge the knowledge and information gap around improved technologies and standards for MSMEs and to improve enterprise development. The focus of activities is to develop a web-based portal to provide information to MSMEs, promoting trade fairs, institute entrepreneurship in the curricula at all levels, review standards, quality assurance and metrology system to enable exports, training in standards and promoting annual awards for entrepreneurship.

6. **Legal and regulatory enabling environment** – The aim is create a conducive environment for MSME growth. The focus of activities is to improve the availability of data (disaggregated), review key laws and regulations to amend those that inhibit MSMEs, analyze the costs of compliance and reduce red tape, implement legislation on Business Registration and improve communication around MSMEs.

The MSME (draft) Policy was presented to Cabinet, which requested that it be amended to incorporate a minimum 20% of GoM procurement through MSMEs. This is potentially problematic on several fronts:

1. The MSME (draft) Policy does not define MSMEs in a way that is definitive. In particular, the employment criterion does not define if employment is full-time, full-time equivalent or on a headcount basis, nor does it address issues like counting the owner, family and any unpaid employees.
2. The ownership of multiple enterprises by a single owner or set of owners suggests that owners might just spit a bigger business into smaller business units to get within thresholds. Feedback validation from the workshop was around ways to ensure politically connected business-people were excluded and not able to take part; otherwise bigger firms may just be being excluded from bidding, making bidding easier for less competent smaller firms.
3. GoM purchasing has a number of large elements, such as the FISP, that it would be problematic to break into smaller contracts. With certain large elements that cannot easily be changed to incorporate MSME procurement, then it means the proportion of those contracts that are potentially deliverable by MSMEs has to be higher than 20%, and may not be possible in practice.
4. Many of the SMEs that had contracts with GoM complained about late payment and several stated that they would not be willing to supply government again. Without attention to late payment, then MSMEs may get preferential access, but then suffer losses due to having their capital tied up for long periods. Selling to GoM is an inherently risky option.

A better approach could be to ensure contract/bid requirements do not unintentionally and unnecessarily exclude smaller firms, and to focus on ensuring that payment of MSMEs is prioritized and within mandated limits enforceable in law. This would probably also necessitate a clearer definition of what is a MSME and there would need to be a more efficient process or registration of MSMEs than at present (see next section).

An amended policy will need to be approved by the incoming government. This may result in further changes and almost certainly delay in approving a final MSME Policy and Strategy.

1.9.3 COMPLIANCE WITH REGULATION/LEGISLATION

It is difficult to determine compliance with regulations/legislation as respondents to FinScope and primary research have an incentive to state they are compliant. Other secondary studies have highlighted generally poor implementation of regulations/legislation. Small enterprises in particular show low compliance.

According to stakeholders, Malawi has most of the rules that might be expected for a functional business environment, but the implementation is weak with many businesses operating informally and practically outside the rules. This is highlighted in the following responses in FinScope (2012):

Table 27: Compliance with Regulations, 2012

“Which of these, if any, does this business submit or act in accordance with?” (E7)	Yes		No		Don't know	
	Small	Medium	Small	Medium	Small	Medium
Income Tax	28.7	62.5	58.3	25.0	13.0	12.5
PAYE (pay as you earn)	12.0	50.0	74.1	37.5	12.0	12.5
VAT (Value added tax)	22.2	62.5	60.2	12.5	15.7	25.0
Minimum wage requirement	27.8	62.5	50.9	12.5	19.4	25.0
Return of earnings	11.1	62.5	63.9	12.5	22.2	25.0
Basic condition of employment	18.5	62.5	55.6	12.5	24.1	25.0
Employment Act	24.1	50.0	53.7	25.0	20.4	25.0
Labour Relations Act	19.4	50.0	54.6	25.0	24.1	25.0
TEVET and Skill Development Levy	4.6	37.5	70.4	25.0	23.1	37.5
Access to information	11.1	37.5	59.3	37.5	26.9	25.0
Health regulation	37.0	37.5	46.3	37.5	14.8	25.0
Zoning laws or regulation	28.7	12.5	50.9	62.5	18.5	25.0

Source: FinScope (2012), Consultants Analysis

It should be noted that compliance is not required on all the above for all enterprises. For example, Pay As You Earn (PAYE) is only required if a business employs others, which many micros do not. The TEVET levy and other pieces of legislation also have thresholds for compliance based on number of employees. Value Added Tax (VAT) has a turnover threshold below which a business does not have to charge and remit VAT. As a result the above gives a misleadingly negative picture on face value. However, there is likely to be an overstatement of compliance by SMEs as they may not fully appreciate the requirements of the rules (like ‘health regulation’) and they would not wish to respond that they are breaking one or more laws when responding to this question. Finally, several of the categories are not clear what they cover and would be difficult for an owner to know what the rules are, such as ‘Health regulations’, ‘Zoning’ and ‘Access to information’; some are also overlapping such as on employment and it is simply not realistic to ask an owner if he complies with a specific piece of legislation that s/he is unlikely to know the contents of.

Looking at the above results in general terms, as would be expected there is generally lower compliance by small enterprises compared to medium enterprises. There is no pattern to the responses with relatively similar levels across the board, other than for TEVET levy which is very low for small enterprises, which would be

expected as they are not required to comply. The high level of don't know responses suggest either an unwillingness to admit that they do not comply, or poor understanding of the rules.

1.9.4 LICENSING AND REGISTRATION

Licensing is enforced at district level as it is an effective means to raise revenue and evasion is difficult for fixed premises owners. Registration is a legal requirement, but registration of a legal entity is relatively rare, as it is poorly enforced. Where registration is required, such as if tendering for formal contracts, ASMEs report delays and challenges at the Registrar General office, which requires them to register in Blantyre. Planned and funded improvements, such as online registration are not yet being implemented by the Registrar General.

In relation to licensing, FinScope (2012) recorded the following:

Table 28: Proportion of SMEs that are licensed, 2012

<i>Is the business licensed? (E5)</i>	<i>% of all Small</i>	<i>% of all Medium</i>	<i>% of all SMEs</i>
Yes	25.9	75.0	29.3
No	74.1	25.0	70.7
Total	100.0	100.0	100.0

Source: FinScope (2012), Consultants Analysis

The responses to this question appear to be affected by the interpretation of what is licensing which researchers and respondents may have confused with registration. At district level, it would be difficult to avoid being licensed by the District Assembly, particularly in the main trading centers. Licensing is an important and relatively easy to collect income stream for the District Assembly, so it is generally enforced. A business with fixed premises would find it hard to avoid. In the primary research, 59 (87%) ASMEs said they were licensed and only one was not, though a further eight said that it did not apply to them.

Table 29: Source of License

<i>With whom are you licensed? (E6)</i>	<i>% of licensed small enterprises</i>	<i>% of licensed medium enterprises</i>	<i>% of licensed SMEs</i>
Ministry of Industry and Trade	21.4	-	17.6
Local City Council	14.3	16.7	14.7
City Council	28.6	16.7	26.5
Other	35.7	66.7	41.2
Total	100.0	100.0	100.0

Source: FinScope MSME (2012), Consultants Analysis, n=34

The above responses are also contrary to expectation, as it ought to be more likely to have licensing by City Council (urban) or local City Council (presumed to be District Assembly). It may be that those responding other meant City or District Assembly. The responses overall may just reflect general confusion by SMEs as to what licensing is required and also a poorly worded question.

Businesses are required to register a legal form and business name with the Registrar of Companies, with the Registrar General's office either as limited liability companies, partnerships or sole traders. The exception for

businesses is Co-operatives which have to be registered with the MoIT. There are other forms of organization, such as associations,⁶⁶ but these are used by groups, and should not be classed as SMEs. According to FinScope (2012) the proportion of businesses registered is as follows:

Table 30: Proportion of SMEs Registered, 2012

<i>Is the business registered under the Business Name Act (Registrar of Companies)? (E1)</i>	<i>% of all Small</i>	<i>% of all Medium</i>	<i>% of all SMEs</i>
Yes	17.6	37.5	19.0
No	82.4	62.5	81.0
Total	100.0	100.0	100.0

Source: FinScope MSME (2012), Consultants Analysis

This shows a lower proportion of SMEs registered than licensed, which is what would be expected. Reasons for registering are set out below:

Table 31: Reasons for Registering, 2012

<i>What do you think is the main benefit of being a registered business? (E4)</i>	<i>% of all Small</i>	<i>% of all Medium</i>	<i>% of all SMEs</i>
Comply with the law	8.3	-	7.8
Avoid harassment from	4.6	-	4.3
Avoid fines	-	12.5	0.9
Issue receipts	-	12.5	0.9
Access to finance	24.1	12.5	23.3
Less bribes to pay	-	-	-
Access to government	14.8	-	13.8
Access to new clients	12.0	37.5	13.8
Access to raw materials	-	-	-
Other	2.8	-	2.6
Don't know	30.6	25.0	30.2
No benefits or none	2.8	-	2.6
Total	100.0	100.0	100.0

Source: FinScope (2012), Consultants Analysis

The main reason for registering given by small enterprises was 'access to finance' and for medium enterprises was 'access to new clients'. For small enterprises, there was also recognition that registration was necessary to get new clients and government contracts. However, the highest proportion of respondents for small enterprises was that they did not know what the benefits were, and had probably not considered them.

For those that had not registered their business, the reasons are given in the table below.

⁶⁶ The Registrar General also handles the registration of Associations/Trusts.

Table 32: Reasons for not registering a business

<i>Please tell me why you have not registered this business? (E3)</i>	% of all Small	% of all Medium	% of all SMEs
Don't have money to register	7.4	-	6.9
It is too complicated	0.9	-	0.9
No benefit	2.8	12.5	3.4
The business is too small	30.6	-	28.4
Don't want to pay tax	3.7	-	3.4
Don't know how to	33.3	50.0	34.5
Registration is being processed	2.8	-	2.6
Other	1.9	-	1.7
Don't Know	4.6	-	4.3

Source: FinScope (2012), Consultants Analysis

The reasons given by small enterprises for not registering were that they did not know how to (33.3%) and the business was too small (30.6%). For medium enterprises, the predominant response was not knowing how to register. These reasons point to a need for a simple and accessible method to register a business. Only 12 (18%) of ASMEs in the primary research were registered, though there was considerable confusion over what registration was, typically being confused with licensing.

According to the Registrar General and MoIT, an initiative is underway to simplify registration for MSME, move it online and provide regional access points. This appears to be imminent, but there continue to be unexplained delays, perhaps from those who want to keep the current system which requires those wanting to register to travel to Blantyre. There are reports of rent seeking from businesses which are made to wait and resubmit.

2 WAY FORWARD

This final section takes the findings and sets out a way forward grouped under BDS, A2F, ICT, Collaboration and clustering and enabling environment. Each section summarizes the main challenges from the foregoing findings, then sets out possible interventions for action that related to gaps that other development partners and GoM are not addressing and finally makes recommendations. It is important to note that **these possible interventions are not mutually exclusive and in many cases are highly complementary.**

2.1 BDS

This section sets out the challenges around BDS for ASMEs, possible interventions for addressing these that are not currently being fully addressed by other development partners/GoM and then makes a recommendation.

2.1.1 BDS CHALLENGES

The major challenges identified in the BDS field relating to ASME development are:

1. Low uptake of BDS by ASMEs despite provision by private, public and NGO sectors
2. Poor co-ordination between BDS providers
3. High subsidy of BDS providers by government/development partners to make BDS affordable to ASMEs
4. Service relevance of BDS providers to ASME owner-manager priorities is low
5. Appreciation of the nature of ASME owner-managed enterprises by BDS providers is low

6. BDS outreach in districts is low

2.1.2 BDS POSSIBLE INTERVENTIONS

The possible interventions for USAID support in BDS include:

BDS Intervention 1: Assisting private, NGO and public BDS providers to refocusing services to be relevant to ASMEs

The analysis in the BDS findings section (see section 1.5) highlighted that most BDS providers have an incorrect conception of SME ownership and operation. Training and advisory services are based on models that are often drawn from business management theory for ‘corporates’, seeking to get SMEs to mimic corporate forms and approaches to enable them to perform like larger businesses. In reality, there are fundamental differences between corporates and SMEs in their size and resources and in the nature of their management, with ‘professional’ employed managers running corporates and owner-managers running SMEs. The totemic symbol of this mini-corporate approach is the focus on developing business plans. SMEs only consider these when they want to raise finance, as this is a bank requirement; they do not use them for guiding strategic choices and business direction.

More useful to a SME manager is to learn enterprising approaches to planning and decision making, supported by key skills, such as working out capital requirements and cashflow, calculating profitability, assessing risk and managing growth. This requires most providers to re-orient their services to owner-managed enterprise models rather than seeking to make SMEs mimic mini-corporates.

This intervention could be enhanced through the development of a ‘community of practitioners’ and possibly by some form of certification of providers.

USAID could support interventions that target private, public and NGO BDS providers to re-orient their thinking and develop more ASME-focused BDS.

BDS Intervention 2: Embedding BDS provision in value chain players and other supporting value chain bodies

BDS is primarily delivered by specialist BDS providers or organizations that include BDS in their mandate alongside other developmental activities. BDS providers typically lack regular direct access to potential clients as their services are ‘one-off’ and out of the normal day to day business activities. As a result they lack an established relationship with SME owners and this makes it difficult for the SME to select an appropriate and trusted BDS provider.

In addition, because BDS are delivered as one-off services, they are not integrated with other activities that could either generate income or spread the cost of delivery, compared to where a provider has an ongoing set of activities, with a BDS added and integrated to enhance the offer and strengthen the existing relationship.

This could include processors and major buyers who want to strengthen aggregators and transporters; and input firms strengthening their dealers/agents. This could be bundled in a supply chain management offer to firms.

Other bodies that work with ASMEs could include some of the more functional trade associations and supporting organizations. As noted in the findings section on groundnut/soybean (see section 1.4.1), CNFA pro-

vided training in stock management and financial management to agri-input dealers, alongside facilitating access to credit. 10 ASMEs were members of STAM, the seed trade body. This approach seeks to ‘embed’ BDS within the value chain.

USAID could support private, public and NGO value chain actors to enhance their existing engagement and relationships with ASMEs by embedding appropriate BDS to their ongoing value chain activities

BDS Intervention3: Work with FIs to support BDS to ASMEs that seek to raise formal finance using a PASS-variant model

The one point where SMEs do seek out BDS providers is when they want to raise finance, as it is a requirement from the banks to present a business plan with supporting financial projections. Yet, all the banks indicated how poor quality many of the business plans were. SMEs use a range of BDS providers, including accountants and government staff preparing plans as a private job. This becomes a frustrating exercise from both the SME and banker sides.

PASS (see section 1.5.3) works with banks to understand their requirements and with ASMEs to develop appropriate business plans with a much improved chance of success. The package is facilitated by a guarantee fund, which gives the banks more confidence and from which the fees paid by banks go to subsidize the support to the ASMEs. Two variants could be considered. Firstly, using USAID’s Development Credit Authority (DCA) as the guarantee fund enabling USAID to leverage its existing investment. Secondly, business advisors working with ASMEs could be trained to analyze the financing requirement and advise ASMEs whether it is appropriate to prepare a business plan at all. Instead, they could advise the ASME to make adjustments to the business operations that release cash from under-utilized assets, increase cash flow from changing the client profile (moving away from supplying poor paying customer groups), and improve internal efficiencies that save cash. The presumption should not be that because an ASME has asked for help, or been referred by a bank to get help with a business plan, that it is always appropriate to follow through and prepare one, when other measures are more beneficial to the business. In a climate where interest rates are punitively high, it could be a negative impact to facilitate more borrowing that ultimately leads to a default situation. Financial analysis should consider a range of external finance options and advise ASMEs accordingly.

Such an approach would require buy in from at least two to three significant ASME-focused FIs, who would accept this more independent advisory approach, knowing that the proposals that ultimately came forward would be fewer but of much better quality.

USAID could support a new project or an existing capable entity to develop and implement a PASS-variant model.

BDS Intervention 4: Research, develop and support the implementation of lower cost delivery models for business information and access to advice/advisory service

The research found that BDS provision is not widely accessed and used by ASMEs. Part of this relates to the inappropriate offers by providers, which are addressed by BDS intervention 1 above. However, a fundamental challenge for BDS providers is the cost of undertaking ‘one-to-one’ and ‘one-to-few’ delivery that is implicit in business advisory and training services. These have to be delivered ‘face-to-face’ which means reach is limited and that they are much less accessible to district based ASMEs, as the vast majority of providers are urban based.

FinScope MSME (2012) highlights low penetration of computers and the primary research found that few owners were using their computers themselves, but having their staff consolidate figures from outlets as a purely administrative function. Technology advances, in particular the adoption of smart phones, is a potential game changer, as the primary research showed that owners appear to be using their smart-phones for email and accessing the web, in a way that even the few that had computers were not doing so. This creates the opportunity to provide them with appropriate ‘decision-taking’ material that supports what they find they need to do at any particular time. Material can be tailored to demand-side stated problems, like: ‘how do I get more customers’, ‘how do I get debtors to pay’, ‘how do I calculate the cost of a new vehicle’, ‘how do I limit my risk of theft’, etc. Owners could sign up for regular business messages and/or use smart phones to access an interactive data base via Apps. These could also provide links to a business advisory service, if appropriate.

There is also scope to support cellular messaging with website(s) and other media such as radio sessions for businesses and ‘tablets’ to show well-produced short training programs.

A supporting concept is that ASME owners could benefit from learning key computing tools like excel (see A2F Interventions below) that could be accessible via a smartphone in conjunction with a MNO offering a paid ‘cloud-based’ service to ASME owners.

This approach could leverage USAID investments in systems like Esoko and the mobile-money work of FHI 360. DFID is working with SMEDI on an information center that might adopt some of these more interactive approaches, but there appears to be plenty of room for

USAID could support existing or new BDS providers to develop smart-phone based applications that enable access to ‘decision-taking’ materials and as an entry point to other BDS offerings.

2.1.3 BDS RECOMMENDATION

Across developing and even developed countries, BDS has faced challenges to address access, cost and relevance.

Intervention four above could build on previous USAID investments and represents an opportunity to leverage these and catalyze a major change in BDS, not only in Malawi, but potentially beyond. It could be delivered through a challenge fund approach or a project that works through a mixture of direct intervention and challenge funding. All four interventions are viable and have potential for Malawi.

It is recommended that USAID should pursue a combination of the above interventions, combining intervention 4 with any or all of interventions 1, 2 and 3.

2.2 A2F

This section sets out the challenges around A2F for ASMEs, interventions for addressing these that are not currently being fully addressed by other development partners/GoM and then makes a recommendation.

2.2.1 A2F CHALLENGES

The major challenges identified in the A2F field relating to ASME development are:

1. Weak financial management skills particularly cashflow, working capital management and calculating viability
2. Low appreciation of ASME operating conditions and limitation by FI staff and product/service designers, which result in missed service opportunities, such as in transactions

3. Insufficient information and capacity by FIs to assess risks in different types of ASMEs and different sectors, leading to risk averse collateral based lending
4. Low uptake of the wider range of formal financial services by ASMEs including credit, due to low owner understanding, poor accessibility in decentralized locations and high cost of services
5. Titles not available on district properties, limiting collateral

2.2.2 A2F POSSIBLE INTERVENTIONS

The interventions for USAID support in A2F include:

A2F Intervention 1: Support demand-led financial innovations targeting ASMEs

SMEs are using a range of non-formal finance options particularly in credit, but also risk management. There is a mismatch between formal FI financial offers and the demand side needs of SMEs. Efforts by FIs are focused on getting SMEs to comply with their requirements, as they make the decision to accept credit applications or reject them. SMEs are three times more likely to borrow from business friends than a formal FI.

A major part of the problem is that FI staff do not appreciate and understand owner-managed ASMEs and want to view the needs only from the FI perspective, without seeing how that effectively excludes viable lending options. These include non-collateral based lending based on contracts and cashflow, leasing and different forms of factoring debt. In relation to transactions, there is scope for products that enable payments to staff and suppliers from cellphones as well as improved internet banking access through smart-phones.

This intervention could be enhanced by training bank staff, so that a new cadre of bank staff brings improved understanding of, and attitudes towards ASMEs, as well as better understanding of agri-business. Alternatively, this could be taken as a separate intervention or added to one of the interventions below, notably A2F Intervention 3 below.

The MoIT's MSME draft policy includes a proposed financial innovation fund.

USAID could support financial innovation generally, or focus on particular segments, such as ASME lending or cell-based applications.

A2F Intervention 2: Support for ASME financial education

The findings of this study indicate that there are gaps in ASME owner financial literacy and capacity. Although these are often highlighted by FIs in terms of poor record keeping, and weak business plans, there are gaps in ASME owners' ability to, for example, manage cashflow, manager working capital, determine viability of specific activities/investments and determine business unit profitability.

FSTAP has been supporting financial literacy for consumers, but this is limited in scope and not sufficiently tailored for ASME financial education needs. Several FIs are engaged in enterprise training initiatives to a limited extent. Currently, training in finance tends to adopt a supply side approach with too much focus on financial records, business planning and use of financial products. What is needed is more focus on day-to-day business issues that owners need to address, such as working out the running cost of a vehicle/outlet, breakeven points of investments, and cashflow requirements for supplying a contract. Financial education needs to be more practical and of immediate application, with more emphasis on using tools, like Microsoft Excel, than on how to keep records or construct a balance sheet.

An important element of financial education concerns investment and the benefits of 'deferred gratification' from investing now, limiting owner's drawings, in order to grow more rapidly and reach a higher level.

Owner-managers need to understand the issues around investing in a range of businesses, and strategies that can preserve capital and liquidity to benefit from new/arising opportunities

This intervention has synergy with the BDS interventions, as finance is likely to be a major subject for BDS content, or could be a standalone initiative from the BDS interventions, though adopting similar principles on approaches.

USAID could support financial education targeting SMEs, in conjunction with BDS interventions

A2F Intervention 3: Support for initiatives to improve borrower identification and credit status

Attempts to implement a national identity system have failed to make progress for many years, apparently stymied by politicians who see the advantages in keeping it on hold. It has been possible to establish a Credit Referencing Bureau for several years, but there seems to be no will to implement the Act through issuing the necessary enabling guidelines. With advances in biometric technology, it is technically possible to establish a bank-managed bio-metric database that would record every borrower and their track record, so as to allow participating banks a mechanism to reference check the identity and the record of borrowers. This would give banks greater comfort to lend to those with good records, and to even compete for their borrowing through better terms for those with good records. It would also underpin new forms of lending that do not depend on collateral for those with good records. Those with poor records could be excluded.

As noted in A2F Intervention 1 above, this intervention could be enhanced by a training program for bank staff in SME owner management and agri-business.

USAID could support an initiative by banks for developing a bio-metric database for ASME lending

A2F Intervention 4: Support for a wider range of bank guarantee mechanisms

This intervention is partly related to BDS Intervention 3 for a PASS-variant BDS-bank guarantee model, but here the focus is more on developing the range of guarantee mechanisms. Currently, USAID has promoted the DCA with a measure of success, but still not fully taken up. There is scope to leverage the DCA funds in support of a BDS program like PASS, which would improve lending and guarantee uptake. There is scope to offer wider range of guarantees that could be tailored to particular market gaps, focusing at categories of ASMEs, such as traders or transporters. Guarantees could also focus on particular value chains, though as noted, ASMEs tend to span several value chains and move in and out of particular activities.

A further intervention is for supporting wholesale funds to MFIs lending to small enterprises. MFIs are likely to better reach and bridge the understanding gap between FIs and ASMEs, though they would still need capacity development support. PASS has supported wholesale fund guarantees for MFIs in Tanzania.

USAID could support a PASS-variant model with that leverages bank lending through one or more bank guarantee products

2.2.3 A2F RECOMMENDATION

A2F regularly tops survey findings on SME stated needs. This can sometimes overstate the requirement, as SMEs may see credit as a response to lack of finance without exploring the full range of steps they can take, short of borrowing. With very high actual and real rates, then ASMEs need to be cautious to take on debt. However, in time there will be opportunities when it would be appropriate to increase borrowing.

To enable this, the above for A2F interventions could strengthen the FI capacity to offer appropriate products, with owner-managers having a better appreciation of what is the best way to manage the finances of their businesses. Supporting mechanism like a borrower biometric database would help banks reduce their lending risks and guarantees could also be effective at encouraging lending where the risk profile is right. These four components can work synergistically or taken as standalones or in some other combination.

It is recommended that USAID should prioritize interventions 1 and 2 including capacity building of FI staff, though interventions 3 and 4 could also be integrated into a program.

2.3 ICT

This section sets out the challenges around ICT for ASMEs, possible interventions for addressing these that are not currently being fully addressed by other development partners/GoM and then makes a recommendation.

2.3.1 ICT CHALLENGES

The major challenges identified in the ICT field relating to ASME development are:

1. Low use of ICT other than mobile phones, with increasing use of smart phones
2. Low use of m-money options for payments and receipts, though there is some nascent interest in these
3. Low ownership of computers and low use for email and web activities where these are owned

2.3.2 ICT POSSIBLE INTERVENTIONS

The possible interventions for USAID support in ICT are:

ICT Intervention 1: Support development of smartphone-based access to BDS, including financial education

This links to BDS Intervention 4 and A2F Intervention 2, with more emphasis here on the technology based approaches, notably smartphone use to access, read and receive materials. There are other SMS based options for communicating simpler messages, but the real potential lies in smartphone access.

As noted, SMEDI is looking at creating an integrated information center for BDS using a combination of fixed locations, website and SMS. This initiative could complement the SMEDI information, driven by a private sector provider with more flexibility and responsiveness than a public institution.

This could be done by a challenge fund to bring forward ideas that could be supported or working with a pre-determined group of BDS providers or a blend of the two methods. The advantage of an open approach, is that there successful ideas could come from any source. Partnerships between players with technical competence and BDS experience could be powerful combinations.

USAID could support innovation in and around smart phone based access to BDS, particularly useful apps and materials

ICT Intervention 2: Support development and access to tailored Apps for ASMEs and access to cloud-based storage for working documents

It appears that smart phones have given owner-managers a mechanism through which they want to access email and the web, in a way that computers did not seem to do. The portability, ease of use and in-built connectivity may all be factors that have encouraged this access.

This intervention would support development of Apps that help owners tackle common business problems, walking them through useful templates and steering them towards downloadable/readable material that inform resolution of the problem. It would be useful to encourage use of spreadsheet programs and to get MNOs or other players to offer cloud-based storage for working documents that owners can then access easily. Finally, the above could be supported by some simple smart-phone user training to speed the learning process, which could also integrate BDS, such as on financial problem solving.

USAID could support development access to ASME Apps that provide access to BDS and to cloud-based storage

2.3.3 ICT RECOMMENDATION

ICT Intervention 1 is related to BDS Intervention 4 and A2F Intervention 2. The emphasis in ICT Intervention 1 is smart-phone, web and possibly SMS based mechanisms, which is narrower than BDS Intervention 4 and A2F Intervention 2. This would be explicitly about technology driven mechanisms for BDS and financial education. In reality, it is the technology that appears to have sparked a change in behavior by owners that could be leveraged by designing engaging Apps and materials to bring important messages to owner-managers. Intervention 2, seeks to provide access to web-based tools, such as spreadsheets and cloud-storage.

Both of these are viable interventions that could be adopted.

It is recommended that USAID implement both ICT interventions.

2.4 COLLABORATION AND CLUSTERING

This section sets out the challenges around collaboration and clustering (C&C) for ASMEs, possible interventions for addressing these that are not currently being fully addressed by other development partners/GoM and then makes a recommendation.

2.4.1 C&C CHALLENGES

The major challenges identified in the C&C field relating to ASME development are:

1. Collaboration is not widely used by ASMEs, with low trust levels and poor experiences
2. Clustering is not adopted as a conscious strategy, even if it does arise organically where there is a high concentration of supply

2.4.2 C&C POSSIBLE INTERVENTIONS

The possible interventions for USAID support in C&C include:

C&C Intervention 1: Support research and promotion of collaboration and clustering

Attitudes to collaboration were mixed in the primary research, but on balance collaboration was not widely practiced and clustering was rare. It would be possible to seek to change attitudes through identifying, researching and promoting appropriate forms of C&C. These could be promoted through the mechanisms identified in the BDS, A2F and ICT interventions.

USAID could support research and promotion of collaboration using a variety of mechanisms to reach ASME owners.

2.4.3 C&C RECOMMENDATION

There is only one intervention identified, as C&C tends to be organic and responsive to circumstance and a function of the owners and their relationships. It is hard to stimulate actual C&C, but the intervention is to share ideas on what could be done, why it is beneficial and how it might be done.

It is recommended that USAID does not prioritize C&C over BDS, A2F and ICT interventions, but rather seek to encourage greater C&C through the other recommended interventions.

2.5 ENABLING ENVIRONMENT

This section sets out the challenges around the enabling environment for ASMEs, interventions for addressing these that are not currently being fully addressed by other development partners/GoM and then makes a recommendation.

2.5.1 ENABLING ENVIRONMENT CHALLENGES

The major challenges identified in the enabling environment related to ASME development are:

1. Registration is practically difficult and time consuming for those businesses that want to register, but there is an initiative to move registration on line and improve responsiveness by the Registrar General
2. Low rates of understanding of enabling environment and compliance with rules among ASME owners

2.5.2 ENABLING ENVIRONMENT POSSIBLE INTERVENTIONS

The possible interventions for USAID support in the enabling environment are:

EE Intervention 1: Support enabling environment education activities

Owner managers of SMEs generally pay limited attention to enabling environment issues, due to weak enforcement by GoM. There are supply side initiatives to improve service delivery, such as offering business registration on-line to improve efficiency and increase certainty for applicants. This intervention would focus on encouraging compliance by owner-managers, addressing lack of knowledge of enabling environment rules, as well as presenting a balance view of the benefits and costs of compliance.

USAID could utilize mechanisms identified in ICT Intervention 1, namely smart-phone access to downloadable materials, to enable this intervention.

2.5.3 ENABLING ENVIRONMENT RECOMMENDATION

There is only one enabling environment intervention identified, which focuses on education of ASME owners. Although ASME owners can get by in some areas without compliance, as the business grows, then compliance becomes more important to enable ASMEs to access bigger contracts and manage their operations in a sustainable manner.

It is recommended that USAID does not prioritize enabling environment education intervention over other interventions, as it is of less immediate importance than the other interventions.

ANNEXES

I SCOPE OF WORK

1. OBJECTIVE OF THE ASSIGNMENT

1.1 Overall Objective

Conduct an assessment of the current small and medium enterprise (SME) sector in Malawi, with a focus on agribusinesses and access to finance for SMEs. The objective is to better understand the current agricultural SME landscape in Malawi, assess SME competitiveness, and identify the most binding constraints to SMEs' development, growth and profitability, with a focus on access to finance, markets, infrastructure, business development services and technology. The consultant will submit a final report which includes the findings of the assessment along with an action plan with recommendations for how USAID/Malawi can best provide support for the development of agricultural SMEs and improved access to finance under a new Feed the Future (FTF) activity.

1.2 Purpose

Conduct an assessment of the agricultural SME sector and access to finance that will inform the design of a new activity to contribute to achievement of the FTF objective of Transformational Agriculture Value Chain Development (FTF IR 2) in Malawi.

The assessment should use primarily existing quantitative data combined with qualitative information gleaned from field work, to focus on the following:

- Status of existing agricultural SMEs operating in the FTF Zone of Influence (Central and Southern Regions), with a focus on those working in the three FTF focus value chains of soy, groundnut and dairy, as well as the input sector relating to these value chains. This stock-taking should include an indicative assessment of the capacity, size, scope, formality, financial knowledge, bankability and competitiveness of existing agricultural SMEs in the focus value chains, and comparisons where relevant to agricultural SMEs working in other value chains.
- Ability of agricultural SMEs to organize and function as competitive clusters to overcome barriers for their industry in order to better compete in both local, regional and world markets, with the goal of stimulating product innovation in the long term.
- Financial services and products (formal and informal) currently available to SMEs in the FTF Zone of Influence; quality and affordability of these services and products; current rate of use of financial services and products; delivery mechanisms for financial services and products.⁶⁷
- Primary barriers to accessing finance by SMEs (disaggregated by gender, geographic location, enterprise size, etc.) and possible avenues for overcoming those barriers.

⁶⁷ Contractor will use data from FinScope MSME 2012 – and FinScope 2008 where relevant -- as the basis for quantitative estimates.

- Key legal and regulatory issues affecting SMEs, including the financial sector and other areas of policy and regulation that impact the business enabling environment.
- Women-owned agricultural SMEs: gender-specific barriers to finance or other business services, and barriers to the entry of women into the SME sector.
- Existing support institutions for SMEs offering specialized training and/or other services.
- Other ongoing and planned donor-funded projects in the finance and SME sectors (e.g. World Bank's Financial Sector Technical Assistance Project).
- Use of ICT for access to finance and other services by agricultural SMEs in Malawi, and particularly in the FTF Zone of Influence.
- Stocktaking of potential SME opportunities in the FTF Zone of Influence (with particular focus on the three value chains). FTF investments will increase production in the three targeted value chains, which will create the need for value chain investments (storage, cold storage for dairy, processing, logistics, etc.) to handle that increased volume. The assessment should map out SME opportunities that could be created over the next several years.

The consultant will submit a report to USAID/Malawi summarizing the findings of the assessment and will present the findings to stakeholders at a meeting organized by USAID/Malawi, expected to be on 28th February 2014.

This assessment is intended to provide answers to the following questions:

- *What are the key opportunities for agriculture related SMEs which will likely arise from increased agricultural production of targeted crops in the Zone of Influence?* As crop production increases, commercial opportunities should arise throughout the value chains in such areas as input supplies, provision of agricultural equipment, development of storage and processing units, aggregation and transportation, etc. Using spatial mapping as a tool, the consultant will explore options for a software or tool to map out the projected increased production of targeted crops in the Zone of Influence over time (a ten year horizon), along with the presumptive value chain investments (input stores, storage units, processing facilities) necessary to service the presumptive increased level of production. Such a simulation model should have the capability of having the assumptions modified by user for the purpose of developing multiple scenarios). The end goal of such an exercise is to provide a public good tool to assist those considering investment in the Zone of Influence (whether they be a group of farmers, a local input supply dealer looking at expanding, or a major anchor off-taker) to better understand the opportunities to be presented by increased production in the targeted crops. As part of this SOW, the consultant will explore and compare options (including analysis of the exercise currently underway in USAID/Ghana), and provide recommendations on design and next steps.
- *What is the current landscape of SMEs in the Zone of Influence?* The consultant will conduct an assessment taking stock of the capacity, size, scope, formality, financial knowledge, bankability and competitiveness of existing agricultural SMEs in the focus value chains, as well as a similar assessment of agricultural SMEs working in other value chains. The consultant will also look at the capacity of SMEs to organize and cooperate as clusters within those value chains. In essence, what is current capacity to pursue those new opportunities, and what sorts of support will SMEs need to pursue them.

- *What is the demand for and availability of financial products and services for those SMEs?* Looking primarily from the perspective of the demand side (borrowers) what are the needs for financial products and services, and what is the current availability? How are their needs being met, and in which ways are they not being met?
- *What is constraining access to financial products and services?* There are a number of constraints in the financial sector ecosystem in Malawi which impinge upon the appetite of financial intermediaries in Malawi to commit financing for rural and agricultural SMEs – the question to be answered is which of these constraints are most significant to the flow of credit so as to inform USAID programming. The contractor is expected to undertake an assessment of the financial community in Malawi (based upon an assessment tool used by USAID). The consultant will then use the findings from the assessment and continued consultations with USAID/Malawi and other stakeholders to develop an action plan with recommendations for the design of a new FTF activity that will provide support for the development of agricultural SMEs and improved access to finance.
- *What other factors such as the legal and regulatory environment are constraining SMEs (and in particular women owned SMEs)?*
- *What are the support services currently present in the Zone of Influence (whether GoM institution or donor funded programs on-going and planned) which can support SMEs through training and advisory services?*
- *What are the opportunities for ICT in expanding financial and other services to SMEs?*

2. BACKGROUND

2.1 The USG's Feed the Future Strategy:

The objective of Malawi's FTF strategy is to sustainably reduce poverty and hunger. This objective represents specific efforts within USAID/Malawi to align agriculture and nutrition programming in order to leverage resources from across the FTF and Global Health Initiative (GHI) portfolios. The coordination of the two initiatives is a critical component of USAID/Malawi's overall assistance strategy and is how the USG will be able to achieve the FTF expected results of lifting more than 275,000 Malawians out of poverty and reducing the number of underweight Malawian children by at least 100,000.

Specifically, USAID/Malawi's FTF strategy objectives focus on: (a) Advancing value chain competitiveness; (b) Improving productivity; (c) Improving community capacity to prevent under nutrition; (d) Promoting innovation; and (e) Developing local systems capacity. A key activity under the FTF strategy is the Integrating Nutrition in Value Chains (INVC) project.

INVC is expected to lead to agricultural transformation across three value chains – groundnuts, soybeans and dairy - resulting in the achievement of the following objectives:

1. Improved productivity (land, water, labor) through soil and water management practices;
2. Increased competitiveness of the legumes and dairy value chains to mitigate food insecurity and increase incomes of the rural poor;
3. Reduced chronic under-nutrition;
4. Improved value chain competitiveness and nutrition outcomes through the fostering of innovation in adaptive technologies and techniques that will increase participation of the poor in agriculture-led growth; and

5. Enhanced capacity of local organizations and institutions developed to promote sustainability and climate change resilience.

Strengthening ASMEs and improving access to finance are important to achieving FTF objectives in Malawi.

2.2 Agricultural SMEs:

The FinScope 2012 MSME Survey for Malawi categorized small enterprises as those with 5-10 employees, and medium enterprises as those with 21-100 employees. This definition of SMEs as those with 5-100 employees aligns with the definition currently used by the Ministry of Trade and Industry, and should be used for the purpose of this assessment. Collectively, SMEs form the backbone of Malawi's economy and are critical to employment, economic growth and poverty alleviation in the country. The SME sector employs more than one million people, and generated more than 32.6 billion MK (approximately 100 million USD) in 2011.⁶⁸ With a predominantly agricultural economy, it is no surprise that the majority of Malawi's SMEs operate in the agriculture sector. This assessment will map those SMEs in the agriculture sector in the FTF Zone of Influence, with a focus on those operating in the soy, groundnut, dairy and input sectors.

For SMEs to thrive in Malawi, a strong private sector enabling environment is needed, in addition to improvements in access to affordable and high quality financial and business development services. FinScope's 2012 Malawi MSME Survey found that 62 percent of small business owners are not aware of small business support available, and that insufficient access to finance presents the greatest obstacle to growth for 34 percent of small business owners.⁶⁹

2.3 Access to Finance:

While agriculture employs at least 80 percent of Malawi's workforce, a key constraint to increasing productivity in the sector is a lack of access to finance. Malawi's majority poor rural population is underserved by existing commercial banks and other financial institutions, most of which do not consider rural households and agricultural SMEs bankable. The nascent microfinance sector, dominated by government and donor-funded programs, has also failed to reach most Malawians, with less than seven percent of the financially included population accessing services through microfinance institutions.⁷⁰

In 2012, only 2 percent of SME owners had a credit or loan product from a bank, and the other 20 percent that borrowed money relied on friends and family, non-bank financial institutions such as village banks and cooperatives, and informal mechanisms such as money lenders.⁷¹

3. SCOPE OF WORK

3.1 Place of Performance

This SOW requires travel to Lilongwe and to the field. The consultant may be required to travel to any of the districts in the FTF Zone of Influence to meet with existing SMEs and other key stakeholders in the field.

⁶⁸ Malawi 2012 SMME Survey, FinScope, 2013. www.finmark.org.za/wp-content/.../FSMalawiSME_Rep2012FNL.pdf

⁶⁹ Ibid.

⁷⁰ Ibid.

⁷¹ Ibid.

The consultant may also be required to travel to Blantyre to consult with key actors in the SME and finance sectors that are based there.

The key deliverables are described below.

a) Work Plan, Proposed Report Output and Assessment Tool (within 10 days of project commencement)

In consultation with USAID/Malawi's SEG Office, the consultant will produce a work plan containing a summary of documents to be reviewed and an indicative itinerary for meetings and consultations in Lilongwe, Blantyre and the field. The work plan shall be submitted to SEG within the first two days of the assignment. In addition:

- Within four days, the Contractor will submit for Mission review and concurrence the proposed format of the Assessment Report, detailing the questions which will be answered in this assessment.
- Within an additional four days, the Contractor will submit for Mission review and concurrence the proposed methodology under which it will conduct the assessment. The methodology is expected to be conducted as much as possible in a manner which will ensure that conclusions are empirically based, and drawing from surveys conducted with an adequate sample of: (i) SMEs, (ii) financial intermediaries, and (iii) BAS providers. With regard to access to finance and financial services, the Contractor will use as a basis but build upon the draft diagnostic tool developed by USAID on constraints to rural and agricultural credit and related financial services.

b) Draft Assessment Report (within 50 days of project commencement)

The consultant will submit a draft assessment report including key findings and recommendations from the assessment for the design of the new FTF activity.

c) Presentation to Stakeholders

The consultant will present the findings of the assessment and key recommendations to stakeholders at a meeting organized by USAID/Malawi. At this meeting the consultant will receive input from stakeholders to be taken into consideration in the writing of the final assessment report and recommendations for program design.

d) Final Assessment Report (within 60 days of project commencement)

The consultant will submit a final assessment report to the SEG Office Director. In addition to the findings of the assessment, the report will include a summary of previous work in Malawi that has focused on agro-dealers and SMEs in the input sector.

3.2 Duration, Timing and Estimated LOE

The assignment will over a three month period during December 2013 and February 2014. Estimated LOE is as follows:

Team Leader: Senior Researcher (US/TCN)	TBC
SME/Finance Spec (Local Hire)	TBC
SME Spec x2 (Local Hire)	TBC
Researcher (Local Hire)	TBC

Additionally, the contract will hire a team of Malawian data analysts for processing the quantitative data from FinScope and any other relevant data sources.

3.2.1 Methodology

The assignment will primarily involve review of secondary documents and data, and consultations with various stakeholders such as bank and non-bank financial institutions including current Development Credit Authority partner banks, NGOs, agricultural SMEs and institutions that provide services to them, MoAFS, Ministry of Industry and Trade, Small and Medium Enterprise Development Institute, USAID and other donors. Throughout the assignment the consultant will frequently liaise with the SEG Office to review progress.

In addition to other methods the consultant might propose, it is strongly recommended that he/she ensure that the following are included as part of the assessment:

a. Determine necessary contacts for interviews/meetings

Discuss with the SEG Office issues surrounding SMEs and access to finance in Malawi; receive guidance on the necessary contacts and literature to consult within the first two days of the assignment.

b. Review available literature

Review available literature on SMEs and access to finance in Malawi, including assessments that have been conducted on these sectors in recent years (see suggested documents). It is expected that the consultant will collect additional documents from stakeholders.

c. Consult with key stakeholders

Consult with key stakeholders at all levels from all sectors (i.e. private, public, donor and NGO) working in the fields of SMEs and access to finance in Malawi.

d. Study the structures of business development service providers

Through literature review and consultations, develop a clear understanding of the services planning and delivery structures of the government, private sector and NGOs involved in providing business development services to SMEs. Make recommendations for how a new activity could improve the accessibility and quality of business development services and products for SMEs, either by providing them directly or by strengthening the structures of existing service providers.

e. Study the structures of financial service providers

Through literature review and consultations, develop a clear understanding of the services planning and delivery structures of banks, non-bank financial institutions and other organizations that provide financial services to SMEs. Make recommendations for strengthening the structures of these financial service providers and for improving the accessibility, affordability and quality of their financial products. If appropriate, make recommendations regarding new modalities of support to increase financing opportunities for SMEs.

f. Map status of service providers

Map current status of business development and financial service providers in the FTF Zone of Influence and establish gaps, e.g. who the services providers are, where in the district they work, the capacity of the organizations, what services they provide, etc. Make recommendations for improved collaboration and coverage of services in the FTF Zone of Influence.

g. Assess the extent and effectiveness of business support services

Assess the extent and effectiveness of business support services available to SMEs in the FTF Zone of Influence. Identify any weaknesses or gaps that, if addressed, could help to strengthen SMEs in the agriculture sector.

h. Identify key policy challenges

Identify key legal and regulatory issues affecting SMEs, including those in the financial sector and other areas of policy and regulation that impact the business enabling environment.

i. Assess current and potential future use of ICT

Assess the current use of ICT by agricultural SMEs and make recommendations on how it can be used to improve access to finance and other services in the FTF Zone of Influence.

j. Consult continuously with the USAID/Malawi SEG Office

Discuss emerging findings with the SEG Office throughout the period of performance and seek any additional guidance needed on a continual basis.

Team Composition/Key Personnel

The assessment will be led by an expert consultant with strong experience in the design and oversight of assessment projects. The consultant will be supported by three local specialists in SME and agriculture-related finance: one senior, one mid-level and one junior-level, at varying levels of effort as reflected in section 3.2.

II METHODOLOGY

This annex presents the methodology and related limitations.

METHODOLOGY

As noted in the SoW, a mixed methodology was used, that combined quantitative and qualitative sources. In practice, this meant combining existing secondary material, including considerable quantitative data from the 2012 FinScope Micro, Small and Medium Enterprise (MSME) study (FinScope MSME 2012), with additional mainly qualitative primary data gathered by the consultants in field research. The latter included:

1. Interviewing 68 SMEs in the seven target districts⁷² in the FTF Zone of Influence
2. Interviewing 68 micro-enterprises⁷³ operating in the target value chains in the zone of influence
3. Interviewing 9 Financial Institutions (FIs)
4. Interviewing 12 agricultural market stakeholders (private sector), such as processors, sector associations and commodity exchanges⁷⁴
5. Interviewing 10 other stakeholders, including governmental bodies (Ministries and agencies) and interested development partners.

The consultants reviewed secondary sources, notably the FinScope MSME (2012) study, the Ministry of Industry and Trade's (MoIT) MSME Policy and Strategy (draft), the Assessment of the SME Sector report (USAID, 2007)⁷⁵ and the Status of Agricultural and Rural Finance in Malawi, (FinMark Trust, 2012). Details of these and other secondary sources consulted are set out in Annex II. The literature provided useful context, but also highlighted the limited extent of studies into Malawi's SMEs. Although the quantitative data is useful in giving some indication of scale, as is set out in the subsequent sections, it also has a weakness based on the conception of SMEs that has generally been adopted by researchers of a single or main small/medium

⁷² These districts are Balaka, Dedza, Lilongwe Rural, Machinga, Mchinji, Mangochi and Ntcheu.

⁷³ Some Micro-enterprises were included to give insights into the target value chains and on the transition from micro to small enterprises.

⁷⁴ Value chain participants from the dairy, soybean and groundnut chains, particularly processors, large traders and input suppliers based in Lilongwe and Blantyre/Limbe. These are technically out of the Zone of Influence, but are important sources of information on SME behaviour in these value chains.

⁷⁵ Undertaken in preparation for a Development Credit Authority.

enterprise, when in practice many SME owners adopt a ‘portfolio’ approach with ownership of more than one business (see discussion in section 1 findings).

The methodology was agreed to be primarily qualitative, but supported by quantitative analysis drawn from an analysis of the original data for the FinScope (2012) study, to draw out SME data from the overall MSME database for the purpose of this assessment. The analysis of quantitative data is integrated with the qualitative findings, to bring additional insights to both quantitative and qualitative data (see section on Findings) and as a means to triangulate the data to increase its robustness. With the availability of the FinScope (2012) data and study, the research team did not seek in its research methodology to replicate or extend the quantitative data collection in that study,⁷⁶ but analyzed the data to draw out its particular relevance for the current assessment. This analysis narrowed the focus to SMEs, rather than the broader category of MSMEs covered in the FinScope (2012) study.⁷⁷

Qualitative data gathering was undertaken using semi-structured topic guides focused on three groups: SMEs, FIs and other stakeholders. For SMEs, the approach was to phrase questions using terms that related to business challenges and opportunities from the perspective of a business owner. For example, rather than ask about the business’ use of insurance for which it is already known that uptake of formal insurance products is limited, the consultants asked about the most important risks faced by the SME and how they manage that risk. The aim of this approach was to understand the needs from the SME owner’s perspective (demand-side), not through a focus on the products currently available from the financial services sector (supply-side) to address risk. Insurance use was probed for, but not until the issue of risk and methods to manage risk more generally had been explored.

The field research team was three experienced business consultants, with direct experience of working with SMEs, as BDS providers, and of FIs. The team was trained in the topic guide with a strong emphasis on probing responses and with a mandate to explore any responses that appeared to cast new light, rather than necessarily to complete all the topics as if it were a questionnaire.⁷⁸ Although this meant that not all topics were covered with all SME interviewees, it did enable the researchers to use their judgment to explore points that would generate fresh insight where a topic was of particular importance for to an interviewee. This methodology enabled a broader appreciation of the issues from a demand-side perspective to emerge, but was not designed to generate quantitative responses that could be summarized and analyzed quantitatively. The focal topics were on financing, collaboration and competition, suppliers (including BDS) and customers, and use of information and communication technologies (ICT). The topic guide for ASMEs is in Annex V.

The consultants considered potential sources of information to identify ASMEs in the seven districts in the ZoI. District Assemblies do license businesses and collect a fee for doing so. The district does keep a list of businesses from which a payment has been collected, noting name, approximate location and broad category. However, this list is primarily produced for revenue recording purposes, so the categorization is very broad and not specific enough to identify the type of business, such as agricultural trading (or details of crops traded) or the size of the business, categorized as micro, small, medium or large. The listing is not up to date,

⁷⁶ FinScope MSME (2012) covered 1,996 MSMEs across all districts and all business categories, though 108 of these could not be included due to lack of categorization into micro, small or medium enterprises.

⁷⁷ There were 108 small and 8 medium enterprises in the database, totalling 116 SMEs.

⁷⁸ It was clear from piloting that not all SME interviewees would be willing to give information in all areas, or would have something meaningful to say, e.g. due to limited use of information and communication technologies.

not comprehensive, not necessarily in an accessible format and availability depends on making a request, which the District Assembly may or may not accede to.

The consultants reviewed the potential weaknesses of the listing (not comprehensive, not able to identify ASMEs, not up to date) and the time to obtain it and re-sort the data so as to be able to draw a sample and decided that it was not the optimal method for finding ASMEs and carried risks if the team began to implement it, but found this was not possible in all Districts. Instead, ASMEs in groundnut, soybean and dairy value chains were identified through enquiry at important trading centers in the seven target districts, primarily at the District Centre.⁷⁹ The research team identified potential ASMEs through asking business people in these localities for details of those that were operating on a sufficient scale to be classed as ASMEs. As the number of ASMEs in the districts is small (supported by the FinScope data), then enquiry was judged to be the most pragmatic method to find ASMEs quickly and relatively comprehensively. Each ASME found, was asked to provide the names of competing ASMEs, as well as ASME suppliers and buyers in its value chain. This enabled the team to identify and find the majority of those that were named by respondents in a relatively short time.

To construct a representative sample would have required identifying all qualifying ASMEs in the locality from which to select at random, which was judged not to be feasible; rather, a purposive sampling approach was taken to identify ASMEs across all the stages and roles within the target value chains and ensure interviews were conducted in at least each category; for example suppliers of inputs, traders, transporters and processors. The intention of the field research was to get a better appreciation of the nature of ASMEs and their behaviors in the subject matters of interest, to generate insights alongside the quantitative analysis from the FinScope (2012) database.

A key focus of the study was access to finance. The research team identified FIs (mainly the banks) active in SME finance and sought to meet the relevant SME departments and/or responsible staff. At an early stage, the team took the view that it would not be possible to get quantitative data on lending to/deposits from ASMEs, as it was clear that each FI was defining its SME portfolio differently and not linked to the GoM's MSME definition (see section **Error! Reference source not found.**). In addition, FIs were also defining 'agricultural' and 'agri-business' in different ways, and were not able to separate the two; in some cases, it was also not always possible to disaggregate agricultural/agribusiness from within the SMEs portfolios. Finally, there was also a reticence on the part of most FIs to disclose quantitative portfolio data, due to confidentiality and perhaps due to known internal limitations of the data. This meant that even if data could have been obtained from every FI, it could not be aggregated, as definitions of ASMEs differed so much.

Instead, the consultants focused on understanding the different ways that FIs were classifying SMEs, the nature of their SME services/products, the structure of their SME departments/teams and the challenges they identified in working with SMEs. The team drew on a financial assessment tool that is under development by USAID, using this to inform the qualitative topic guide, but for the reasons identified above, it could not implement a quantitatively oriented tool. The topic guide for FIs is included in Annex VI.

⁷⁹ This is called the 'Boma', being the main town in each District, as the Government's administration Headquarters for that District. For Machinga, the team covered both Machinga Boma and Liwonde, as there is much more business activity in the latter center. For Mchinji, the team also covered Waliranji, where there is a concentration of groundnut traders. For Lilongwe Rural (excluding the city), the team visited Mitundu and Lumbadzi, as well as other locations where specific ASMEs were identified.

USAID requested that the consultants look at possible models for determining the effects of increases in production of groundnut, soybean and dairy in the seven Districts. A proposal has been made by ACIDI-VOCA to USAID on how the model might be developed as a separate assignment.

LIMITATIONS OF THE METHODOLOGY

There are challenges around the definition of SMEs and, related to this, the way in which they are characterized by previous studies. There are merits in the different definitions, but this has led to inconsistent use between different stakeholders, notably among the FIs. The effect of this is that it is not possible to undertake meaningful comparisons and aggregate quantitative data from different sources. It was in anticipation of this limitation that the study methodology was originally determined to be more qualitative in focus. As a result, although the research team did seek quantitative data, such as the lending portfolio, it was clear from the variation in definitions used by FIs that where this was provided, it was not possible to aggregate it, so it has not been reported.

A second related limitation was the low number of SMEs surveyed in FinScope (2012). Out of 1,996 interviews, 108 had missing values,⁸⁰ giving a usable sample of 1,888 MSMEs. From the remainder, 1,772 were classified as micro enterprises, 108 small and eight medium giving a total of 116 SMEs. The balance of any business community is that there are many more Micro Enterprises (ME) than SMEs and large enterprises, particularly in economies like Malawi where many people have limited choices, other than to start/run an enterprise. The SME portion of the FinScope MSME database is less than seven percent of the database and too small to generalize from without wide margins of error. Although, the quantitative data for SMEs is presented, caution is needed on generalizing from it.

The consultants analyzed SMEs that were reportedly operating in Agricultural/Agri-business sectors, as well as in the seven target districts and disaggregated all results by male and female respondents.⁸¹ However, adding additional data filters to the sample of 116 SMEs reduced the numbers of respondents even further, thereby exacerbating the reliability of generalizing. Combining these filters to determine potentially interesting responses, for example, of female respondent ASMEs in the target districts, resulted in too small numbers of responses; therefore, this level of analysis is not presented as it risks being misleading.

The response to this quantitative data limitation around male/female and location was to consider at what level the data could be most usefully presented. In the data analysis of respondents' sex, the only question on which there was a notably different response between men and women was on business licensing, with women less likely to have a license; otherwise the responses were not clearly differentiated. As a result, although the SoW asks for disaggregated data by sex, this has not been reported as there is no clear differentiation in the data. Also, although a total of 116 SMEs from the seven target districts were identified in the database, separating these out and analyzing these did not obviously yield any notable differences with data for other districts or between districts. As a result of this review of the MSME database, the consultants judged that the most useful approach would be to present the data tables for all types of SMEs in aggregate, rather than disaggregated by sex and location of respondents. A second response was to integrate qualitative and quantitative findings to increase robustness through triangulation.

⁸⁰ This is a relatively high missing value total and it is unclear if this arose at the data collection stage, or at data entry. For analytical purposes, it is better to remove those that have missing values in relation to the classification as micro, small or medium, as the responses on other questions, where they exist, cannot be assigned to one or other category of MSME. There were missing values of this magnitude across the database, not only in relation to MSME categorization.

⁸¹ Almost all the respondents were stated to be owners, but some were managers or unspecified 'other'.

While this is an ideal outcome, the research team’s view is that the main differences are between MEs and SMEs and that there would likely be less notable differences based on sex and location. Therefore, the data that is presented is predominantly data for SMEs of all types across all districts, rather than further aggregated or disaggregated.

Further Notes on SME Definition and Categorization

Historically, the categorization of enterprises was based on a combination of employment, turnover and capital employed. However, the latter two criteria are no longer used, partly because inflation makes it necessary to keep updating the values for turnover and capital employed and partly due to definitional difficulties.⁸² In addition, using three criteria in combination creates additional complications in the categorization, as a business may fall into different categories when assessed on each criterion separately. This challenge stems from the considerable diversity in businesses, according to their sector of operation,⁸³ their function within the value chain⁸⁴ and even their business models.⁸⁵ For example, a firm that runs a processing plant or a transport operation will have much higher capital to turnover and employee ratios than a firm that services equipment or provides contract security staff.

Therefore choosing one criterion through which to categorize businesses, ensures that businesses can only fall into only one category and employment is the easiest criteria to measure, and the one that governments are most interested in. However, there are still definitional problems with using employment. It is not explicitly stated in the MSME Policy (2013, draft), but the presumption in the above categorization is that ‘employees’ refers to full-time or full-time equivalent, rather than a headcount of full-time, part-time and temporary/casual employees. Unfortunately, this methodological difference can lead to inconsistent counting. One observation from the field research was that owners had to be reminded to count guards that they were employing, as many were only counting staff working in the premises, than all their employees.

Table: Categorization of MSMEs by Employees, per MoIT

Category	Employees
Micro	1-4
Small	5-20
Medium	21-100
Large	100 plus

Source: MSME Policy Strategy for the Republic of Malawi, MoIT, (Draft 2013)

The FinScope (2012) study used employment as the basis to differentiate MSMEs. It estimated that there were 987,480 MSMEs⁸⁶ of which 81% were recorded as micros, 17% as small and 2% as medium enterprises. However, the percentage breakdown of micro, small and medium enterprises in the FinScope (2012) report

⁸² For example, turnover and capital employed can be calculated in different ways, resulting in the need to impose common definitions which may not fit firms own definitions; these are difficult to enforce. The result is that turnover for different firms is often not comparable.

⁸³ Businesses in agricultural sectors are likely to be more labour intensive than those telecoms or tourism, for example.

⁸⁴ Businesses that are engaged in farming are likely to be more labour intensive than those providing services into the value chain e.g. veterinary.

⁸⁵ Businesses adopt models that outsource/sub-contract to other firms or individuals. E.g. transport services can be in-house or outsourced.

⁸⁶ Unfortunately, the report does not explain how the total of MSMEs was calculated, and does not break them into micro, small and medium.

excludes micros that have no employees, other than the owner. This fits the MoIT's definition of a micro having 1-4 employees rather than the FinScope method which defines a micro as 0-4 employees, ***on the basis that the owner is not counted***. This method overstates the proportion of small and medium enterprises at 17% and 2% respectively.

III SECONDARY SOURCES

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IV PERSONS/ORGANIZATIONS CONSULTED

Name	Position	Organization
Agricultural Market Stakeholders		
Mrs. Valeria Morua	Technical Advisor	Agricultural Commodity Exchange
Mrs. Maria Kritzas	Director	Agora
Mr. Davie Lockie	Senior Economist	Auction Holdings Commodity Exchange
Mr. Jonathan Kaphela	Office Manager	CREMPA
Mr. Robert Renshaw	Managing Director	Farmers Organization Ltd
Mrs. Veria Laemaile	Executive Desk Officer	Fertilizer Association of Malawi
Mr. Uyala Penifolo	HR & Admin Manager	Katete Farms
Edward Khoromana	Managing Director- Export Department	Nali Ltd
Mr. Mr. Simon Itaye	Managing Director	Nampak (formerly Packaging Industries Malawi)
Mr. Sai Kiran Josyabhatla	Managing Director	Rab Processors
Mr Supply Chisi	Executive Director	Seed Traders Association of Malawi
Mr. Farouk Kali	Director	Suncrest Creameries
Government Stakeholders		
Mr. Chifwayi Chirambo	Principal Assistant Registrar General	Department of Registrar General
Mr. Fred Sikwese	Director, Standard Development	Malawi Bureau of Standards (MBS)
Mr. Bob Mkandawire	Commercial Director	Malawi Industrial Research and Technology Development Centre
Mr. McCartney Gift Lora	Enterprise Development Officer	Ministry of Industry and Trade
Mr. Charles Kazembe	CEO	SMEDI
Development Partners		
Mrs. Kerry Johnstone	Private Sector Adviser	DFID
Mr. Duncan Warren	Program Manager	Farmers Union of Malawi
Mr. Francis Banda & Mr. Ian Goggin	Groundnuts VC Coordinator	Integrating Nutrition into value chains
Mrs. Prisca Mdzolera	M&E Officer	Malawi Milk Processors
Mrs. Towera Jalakasi	Intervention Manager	Malawi Oilseed Sector Transformation
Ms. Cinzia Tecce	Senior Private Sector Specialist	United Nations Development Program
Financial Institutions		
Mr. Floris Vermeulen	Project Officer for Malawi	EIB
Mr. Jana Kadian	Chief Executive Officer	FINCA
Mr. Mbachazwa Lungu	Senior Manager-SME	FDH Bank
Mr. David Kavinya	Manager- SME Banking	Indebank
Mr. Howard Bowa	Head of SME Banking	Indebank
Mr. Brenda Chilima	Marketing & Business Devt' M'ger	Malawi Saving Bank Ltd
Mr. Gift Livata	Country Manager	Micro-ensure
Mr. Lackson Kapito	National Credit Coordinator	National Association of Business Women
Mrs. C. Chikaonda	Accountant	National Association of Business Women
Mr. Henry Chalowa	Business Development Manager	National Bank of Malawi

Mr. Samuel Ngwira	Business Development Manager	National Bank of Malawi
Mr. Jones Kameta	Agriculture Liaison Manager	National Bank of Malawi
Mrs. Ruth Bema	SME Account Executive	NBS Bank Ltd
Mr. Mike Gapala	Relationship Manager	OBM
SMEs		
Dedza		
Mr. Peter Kamele	Admin & Accountant Manager	Asumi Milling Company
Mrs. Chrisy Phinifolo	Shop Manager	Beni Traders
Mr. Brave Dabwa	Owner	Dabwa Investments
Mr. Wesley Dausi	Farm Manager	Evergreen Diary Farm
Mr. Iffani Mussa	Director	IFUM Trading
Mr. Mark Kondowe	Owner	Kaka Transport
Mr. Hendrix MTambalika	Owner	Nkhoma Farm Shop
Mr. Peter Muskwa	Director	PC Transport
Mrs. S. Leng'i	Owner	U2 Agrodealers
Mr. Lazaro Gumbo	Owner	Yamikani Traders
Balaka		
Mr. Salanje	Owner	2010 Agrodealers
Mr. Ishmael Jasati	Owner	A.Jasati Transport
Mr. Brazio Kokota	Store & Restaurant and	Balaka Best
Mrs. Chipande	Owner	N/A (Farmer)
Mrs. Banda	Director	OPS General Dealers
Mr. Robert Makwecha	Owner	RAM Investment
Mr. Richard Saula	Director	Rasiyana Agrodealers
Mr. Redson Chisale	Owner	Redson Enterprise
Mr. Emanuel Kapito	Branch Manager	Tropical Agriculture
Mr. Jumbe	Owner	Yankho Ladza Enterprises
Mr. Charles Londwe	Head Driver	Yes Rasta Transport
Lilongwe Rural		
Ms. Patience Banda	Saleslady	Dalitso General Dealers
Mr Bruce Somanje	Shop Manager	Green Valley – Namitete
Mr Richard Chapweteka	CEO	Green Valley Limited
Mr Brighton Jamali	Owner	Jamali Agro dealers & processors
Mr Kizito Banda	Shop Manager	Jet Investments
Mrs. Emmie Phiri	Vice Chairperson	Lumbadzi Milk Bulking Group
Mr Bright Maniki	Driver	Lumbadzi Truck Rank
Mr Lloyd Nkosi	Shop Manager	Mitundu Market Resource Centre
Mr. Fanwell Matsimbe	Shop Manager/Buyer	Muligo Just General Dealers
Mr Isaac Kazanga	CEO	Ndatani Investments Limited
Ms. Florida Pabulika	Shop Manager	Ndatani Premier Feeds – Mitundu
Mr Edson Whiteson Pasulani	Managing Director	W & H Food Processing and Chawanda Farm
Mr Naphutali Banda	Farm Manager	Zanzi Estate
Machinga		
Mrs. Chatepa	Owner	DEBS Agrodealers
Mr. Banet Majawa	Owner	Discount wholesale and retails
Mrs. Linda Selemani	Shop Manager	Divine Agro dealers
Mr. Tambula Gross	Owner	Gross Agro dealers and aggregators
Mr. Admuson Jasiya White	Director	Jasiya logistics

Mr. Chipeta	Shop Manager	Lilongwe Livestock Centre (Liwonde)
Mr. Mc Deveson Matumba	Owner	Matumba Investmnet
Mr. Robert Chauya	Owner	REG Transport
Mr. Damiano Machika	Owner	S and M Investment
Mr. Ulanda Pongolani	Owner	UP Enterprise
Mangochi		
Mr. Orman Osman	Owner	Abroo Transport
Mr. Kaphuluza	Onwer	Atupele Agro suppliers
Benedicto Chambo	Owner	Chambo Agrodealers
Mr. Carlos Kalombola	Owner	Changu pa Malo
Mr. Edward Kapichira	Owner	DAC Logistcis
Mrs. Coreta Tchongwe	Farm Manager	Fermano Veterinary Services
Mr. Gift Njolomole	Owner	GEF Agrodealers
Mr. Lujeliyo Kambalame	Owner	Kambalame General Dealers
Mr. Grey Misomali	Owner	N/A-
Mr. Samson Phiri	Manager	Pindulani Seed Company
Mr. Dyson Mumba	Manager	Utawaleza Farm
Mchinji		
Mr Mbalale	Farmer	
Mr Sineki Labson	Farmer	
Ms. Patricia Banda	Secretary	A.B.Mwale Commodities
Mr Petulo Chatera	Shop Manager/Buyer	Chatera Invesment
Mr Kapalanga	Farm Manager	Chichere Farm
Mr D.H. Masina	Owner	Dalitso General Dealers
Mr Peter Oscar	General Manager	Dalitso General Dealers
Mr Dave Phiri	Shop Minder	Fertilizer & Forage Limited
Mr Aback Kapasula	Shop Manager	Green Valley Limited - Kamwendo
Mr Boliani Msampha	Co-Owner	Kaporo Adyenji Transport
Mr Mickford Msampha	Co-Owner	Kaporo Adyenji Transport
Mr Bazilio Chakale	Shop Manager/Buyer	Kaufa Commodities
Ms. Grace Jane	Saleslady	Lilongwe Livestock Centre
Harry MTawasa	Driver	Mchinji truck Rank
Mr Tiyamike Makhwazi	Shop Manager	RW Traders
Mr Milward Nyangulu	Owner	Takondwa Commodities
Mr Frank Jonasi	Shop Manager	Takondwa Commodities – Kamwendo
Mr Richard Kaliwa	Branch Manager	Takondwa Commodities – Mchinji
Ms. Vilolet Jackson	Sales Representative	Universl Farmers Hub – Kamwendo
Ntcheu		
Mr. Alfred Masangano	Director	Agri-Hort Suppliers
Mr. Noel Masangano	Managing Director	Ask Enterprises
Mr. Zamani Cassim	Owner	Big Mwana Transport
Mr. Chipiliro Daniel	Owner	Doba Enterprise
Mr. Brian Frazer	Owner	Kamuzeni Farmers Centre
Mr. Levi Holobert	Owner	L. Holobert Agro-dealers
Mr. Chimembe	Shop Manager	Lilongwe Livestock Centre (Ntcheu)
Mr. Faziliam Mogra	Owner	Mogra Transport
Mr. Jesemani	Owner	Mpamadzi Farm
Mr. William Mwaiwadza	Managing Director	Mwaiwadza General Dealers
Mr. Banda	Director	OPS General Dealers
Pastor Chagoma	Owner	Reform Enterprises

V SME TOPIC GUIDE

1.0 Background

Date of interview:

Name of business:

Name of owner(s):

Male/female (*circle*)

(If no owner is present, then you can interview the manager as long as they are forthcoming)

Number of full-time employees:

Number of part time and/or casual employees:

Split of male/female employees: Male % Female _% Contact cellphone (*for follow up info*):

2.0 Nature of business (*circle all relevant and underline most important*):

Comment (state in brief what the business does):

3.0 Suppliers, ICT, & Finance, (focus on the relevant part of the business, if multiple)

Who are your main suppliers? (*names, what supplied, locations, size, etc. try to also think of business service providers in this – training, accounting, legal, IT, etc.*). (*Try to identify key supplier-buyer relationships that are not just transactional and find out how they came to be more than just transactional, if you can*)

What challenges do you have in getting the supplies and services you need to operate/grow your business? (*probe for finance issues, absence of local suppliers, quality of supply, timeliness of supply, labor/ skilled staff, premises, water/ electricity, missing services, etc.*)

What has been your experience of accessing finance for your business? [*Probe for formal and informal loans (when, who from, form of loan etc.), trade credit (suppliers and customer advances) and ‘internal’ finance (from other businesses, from family, friends & business partners)*]. (*Probe for challenges and how they understand finance issues, managing cashflow, separating business/ personal finance*)

Do you operate bank account for the business? [*Probe: which bank (+location), savings and/ current account, what is it mainly used for (receiving, paying out, savings...) etc.*]

What risks are the main risks for this business? How do you cope with the risks you face in your business? (*Probe: insurance for vehicles, buildings, stock, equipment; strategies for dealing with risk*)

By what means (phones, internet access, computers and other ‘ICT’ technologies) do you communicate with suppliers and customers etc.? How do you maintain records and find out information? (*Probe for how ICT used, what purpose, importance, problems and opportunities to improve, etc.*) (*Looking for use of phones, smart phones, emailing, business records, payments (m-mobile), software for business operation, etc.*)

4.0 Customers, Collaborators & Competitors

What types of businesses and/or people are you mainly selling to? (*probe for importance of each group, why these groups, challenges in selling to them, why is it a challenge, what could make it easier, etc.*) (*explore any key longer term seller-customer relationships*)

Which other businesses/people do you collaborate with in order to buy and sell? [*E.g. traders and transporters, traders and warehouse/ storage provider, agro-dealers and vets, etc. Nb we are looking for collaboration to improve operation, not for key supplier-customer relationships (see above)*] (*why this relationship, how does it help you, how can it be strengthened?*)

Who are your main competitors? (*Probe: sizes, how they compete (price, service, quality), who is doing well and why*). (*Nb use this information to identify other possible interviewees*)

5.0 Enabling environment - rules

What rules does Govt set/have that affect your business? (*Probe for what they are, how affects them, how they manage them/get around them, etc.*)

What government agencies do you have contact with and what has been your experiences? (Bureau of Standards, District Assembly, Ministry of Agriculture, Police, etc.)

Any other comments? (*Add any other comments that appear of interest to our study*)

VI FINANCIAL INSTITUTION TOPIC GUIDE

Definition of SMEs

1. How does your bank define/categorize Micro, Small and Medium Enterprises?

Micro defined as:

Small defined as:

Medium defined as:

Large defined as:

(Nb after getting these, get them to focus the rest of the discussion on the ones that most look like SMEs as defined for our study.)

2. How is your bank structured to address micro, small, medium and large? *(Probe: some banks have a corporate section covering large and medium... and some have an SME unit. Need to find out where they locate SMEs...possibly split over SME unit and corporate unit...).* *(Probe for number of locations SME services provided from particularly in the seven target districts, number of SME dedicated staff (and where – HQ, in the branches), experience/training of staff etc.)*
3. How does your bank split clients according to sectors? Specifically, how do you define agricultural/agri-business and do you have different arrangements for managing these within the bank and/or with the SME section? *(We are trying to understand how they capture these businesses in the system and if they can report on agric/agri-business lending etc....)*
4. What initiatives or services/products do you have specifically for the SMEs in the agricultural sector, including agri-businesses (processors, transporters etc.) and how different are they from services/products? *(Probe: for loan products, but also services like transfers, forex, savings products, insurances.... We are interested in more than loans, though loans is likely to be the most common/important, so spend time on it).* *(Probe: what have proven to be most popular with SMEs and why? What has been least taken up/popular, and why?)*

Loans *(categories – short/medium/long, overdraft, other borrowing instruments/methods (letters of credit, invoice factoring), security/collateral, restrictions on use (capital investment, operational/working capital) etc.?)*

Other products/services *(would be particularly interesting to know about internet/SMS or other ICT based banking services for businesses)*

5. What has been the trend for the past five years of loans and other products offered to SMEs? *(Probe: What explains the trend(s), how has the bank changed its products/services as a result?)*
6. What patterns do you see in terms of gender, race and age as to the bank's major customer for the loans and other products/services? *(Probe: why is this case? Looking to see if hints of groups excluded...women, Malawians, old/young)*
7. Who are the most common customers for you split as far as possible per the table below? *(Nb: try to make this for the year just ended on 31st Dec 2013, but if not, then specify the period it relates to).*

	# of SME customers	Borrowing SME customers	Value of loans outstanding
	#	MK	MK
Agricultural (farming)			
Agri-dealers (inputs)			
Agri-traders			
Agri-transporters			
Agri-storage			
Agri-processing			
Total			

Any comments on above?

Loan requirements

8. What are the general requirements for agricultural/agri-business SMEs to qualify for a bank loan? What percentage of loan applications are not approved by the bank and what are the major reasons for that? (*nb may be covered earlier, but if not, then probe here. Second question is not yet covered*) What relationships do you have with SMEs to better understand/monitor their operations after issuing a loan?
9. From your experience working with SMEs, what could be some of the suitable innovative credit services that could be developed for the agricultural/agri-business SMEs?
10. How many agricultural/agri-business SMEs come back for subsequent bank loans? (*Probe: Give reasons why they come back e.g. seeking additional working capital, capital for expansion, paying debts, etc. And for those that do not come back, what could be the reasons?*)
11. What is the default rate on loans in the agricultural/agri-business sector? What are the causes behind this default rate? What has been the trend? What do you do about default (*Probe: restructure, take assets, etc.*)?

Challenges

12. Overall, what are some of the challenges you face working with SMEs? (Give reasons why these challenges exist and what could be done to address them)?

Policy

13. Which policy issues or laws, if any, adversely affect the bank services to agricultural/agri-business?

Risks

14. What are some of the risks that your bank is exposed to when working with SMEs and how could these risks be mitigated?

Plans for the future

15. What proportion of your total bank loans are issued to SMEs? What importance do you think agricultural/agri-business SMEs will have for your bank in the future? (*Probe: for reasons to support this*)
16. What plans does the bank have aimed at serving SMEs in the agricultural/agri-business sector in the future?

Thank you

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