

Private Sector Participation in the Farm Input Subsidy Programme in Malawi

The Farm Input Subsidy Programme (FISP) in Malawi has been implemented since the 2005/06 season with the objective of improving household and national food production and incomes. It targets more than 1.5 million farm families who receive subsidised fertilisers, improved maize seeds and/or legume seeds. The implementation of the FISP has involved the interaction of the Government of Malawi, the private sector, development partners, civil society organisations (CSOs), non-governmental organisations (NGOs), traditional leaders and smallholder farmers, all playing different roles in the implementation and success of the programme. The private sector has played a critical role, but its involvement in the programme has changed over time. This has included the procurement of fertilisers, the transportation of fertilisers to various markets, the retail sale of fertilisers, and the production and sale of improved seeds.

Benefits from the inclusion of the private sector in the implementation of a nation-wide agricultural input subsidy programme include efficiency, reduced bureaucracy, strategic

development of the private market system, cost savings on the part of the Government, shared investment finance and costs, and reduction in displacement of commercial sales of inputs.

Nature of private sector participation

The role of the private sector in the fertiliser component of the programme has varied over time with regard to its participation in and exclusion from retail sales, while private actors have remained important partners in the procurement of fertilisers for the programme, and in unsubsidised commercial sales. On the other hand, there has been consistent private sector participation in the seed component of the programme. The private sector also procures fertilisers for commercial sales in various market outlets and provides transport services for moving subsidised fertilisers from the depots to unit markets (parastatal retail markets) across the country.

There are four main types of formal private sector involvement in the FISP. The procurement

of fertilisers has been the major mode for increasing its participation, with the private sector procuring more fertilisers under the subsidy programme than state marketing agencies. Second, the distribution and transportation of fertilisers is entirely handled by the private sector with a number of contracted transporters. Opportunities in retailing of subsidised fertiliser have been more mixed, with the inclusion of four supplier networks in the programme only taking place in 2006/07 and 2007/08. Small-scale input suppliers, agro-dealers, have never participated in the retailing of subsidised fertilisers. However, the private sector has enjoyed full participation in improved seed production and in seed retailing (including by agro-dealers), with a number of new entries supplying seed to the subsidy programme.

Private sector fertiliser activities

Over the life of the FISP there has been a decline in the supply of fertiliser to the subsidy programme by state-owned enterprises,

and a substantial increase in private sector participation. The number of private sector bidders increased by 170 percent between 2009/10 and 2011/12 with a corresponding 100 percent increase in the number of companies awarded contracts, as shown in Figure 1. Nonetheless, during the period there have been exits, including the National Association of Smallholder Farmers of Malawi, Rab Processors and Yara (who participated in 2006/07 but have not participated since).

These contracts have brought between US\$51 million and US\$110 million worth of business to the private sector in terms of new fertiliser procurement. In addition to subsidised fertilisers, the private sector also continues to import fertilisers for commercial sale, and NSO import figures show increasing availability of commercial fertilisers in spite of the subsidy. For instance, a small reduction in subsidised fertiliser between 2007/08 and 2008/09 was associated with a substantial increase in imports and hence in the quantity of fertiliser

Figure 1: Number of fertiliser contracts awarded, 2007 - 2012

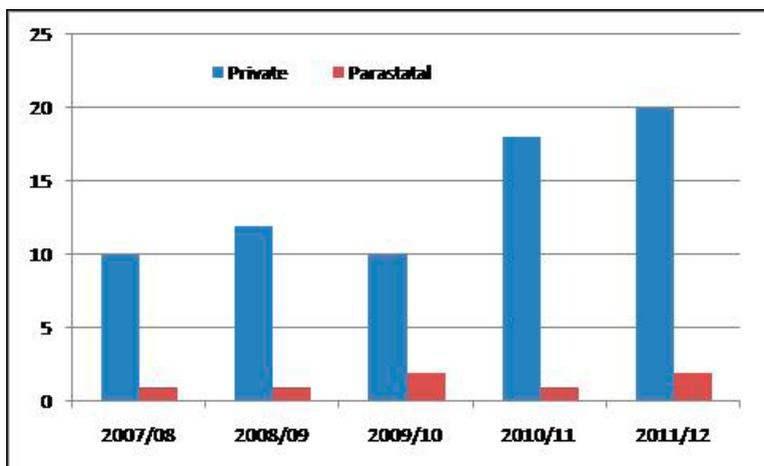
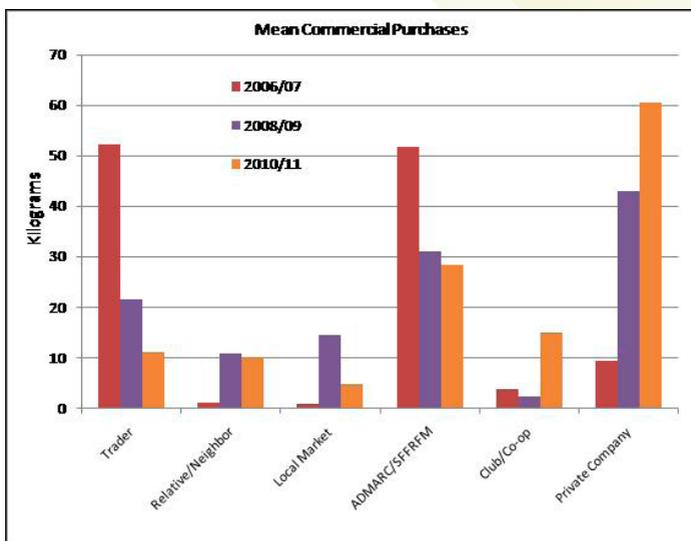


Figure 2: Mean quantities of commercial fertiliser purchases, 2006/07 – 2010/11



available for commercial sale in 2008/09. The subsidy programme in the 2010/11 season excluded tobacco fertilisers, and the increase in the available commercial fertilisers may reflect lower displacement due to the focus of the programme on maize fertilisers. Except in bad years for tobacco, there has been an overall increase in fertiliser importation and consequently an increase in fertilisers available for commercial use, suggesting that after an initial decline the subsidy programme might have stimulated fertiliser use.

The participation of the private sector in the retail marketing of subsidised fertilisers has been the most difficult aspect in relation to the development of private input markets across the country. The private sector was allowed to redeem fertiliser vouchers only in the 2006/07 and 2007/08 seasons. In these years the private sector retailed about 28 percent of subsidised fertilisers, while 72 percent were retailed by

the Agricultural Marketing and Development Corporation (ADMARC) and Smallholder Fertiliser Farmer Revolving Fund of Malawi (SFFRFM).

The buoyant picture above, with an increase in available commercial fertilisers, is also revealed in survey data about smallholder farmers' commercial purchases. There is a general increasing trend in the use of private sector input outlets in procurement of commercial fertilisers by smallholder households, and a declining trend for commercial purchases from parastatals. One reason for this decline is the withdrawal of ADMARC from commercial sales, stocking only subsidised fertilisers. The proportion of farmers making commercial purchases from large retailers' outlets increased from 5 percent in 2006/07 to 30 percent in 2010/11.

The trend in the average quantity of commercial fertiliser purchases from private sector retailers is somewhat mixed. While the average quantity purchased by households from small-scale traders has declined, there is a substantial increase in average purchases from large retail outlets, from 10 kilograms in 2006/07 to 60 kilograms in the 2010/11 agricultural season, as Figure 2 shows. Although international fertiliser prices almost tripled in the 2008/09 season, there was an increase in the reported purchase of commercial fertilisers from private retail shops. This is consistent with the lower estimated displacement in the 2008/09 and 2010/11 seasons and the decrease in the average quantity of subsidised fertilisers received by households.

Private sector seed activities

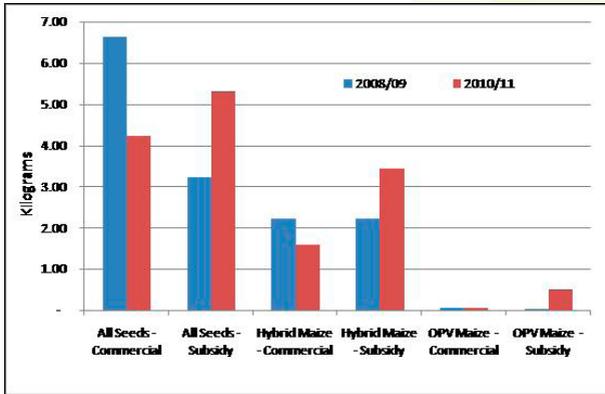
The private sector has consistently participated in the seed component of the subsidy programme, providing improved maize seeds and legumes to smallholder farmers. At the production level the seed industry is highly oligopolistic. Hybrid maize seeds that have become popular with farmers are produced by three international companies, one of which also participates in open-pollinated variety (OPV) maize seed production. The number of firms supplying various seeds to the programme increased from six companies in 2006/07 to twelve companies in 2011/12. The new entrants occurred mainly in legume seeds supply, and the competition brought by new entrants in improved maize seeds remains marginal or fringe. The three largest suppliers of seeds to the subsidy programme account for 87 percent of maize voucher redemption, with the top two alone accounting for 71 percent. Similarly, in the legume seed market, the three largest suppliers to the subsidy programme account for 75 percent of voucher redemption, with 65 percent of redemption going to two of these.

There is, however, an increase in the level of competition at the retail level in terms of the number of competitors in the local communities. Agro-dealers reported a 15 percent increase in competitors between 2005/06 and 2008/09 while distributors reported a 3 percent increase in the number of competitors. However, community surveys revealed that only 22 percent of the communities believed that the number of seed sellers accessible in their community had increased while 57 percent maintained that the numbers had remained the same between 2006/07 and 2008/09.

On average, the programme has distributed to smallholder farmers 5,852 tonnes of hybrid maize seeds, 1,839 tonnes of OPV maize seeds and 2,280 tonnes of legume seeds per year between 2007/08 and 2011/12. There was a steady increase in hybrid seeds obtained by smallholder farmers from 2007/08 up until a fall in 2011/12. On the other hand, OPV maize seeds dropped substantially in 2008/09, but then increased steadily from the 2009/10 season. In 2009/10 OPV maize seeds accounted for 12 percent of maize seeds, but the share rose to 32 percent in 2011/12. The hybrid maize share fell from 89 percent to 68 percent across the same period. Private sector business promoted directly by the seed subsidy amounted on average to US\$19.1 million per year in the past five seasons.

The data from household surveys reveal that in 2008/09 and 2011/2011 most smallholder farmers accessed improved maize seeds through ADMARC and SFFRFM retail outlets (more than 70 percent), followed by private companies' retail outlets (15. percent) and agro-dealers (8 percent). However, there was a decrease in commercial purchases of seeds as subsidised seed sales increased between 2008/09 and 2010/11 (Figure 3), suggesting

Figure 3: Volumes of seeds purchased by households, 2008/09 and 2010/11



possible displacement of unsubsidised seed purchases by subsidised seed.

Farmers are also purchasing more hybrid maize seeds than OPV maize seeds under the subsidy programme. While commercial purchases of OPV maize seeds have remained the same, for hybrid maize seeds commercial purchases declined from an average of 2.1 kilograms per household in 2008/09 to 1.6 kilograms in 2010/11. Meanwhile, in both the cases of hybrid and OPV maize seeds, there was an increase in subsidy redemption. These trends suggest that the subsidy programme is to some extent crowding out commercial purchases, although the overall use of improved seeds has been increasing.

The proportion of households accessing the private market system is small, but the average purchases of seeds from private market outlets are higher than those from parastatal outlets. Agro-dealers have played a particularly important role in facilitating access to inputs in rural areas.

Challenges to private sector participation

Although there have been positive developments in the participation of the private sector in the implementation of the subsidy programme, there are challenges that need to be resolved to improve its efficient contribution to the programme. First, despite improvements over time, there are still considerable delays in the award of tenders, particularly for the supply of fertilisers. This increases the risk of price rises, leading to protracted negotiations about supply prices and sometimes failure by companies to supply at tender prices.

Secondly, there is a problem of trust between the private sector and the Government, leading to the continued exclusion of the private sector from retailing of subsidised fertiliser. The Government believe that the private sector is driven by profit motives and pursues rent-seeking opportunities, redeeming coupons for merchandise other than fertilisers, as the sector is unable to self-regulate. The private sector dislikes the inconsistency in the Government's

decision-making, which creates uncertainty for private input market development.

Thirdly, the subsidy programme has attracted new entrants who were hitherto not interested in the fertiliser business, particularly from domestic companies. Some of these have been created just to bid for contracts to supply fertilisers to the programme. Some companies were closely connected to the political establishment, and when awarded contracts they were unable to deliver on time, no punitive measures were imposed. They continued to be awarded tenders to supply in the following season.

Fourthly, in the seed component, there is collusive behaviour among seed suppliers in deciding the supply price of seeds offered to the subsidy programme. Although the subsidy programme has attracted a number of players in seed production and supply, the pricing arrangement is tantamount to collusive pricing due to the desire by the Government to have a uniform top-up for farmers.

There is also evidence that the Government's payment system for supplies and services rendered to the programme by the private sector is inefficient. As the 2011/12 subsidy programme was taking place, the Government still owed seed, fertiliser and transport companies for supplies and services provided during the 2010/11 programme.

Opportunities from private sector participation

Greater involvement by the private sector in the subsidy programme not only promotes private sector development in input markets but can also improve efficiency in the implementation of the programme. Firstly, this can be accomplished by increasing the number

of outlets from which smallholder farmers can redeem their input coupons, thereby broadening their choice of markets. The increase in competition may consequently improve the quality of services at market outlets and reduce the incidence of queues and demands for 'tips' at the markets.

Secondly, the involvement of the private sector can also encourage private investments in rural input markets. This requires consistency and transparency in Government decisions in order to build the confidence needed for private investments in rural markets.

Thirdly, there are also opportunities for designing future private sector participation on the basis of performance-based indicators such as verifiable expansion of retail outlet coverage.

Fourthly, the subsidy can exploit opportunities for private sector involvement in storage facilities. With the exclusion of the private sector from fertiliser retail, all programme fertilisers have to be delivered at SFFRFM depots for uplifting to markets, and their congestion causes delays.

Fifthly, better methods of targeting can reduce displacement by targeting households who cannot afford to buy fertilisers at commercial prices, and therefore increase demand for commercial purchases.

Sixthly, earlier timing of coupon distribution can help farmers to plan for commercial purchases and thereby help commercial sales. Earlier distribution of coupons can bolster input sales, as those who do not receive coupons and those who receive coupons but want to top these up would be certain of their subsidised supplies and hence their need for commercial purchases.

Finally, there are also opportunities that may arise with the use of electronic vouchers. These could enable the private sector to invest in electronic systems, resulting in shared costs benefiting both parastatal and private suppliers

Conclusion

The main conclusion of the study is that although the subsidy has had some negative impacts on private sector development in the form of displacement in the short run, in the medium to long term it appears to have been catalytic in raising the demand for fertilisers and improved seeds. The private sector is increasingly the main supplier of fertilisers to the programme, and its exclusion from the retail market for subsidised fertilisers has not prevented growing demand for commercial fertilisers in the medium term. In the seeds market, the increase in the seed subsidy from 2009/10 seems to be crowding out commercial sales to some extent. However, like the fertiliser market, in the medium to long term it may stimulate demand for improved seeds as farmers witness the benefits of technology adoption.

In both the fertiliser and seed markets there is an increase in the number of private sector players, although exits, especially in the fertiliser market, are evident. However, the challenge is to translate this increase in competition into reasonably priced inputs and quality of services offered to smallholder farmers in under-served areas.

There are benefits to expanding the role of the private sector in reducing programme costs, increasing efficiency and alleviating problems of storage capacity in parastatal markets. However, the involvement of the private sector will require mutual trust among stakeholders; systems of transparency and accountability; and policy consistency and credibility.

The volume of subsidised fertiliser provision has held relatively constant, and the growing demand for commercial purchases by smallholder farmers should also provide incentives for the private sector to strategically position itself by expanding its networks in underserved areas. This could be achieved by developing sustainable partnerships with the agro-dealer network that exists in rural areas. There is also scope for increasing private participation in the fertiliser retail market through performance-based contracts to supply underserved areas.

It is also important to continuously monitor the impact of the subsidy programme on private sector markets and to monitor the integrity and efficiency of the private sector. Improving the efficiency and competitiveness of input suppliers is one of the conditions that can facilitate graduation from the subsidy programme at household, area and national levels. The efficiency of the private sector also needs to be studied through the lens of market structure (players, their market power and vertical restraints), behaviour in the market, and resultant benefits in terms of efficiency and smallholder farmer welfare.

Acknowledgements:

This Policy Brief was written by **Ephraim W. Chirwa** and **Andrew R. Dorward** for the **Future Agricultures Consortium**. The series editors are **Beatrice Ouma** and **Paul Cox**. Further information about this series of Policy Briefs at: **[www. future-agricultures.org](http://www.future-agricultures.org)**

The Future Agricultures Consortium aims to encourage critical debate and policy dialogue on the future of agriculture in Africa. The Consortium is a partnership between research-based organisations across Africa and in the UK. Future Agricultures Consortium Secretariat at the University of Sussex, Brighton BN1 9RE UK T +44 (0) 1273 915670 E info@future-agricultures.org

Readers are encouraged to quote or reproduce material from Future Agricultures Briefings in their own publications. In return, the Future Agricultures Consortium requests due acknowledgement and a copy of the publication.



The views expressed do not necessarily reflect the UK Government's official policies.