ISSUES IN RURAL INFRASTRUCTURE AND RURAL SERVICES FOR SMALLHOLDER AGRICULTURAL DEVELOPMENT IN MALAWI

FINAL REPORT

Prepared for

NASFAM Centre for Development Support
PO Box 30716
Lilongwe 3.

Prepared by

Ephraim W. Chirwa, PhD
Wadonda Consult
MPC Building, Room 317/309
P.O. Box 669, Zomba
Tel/Fax: (265) 01 527399 Mobile: (265) 08 839296
Email: echirwa@yahoo.com

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1. Introduction

The smallholder sub-sector plays an important role in generating national output and livelihood systems in the predominantly agro-based economy of Malawi. The agricultural sector accounts for more than a third of gross domestic product and generates more than 90 percent of the foreign exchange earnings. The World Bank (2003) notes that approximately 84 percent of agriculture value-added originates from 1.8 to 2 million smallholder farmers who on average own only 1 hectare of land. Recent national surveys estimate that crop production accounts for 74 percent of all rural incomes and agriculture is the most important occupation for 71 percent of the rural population. It is also important to note that more than 90 percent of the population in Malawi lives in the rural areas. The irony is that the bulk of the population that significantly contributes to the total wealth of the nation remains poor. In 1998, the integrated household survey revealed that 65.3 percent of the population were poor with consumption of basic needs below the minimum of MK10.37 (US$0.34) per day (GoM, 2000). At the same time, productivity in agriculture in general and in the smallholder sub-sector has been declining in spite of government investments in the ‘green revolution’, promotion of fertilizer technologies coupled with extension services and agricultural sector structural reforms.

Others have argued that although structural adjustment programs have resulted in removing policy linked distortions in the agricultural sector to a larger extent, these policies are not sufficient for increasing the incomes and the growth potential for a majority of the Malawian population (Kaluwa et al., 1992; Chirwa and Zakeyo, 2003). The smallholder agricultural sector still experiences problems of physical access to markets, high transaction costs due to poor infrastructure, access to credit facilities and other financial services, inequitable distribution of land and low agricultural productivity. However, the importance of infrastructure and provision of support services in the rural areas for effective agricultural development can not be understated.

Members of the National Smallholder Farmers’ Association of Malawi and smallholder farmers in general continue to experience various problems in their farming enterprises. Although investment in rural services and rural infrastructure is at the centre of poverty reduction strategies and government realizes the importance of these services for pro-poor growth (GoM, 2002), progress in improving rural services has rather been limited. NASFAM (1999) and NASFAM (2000) highlight the major issues affecting farming enterprises and the slow progress made in alleviating the rural infrastructure and rural services problems. For instance, smallholder farmers note that commercial banks operate mainly in the urban areas with products tailored towards the working urban or business enterprises, and where banking facilities exist in the rural areas the services and products do not necessarily meet the needs of the farmers.

NASFAM, in its policy platform that is based on consultations with their membership, recognizes the various channels through which poor rural infrastructure and the non-existence or poor quality of rural services impact on the performance of farming enterprises (NASFAM, 1999). For instance, the poor road infrastructure increases the transaction costs of smallholder farmers in input procurement and product marketing through high transportation costs. Lack of access to financial services undermines farmers’ potential to make savings, the long distance to banks increases transaction costs per bank transaction and lack of access to production credit affects productivity through adoption of technology. While the implications of poor rural infrastructure and lack of rural services are known from
the demand side (from the point of view of smallholder farmers), the issues that affect the supply side (providers of the services) in the rural areas and their policy implications have not been adequately analysed. It is in this light that the National Smallholder Farmers’ Association of Malawi (NASFAM), a member-owned, democratically governed and non-political organization that provides services to its smallholder farmer members commissioned this study on the in-depth analysis of rural infrastructure and rural services that affects the livelihoods of its members in particular and smallholder farmers in general.

The overall objective of this study is to gain fuller understanding of the factors that determine the provision of rural infrastructure and rural services for agricultural development in order to determine policy issues. The specific objectives of the study are to:

- determine the extent to which service providers reach out to smallholder farmers;
- describe the types of services provided by various institutions in the rural areas and assess the extent to which the designs meet the needs of smallholder farmers;
- analyse factors that impede, or that are necessary for, the provision of rural infrastructure and rural services in Malawi, and
- assess the potential collaboration between farmers’ organisations and the various service providers.

The approach adopted in the study involved conducting key informants’ interviews with various service providers in the following sectors: transport, financial markets, telecommunications, distribution particularly storage and utilities. In addition, group interviews were conducted with two NASFAM associations, one in Mchinji and the other in Lilongwe north to gain some understanding on how the various infrastructure and rural service problems affect their farming enterprise operations. Table A1 presents a list of key informants interviewed in the study.

The report is organized as follows. The next section briefly provides the theoretical and empirical link between investments in rural infrastructure and rural (agricultural) development. Section 3 presents the state and issues in rural infrastructure and rural services in Malawi. Section 4 outlines the various areas of donor support in improving rural infrastructure and services. Finally, section 5 provides concluding remarks and recommendations.

2. Rural Infrastructure, Services and Agricultural Development

The important role infrastructure and services play in rural development is well established in the development literature. Todaro (1989, 1992) argues that the level of capital accumulation and capital accumulation embodied in infrastructure development in a country is a crucial factor determining the pace and diversity of economic development. Although the direct link exists between productive investments and growth, social and economic infrastructure (such as roads, electricity, water and sanitation, and communications) facilitates and integrates economic activities. For example, a farmer can increase output following adoption of new technology or investing in farm machinery, but without adequate transport facilities and market institutions, the extra production may be worthless.

The role of infrastructure has also been asserted in rural livelihood systems. Ellis (2000) notes that roads have multiple effects of reducing the spatial cost of transaction costs in resources
and outputs; facilitate the movement of farmers between places offering different income-
earning opportunities; create markets; and serve as an important vehicle for the transfer of
information in the absence of telecommunication facilities. Investments in rural
infrastructure and rural services are often not under control of rural households, and are
typically provided by the government as public goods. Nonetheless, the quantity and quality
of social and economic infrastructure and rural services make a big difference to the viability
of rural livelihoods.

The theoretical and conceptual views on the critical role of rural infrastructure and rural
services in promoting agricultural development and livelihoods in smallholder agriculture
are largely supported by the empirical evidence in Malawi and elsewhere. Zeller et al. (1998)
in a study of smallholder agriculture in Malawi find that the household’s transaction costs in
accessing the nearest state market outlet for agricultural inputs and outputs have a negative
influence on the share of area cropped with hybrid maize and conclude that access to
agricultural markets and related improvements in rural infrastructure and marketing
institutions are essential for adoption of new technology and transformation of subsistence-
oriented smallholder agriculture.

Obare et al. (2003) find that inadequate road infrastructure imposes significant burdens on
cost-minimising smallholder farmers; and farmers faced with high farm-to-market access
costs commit less land, fertiliser and machinery resources to production in Kenya. A study in
Madagascar reveals that distance to the main paved road and the quality of the road
infrastructure connecting to the main road are significant determinants of rice prices; with
communities that have access to all season roads earning, on average, higher prices than
communities that have only access to seasonal roads or communities that do not have access
to roads (Minten, 1999). Mundlak et al. (2002) find that policy driven investments in road
infrastructure were positively related to agricultural output growth and productivity in
some Asian countries. Khandker and Faruqueel (2003) provide evidence of a significant
positive relationship between institutional credit (by state-owned agricultural bank) and
agricultural output, consumption and other household welfare indicators in Pakistan.

3. Rural Infrastructure and Rural Services in Malawi

3.1 Rural Roads Networks

3.1.1 Situation in Rural Areas

The transport infrastructure in Malawi, particularly in the rural areas, remains
underdeveloped and is one of the major constraints for economic development in general
and agricultural development in particular. The existing infrastructure is not in good
condition. For instance, most of the road network is in poor condition. Of the total
designated road network of 7,718 kilometres, 33 percent is paved and 67 percent is unpaved;
and 33.5 percent of the total road network is in poor condition and 34.9 percent is in fair
conditions while the rest is in good condition (SweRoad and Bua, 2002). The situation for
rural roads is even worse, with 33.8 percent of 7,494 kilometres of the rural road network in
poor conditions. These figures, however, do not include undesignated roads. According to
NCG (2002) about 38 percent of the roads in the rural areas are not passable during the wet
season. Smallholder farmers have also observed that in the rural areas, the road network is
poor and roads are poorly maintained, and most of the roads are not passable during the
Coupled with the problem of poor infrastructure, is the lack of transport services in the rural areas. The poor state of the road infrastructure presents many problems for smallholder farmers – it creates difficulties in access to product and input markets, increases the transaction costs of farming as an enterprise. Improving accessibility in rural areas will therefore reduce transport costs, facilitate access to markets and social facilities thereby stimulating agricultural production and non-farm activities, reduce food insecurity and improve the livelihoods of the rural population.

3.1.2 Existing Service Providers

There are a number of institutions that are involved in the rehabilitation and maintenance of feeder roads in the rural areas. The two main key players in the development and maintenance of rural road networks at a regional or national scale, particularly feeder roads, in Malawi are the Malawi Social Action Fund (MASAF) under the Public Works Programme (MASAF PWP) and the Government of Malawi / European Union Public Works Programme (GoM/EU PWP). The MASAF PWP targets all the three regions in Malawi while the GoM/EU-PWP targets selected districts in central region. In addition, the Department of Local Government is managing the Malawi Rural Travel and Transport Programme, an integrated programme of infrastructure development, capacity building and promotion of intermediate means of transport implemented through local authorities.

3.1.2.1 MASAF Public Works Programme

MASAF has been rehabilitating rural roads through the public works programme component since 1996. The MASAF public works programme is a safety net for the poor households in which MASAF funds labour-intensive public works to create employment as a cash transfer strategy while at the same time improving infrastructure in the rural areas. Projects under MASAF are funded by a loan from the World Bank. MASAF is in its Phase III in which emphasis is placed on strengthening District Assemblies (DAs) in the implementation of infrastructure projects.

The main activities under the PWP component include rehabilitation and construction of economic infrastructure such as access roads, rainwater harvesting structures, afforestation and environmental assets. However, under MASAF I, most of the projects involved the rehabilitation and construction of rural access roads. Mvula et al. (2000) find that out of 398 public works project, 85.9 percent were road rehabilitation and construction, 9.8 percent were afforestation projects, 3.0 percent were dams or water tanks and 1.3 percent were river bank rehabilitation. However, over the years there has been a gradual shift away from concentrating in road rehabilitation or construction and maintenance projects towards environment-oriented projects such as river bank rehabilitation and afforestation, particularly under MASAF II.

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1 These problems were also highlighted in a group interview conducted with members of the Chiosya NASFAM chapter in Mchinji.
2 There are other rural road rehabilitation and maintenance projects in specific districts such as under the public works programme implemented by CARE in the Central Region Infrastructure Maintenance Project (CRIMP) in Dedza and Lilongwe. Under CRIMP about 821 kilometres of rural roads were rehabilitated, upgraded and maintained through public works or small scale community contractors.
Under MASAF I and II PWP targeted infrastructure development projects in an Extension Planning Area (EPA), were identified using the Vulnerability Assessment Mapping (VAM) which focuses on food poverty and food insecurity. Once an EPA had been identified as vulnerable, there were two main ways of identifying project sites and project types. First, proposals were identified from a list of projects approved by the District Development Committee (DDC) and awaiting funding in the District Development Plan. These projects are identified by communities and submitted through their village development committees (VDC). The VDCs refer the identified projects to the area development committee (ADC), which consists of all group village heads under the Traditional Authority who chairs the committee. This committee sends project proposals to the District Assembly. Second, the members of the DA identified projects in target EPAs, in consultation with the communities using participatory methodologies. The project proposals were approved by the DDC before submission to MASAF for funding. However, under MASAF III, the emphasis is placed on strengthening the DAs in the implementation of development projects and MASAF will only fund projects that are included in the three-year District Development Plan.

Under MASAF I 5,144.6 kilometres of rural roads representing 112.7 percent of the target were constructed and rehabilitated. However, one concern about infrastructure projects under MASAF relates to the quality of infrastructure and the lack of maintenance. Under MASAF I and II, the public works programme only funded the cost of rehabilitation or construction, and handed over the assets to the DA and the communities were expected to undertake routine maintenance. The failure to maintain the roads has substantially reduced the quality of the roads. Others note that the emphasis placed on ensuring that a large proportion of the project budget is wages for unskilled labour compromises the quality of the assets (IDS et al., 2003). Under MASAF III, learning from the experiences of maintenance of created assets, there is a provision for additional funds that will be available to DAs for routine maintenance on a matching grant basis with DAs. In the first year of maintenance, MASAF will provide 75 percent of the maintenance budget while the respective DA will have to meet the remaining 25 percent; and in the second and third years the ratios will be 50:50 and 25:75, respectively.

3.1.2.2 European Union Public Works Programme

The premise of the GoM/EU public works programme is the improvement in accessibility in the rural areas as a means of improving the socio-economic status of rural communities. The overall objective of the GoM/EU public works programme is to contribute to poverty alleviation and food security. One of the strategies in achieving this objective is to address the lack of accessibility to rural areas, thereby stimulating economic activities in the rural areas that would lead to poverty alleviation and improvements in food security. Rehabilitation and maintenance of feeder roads is one of the components of the GoM/EU public works programme.4

The road component aims at improving accessibility and reducing the cost of transport, in turn enabling farmers to reach better agricultural produce and input markets. Since the

3 District Assemblies or local authorities had to agree to take over the responsibility of routine maintenance of rural roads funded by MASAF. However, due to capacity and financial constraints, most of the roads rehabilitated by MASAF are not maintained.

4 Other activities in the GoM/EU public works programme include establishments of village forestry funds, establishment of village small scale irrigation schemes and the District Assembly ‘Cash for Assets’ projects.
primary aim is accessibility, GoM/EU constructs roads to ensure their durability and long life expectancy. The road component activities include rehabilitation of low trafficked rural feeder roads, drainage improvement works and the replacement of existing timber bridge decks with concrete decks by means of labour-based construction methods (EU, 2004). The road component accounts for about 45 percent of the public works programme budget. The GoM/EU public works programme uses a multi-tier approach addressing both immediate and long term poverty alleviation and food security, through employment creation in the short-term in road rehabilitation and long term cash injection into rural economies through village based road maintenance.

The project targets districts in the central region and in the first year of implementation projects were only implemented in five districts including Lilongwe, Dowa, Mchinji, Ntchisi and Kasungu. The target districts were expanded to seven in the second year of implementation to include Salima and Nkhota-kota; and due to the savings made the programme will be extended to Dedza and Ntcheu – thus covering all the districts in central region by 2005. The projects are implemented through DAs based on participating districts’ District Development Plans. Thus for the project to benefit from the GoM/EU public works programme, communities need to submit the proposal to the DA to be considered for inclusion in the District Development Plan.

The GoM/EU public works programme completed 1,796 kilometres of road rehabilitation and 298 kilometres were still being rehabilitated; 55 bridges have been completed and 16 drainage contracts had been completed by the first month of 2004. Roads rehabilitated under the GoM/EU public works programme are maintained by the communities through the village maintenance clubs. The villages next to the road form clubs and are responsible for maintenance of the roads throughout the year. One person is responsible for maintaining 1 kilometre metre and clubs are paid based on performance through Malawi Rural Finance Company (MRFC) for the tasks that they have completed and bonuses are paid to clubs that do a good job. The clubs are provided with all the necessary tools needed to carry out maintenance work. A total of 895 kilometres of rural roads in the target districts are under the length-man maintenance system in which 102 clubs are participating with 879 members.

3.1.2.3 Malawi Rural Travel and Transport Project

The Malawi Rural Travel and Transport Project (MRTTP) is a joint initiative of the Government of Malawi and the World Bank and United Nations Economic Commission for Africa (UNECA) which seeks to address problems of accessibility of rural areas in a coherent, sustainable and well-coordinated manner. The main objective of the MRTTP is to alleviate poverty through the improvement of accessibility to socio-economic goods, services and facilities by rural communities. The MRTTP is under the Department of Local Government and plans to implement an integrated infrastructure programme through District Assemblies. The project will involve the rehabilitation and construction of rural roads, capacity building in the District Assemblies in road infrastructure construction and maintenance, and promotion of non-motorized (intermediate) means of transport. The project will first be implemented on a pilot basis in one District Assembly in which all the three components will be implemented in an integrated manner. The intermediate means of transport being promoted include bicycles, hand-carts and ox-carts.

5 Members are paid a wage of MK55 per task that is completed within 3 – 4 hours per day.
6 Two non-motorized means of transport, bicycles and hand-carts, have been tested in the 4 baseline districts (Mchinji, Mwanza, Zomba and Mzimba) and turned out that it was difficult in the rural areas
3.1.3 Issues in Rural Road Infrastructure

The major constraint in the provision of rural road infrastructure is the lack of financial resources devoted to the development of a rural road network. The National Road Authority (NRA) focuses on primary, secondary and tertiary roads. The rehabilitation and maintenance of rural feeder roads remain the responsibility of the local authorities. Most DAs are, however, financially constrained to embark on a comprehensive programme of rural road infrastructure rehabilitation and maintenance. With the decentralisation process, government and donor infrastructure programmes, such as MASAF and GoM/EU, are increasingly being implemented by District Assemblies and emphasis is being placed on funding projects that are submitted by the communities to the DAs and are contained in the District Development Plans.

There are limitations to which the resources under MASAF PWP and GoM/EU PWP can substantially improve rural infrastructure. The national-wide nature of MASAF and the emphasis on income transfers as a safety net, implies that resources are spread thinly and areas with potential agricultural activities cannot be funded is deemed not vulnerable. The GoM/EU PWP is only targeting central region. Although, GoM/EU PWP has made most rural areas accessible in Lilongwe, Dowa, Kasungu, Mchinji and Ntchisi districts, the expansion of the programme is limited to only central region. However, the advantage of GoM/EU PWP is that it is directly focusing on development of rural feeder roads in areas that have active agricultural activities. Thus, while vulnerability is one of the criteria for determining funding of a project on the District Development Plan list, the primary objective is to connect market places for agricultural development.

Another issue in rural infrastructure is the variations in the quality of the rehabilitated feeder roads due to low construction standards and poor maintenance. This is particularly true for roads rehabilitated or constructed under MASAF PWP. Most feeder roads constructed by MASAF are not maintained after rehabilitation. Under MASAF I and II the communities were expected to maintain the roads as part of community services, but since roads are public goods the free-rider problem created disincentive for the communities to maintain the roads without public works employment. Mvula et al. (2000) find that assets that had localized benefits such as dams stood a high chance of being maintained than roads. On the other hand, the roads funded by the GoM/EU PWP tend to be of better quality and regularly maintained at least within the time span of the project. However, unless the DAs are going to continue with the club system of maintaining the roads, the quality of GoM/EU public works programme roads will deteriorate.7

7 The GoM/EU PWP management unit contends that feeder roads are built to the highest standards such that with regular maintenance, the road can be in good condition for about 15 years. These roads are built under public works programme are constructed with the same quality that would be expected if conventional construction were used (EU, 2004).
3.2 Financial Institutions and Services

3.2.1 Situation in Rural Areas

The financial system in Malawi is segmented into the formal, semi-formal and informal sector and this segmentation is large although direct and indirect deposit links exist (Chipeta and Mkandawire, 1992). Formal financial institutions are those licensed under the Banking Act of 1989, semi-formal institutions are those licensed under trust law or cooperative society law and the informal system is not licensed. Prior to financial sector reforms in 1988, the formal sector comprised a few players with branch networks confined mostly to urban and semi-urban areas. Liberalisation of the financial sector has led to entry of new commercial banks, although all the new banks operate only in the main urban centres of Blantyre and Lilongwe. The bulk of the 89 percent of the population which is rural therefore makes very little use of the formal financial sector. This location problem has led to the development of the semi-formal sector in form of cooperative savings association and savings and credit associations, more generally the development of the micro finance sector. In the absence of formal banking services, the informal financial sector has proved vital for the rural population.8

3.2.2 Existing Service Providers and Rural Services

3.2.2.1 Commercial Banks and Other Financial Institutions

Commercial banks and other financial institutions are licensed under the Banking Act of 1989 to provide banking services. The license may cover retail banking (commercial banking), merchant banking, leasing and financing, discount house and mortgaging. Commercial banking licenses allow providers to accept deposits from the public and are free to intermediate the savings to borrowers.9 Following liberalisation of the financial sector, there are eight commercial banks in Malawi from two commercial banks (National Bank and Stanbic Bank (formerly Commercial Bank)) in the 1980s, the latest being the New Building Society that is converted to a commercial bank on 1st April 2004.

Most of these commercial banks, as can be seen from Table 1, are located in the main urban centres and some selected rural areas. Commercial banks typically offer services to non-agricultural activities. Although, some of the banks are relatively new and concentrating on consolidating their market position in urban markets, the extent to which the two long-established commercial banks have expanded outreach into rural towns or areas is limited. It is worth noting that the legal framework does not require banks to expand into specific areas nor does it require provision of services to particular sectors on preferential terms.

There are several reasons that the commercial banks advance for their absence in the rural areas. First, the critical effective demand for sustainable banking services in the rural areas is lacking. Savings are the cheapest form of loan capital for commercial bank and as profit

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8 Chipeta and Mkandawire (1996) assert that the commercial banking sub-sector has for too long focused on short-term lending which historically has largely targeted the foreign trade sector and large enterprises, with persistent unsatisfied demand for medium and long-term capital finance from both large and small scale enterprises.

9 The prudential regulations under commercial banking licenses are stricter than under other banking licenses, including constant supervision and maintaining the liquidity reserve ratio (imposed to protect depositors).
seeking institutions they are likely to locate in areas where the savings potential is high. Some argue that there is a lack of savings culture in Malawi more generally and in the rural areas. According to the World Bank (2001) the gross national savings as a percentage of gross domestic product in 1999 in Malawi was 10 percent compared with 14 percent for Sub-Saharan Africa and 37 percent for East Asian and Pacific countries. The low savings rate is exacerbated by the pervasive and high poverty in both urban and rural areas, and the scattered nature of settlement patterns in Malawi. Recent macroeconomic developments, such as high inflation, are also crippling the savings potential in the rural areas. There is evidence of declining profitability in commercial agriculture both in estates and smallholder sectors (World Bank 2003). Thus, for commercial banks rural areas are seen as less profitable locations for banking services.

<table>
<thead>
<tr>
<th>Name of Financial Institution</th>
<th>Type of Services</th>
<th>Locations</th>
</tr>
</thead>
<tbody>
<tr>
<td>2. Stanbic Bank</td>
<td>Commercial</td>
<td>Mzuzu, Lilongwe (2), Kasungu, Salima, Dwangwa, Dedza, Ntcheu, Blantyre (4), Balaka, Mwanza, Zomba</td>
</tr>
<tr>
<td>4. First Merchant Bank</td>
<td>Commercial</td>
<td>Blantyre (2), Lilongwe (2), Mzuzu</td>
</tr>
<tr>
<td>5. Finance Bank</td>
<td>Commercial</td>
<td>Blantyre (2), Lilongwe, Mzuzu</td>
</tr>
<tr>
<td>6. Nedbank Malawi</td>
<td>Commercial</td>
<td>Blantyre, Lilongwe</td>
</tr>
<tr>
<td>7. Loita Investment Bank</td>
<td>Merchant</td>
<td>Blantyre, Lilongwe</td>
</tr>
<tr>
<td>8. Indebank Bank</td>
<td>Commercial</td>
<td>Blantyre</td>
</tr>
<tr>
<td>9. Opportunity International Bank (OIBM)</td>
<td>Commercial</td>
<td>Lilongwe (2*), Dedza – Lobi*, Mobile Services*</td>
</tr>
<tr>
<td>10. First Discount House</td>
<td>Discount House</td>
<td>Blantyre</td>
</tr>
<tr>
<td>11. Leasing and Finance Company</td>
<td>Leasing</td>
<td>Blantyre, Lilongwe</td>
</tr>
<tr>
<td>13. Continental Discount House</td>
<td>Discount House</td>
<td>Blantyre</td>
</tr>
</tbody>
</table>


Note: * These are planned points and services.

Secondly, the problem of insecurity in the rural areas is one of the factors that constrain commercial bank expansion into rural areas. National Bank and Stanbic (then Commercial Bank) previously used to operate mobile bank facilities, but withdrew because the risk-return trade-off made operations uneconomic. The withdrawal of these services was also conditioned by the increased insecurity of mobile operations – due to some incidences of
armed robbery particularly since the 1990s. With the increase in competition in the banking sector, banks are restructuring and modernizing. Some commercial banks are more risk-averse to establishing branches or operations in rural areas and are reducing their rural outreach networks such as Stanbic Bank while others are less risk-averse and are planning to extend services into major trading centres such as National Bank in Liwonde and Salima and New Building Society in Liwonde and Chitipa.

Some banks are planning to introduce mobile banking services – such as OIBM and New Building Society Bank. OIBM, the only bank that provides documentation in Chichewa, is planning to launch a five-way mobile service with each route being served once a week (Lilongwe – Mchinji, Kamwendo – Kasungu, Lilongwe – Kasungu, Lilongwe – Salima and Lilingwe – Lobi – Dedza) with intermediate stopping points. OIBM has placed an order for an armoured vehicle that will use solar panel as source of power for the laptop and satellite that will link the mobile unit on-line with the branch in Lilongwe. OIBM is also planning to establish a containerized bank in the Area 25 and Lobi area. It should be noted, however, that the mobile services are initially going to offer savings products than loan products. New Building Society Bank is also planning to introduce mobile services starting with on-campus (educational) banking services with the possibility of extending services to the rural areas.

The Malawi Savings Bank (MSB) is undergoing through the restructuring process, albeit at a slower pace. MSB is reducing reliance on the agency arrangement with the Malawi Posts Corporation and 38 (expected to increase to 45 by the end of 2004) transacting locations are computerized and operated by its own officers. MSB is also reviewing the agency agreement with the Malawi Posts Corporation to only handle MSB operations only in 27 locations and Malawi Posts Corporation staff are being trained to handle banking operations. Nonetheless, the quality of services has not significantly improved with withdrawal limits still at MK2,000 per day from MSB operated branches and MK500 per day from Malawi Posts Corporation operated points. Larger withdrawals require five days notice or a charge of MK350 per transaction in lieu of notice subject to availability of cash. Modernization and rationalization in MSB requires a lot of cash injection in order to upgrade systems, and the lack of capital will further slow the pace of modernization in MSB.

Thirdly, the lack of complementary infrastructure such as electricity and telecommunications is also one of the factors affecting the attractiveness of rural areas as viable markets for commercial banking activities. The reliable sources of electricity and telecommunication facilities are critical in modern banking services. Nonetheless, apart from issues of security which falls within the spheres of government, there are no policy induced factors that constrain the expansion of commercial banking services to the rural areas.

3.2.2.2 Microfinance Institutions

The failure of formal financial institutions to service the poor and rural areas has led to the proliferation of semi-formal finance institutions in the form of savings co-operatives and microfinance institutions. Microfinance institutions (MFIs) tend to bring banking services closer to the poor and to the rural areas. These institutions are involved in either savings

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10 Members of staff were actually refusing to operate these services, and the option of hiring armed guards would have increased the costs of operations in a service that was already being cross-subsidized by urban services.

11 For security reasons, agencies do not hold a lot of cash. In the rural areas, this is also compounded by the low savings rate.
mobilisation or credit extension or both to clients who find it difficult to access formal financial services in the urban or peri-urban areas. Table 2 shows the main microfinance institutions in Malawi. Malawi Rural Finance Company (MRFC) operates in all districts of Malawi except Likoma district while the Foundation for International Community Assistance (FINCA) also operates in all districts except Chitipa and Likoma districts. Malawi Union of Savings and Credit Cooperatives (MUSCCO) through Savings and Credit Cooperatives (SACCOs), Pride Malawi (PM) and the National Association of Business Women (NABW) operate in all the three regions, but only cover 20, 11 and 10 districts, respectively. FINCA, used to operate mainly in urban and peri-urban areas, but more recently it is extending its outreach to the small towns in the rural areas and is planning to use the existing infrastructure to reach out clients in the rural areas. PM’s activities are mainly in the urban areas and district towns, although a small number of clients particularly in the district towns are rural entrepreneurs.

Table 2 Main Microfinance Institutions in Malawi

<table>
<thead>
<tr>
<th>Name of Financial Institution</th>
<th>Type of Services</th>
<th>Districts/Branches</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Foundation for International Community Assistance (FINCA)</td>
<td>Savings and credit</td>
<td>27 districts (except Chitipa and Likoma) with 15 branches</td>
</tr>
<tr>
<td>2. Malawi Rural Finance Company (MRFC)</td>
<td>Savings and credit</td>
<td>All districts with 198 offices</td>
</tr>
<tr>
<td>3. Malawi Union of Savings and Credit Cooperatives (MUSCCO) / Savings and Credit Cooperatives (SACCOs)</td>
<td>Savings and credit</td>
<td>20 districts with 71 SACCOs</td>
</tr>
<tr>
<td>4. National Association of Business Women (NABW)</td>
<td>Credit</td>
<td>10 districts</td>
</tr>
<tr>
<td>5. Pride Malawi</td>
<td>Savings and credit</td>
<td>11 districts with 12 branches</td>
</tr>
</tbody>
</table>

The microfinance institutions bring a number of innovations to rural banking such as group and individual loans, the principle of joint and several liability, compulsory savings, loan amounts made conditional on savings capacity, loans without collateral, use of local languages, beneficiary monitoring and business advisory services and flexible loan products and repayment schedules; aspects that are more tailored to serving the rural population.

Most of the savings in the microfinance institutions are mandatory, but in some cases clients save more than the required minimum. In 2002, for instance MRFC, SACCOs, FINCA and Pride Malawi mobilized savings amounting to US$2.44 million, US$4.86 million, US$0.59 million and US$0.36 million, respectively. Only MUSCCO - SACCOs, MRFC and Pride Malawi, manage savings accounts and determine the interest rates paid to depositors. However, only SACCOs are allowed by law to intermediate savings while others intermediate savings by virtue that the savings are maintained directly by the institution.

The loan products are also designed to suit the characteristics of small savers. Loan amounts are usually small and are usually guaranteed by a peer group. Loans are mostly given to support non-farm business activities, although SACCOs, MRFC and FINCA also offer agricultural credit facilities. MRFC requires 15 percent cash collateral for agricultural loans and for individual loans farmers are required to lodge their land title deed with MRFC in addition to the cash collateral. FINCA offers seasonal agricultural loans in addition to

12 However, resource poor farmers who cannot raise the required cash collateral are exempted from this condition in the first loan cycle provided they are in groups although the collateral is still required in subsequent loan cycles.
business through its participation in the Agricultural Productivity Improvement Programme (APIP).

Although microfinance institutions tend to be within reach of the rural communities, their banking services are limited and MFIs face several problems and constraints. First, insecurity in the rural areas makes cash management difficult. There have been a number of incidents when MRFC offices for instance have been raided by robbers. Hence, officers are not allowed to maintain substantial cash at the rural offices. Secondly, in some cases the location of MFIs depends on the availability of formal financial institutions. For example, savings for FINCA and NABW clients are managed by commercial banks to which clients are linked; and the availability of commercial banks affects the expansion their programmes into the rural areas. Thirdly, many MFIs rely on grants to expand their programmes and lack of capital is a major impediment to the extension of services in rural areas. The NABW credit programme is entirely funded from external sources and is restricted to their members. Pride Malawi also relies on grants to expand its programme. FINCA also requires some capital injection to extend outreach to rural areas, although it is the only MFI that borrows from commercial banks at market rates of around 42 percent and on-lend the funds to their clients at an annualized interest rate of 72 percent. The problem of capital in these institutions is exacerbated by the fact that although MFIs mobilize lots of savings but cannot on-lend the mobilized savings because they are neither licensed banks nor financial cooperatives. Fourthly, for MFIs that are managing clients’ savings, the savings transactions are usually inefficient with withdrawals taking about a week at MRFC.

3.2.3 Issues in the Financial Sector

The financial system in Malawi remains highly segmented with very few links between the formal, semi-formal and informal financial sectors. There is no deliberate policy by the government to encourage the expansion of banking services in the rural areas by formal financial institutions. Nonetheless, there are very few policy impediments in the banking sector that affects the efficiency and outreach expansion of services. One of the policy areas is the restrictions on intermediation by some semi-formal financial institutions, the prudential requirements of licensed banks and the security features required at banking premises. However, the Banking Act of 1989 is very flexible on the prudential requirements and provides for exceptions for special types of financial services. For instance, although OIBM is licensed as a commercial bank, the liquidity reserve requirement was waived recognizing the micro banking nature of the services being offered to their customers.

While some commercial banks are cautiously expanding into rural areas, banking facilities will remain far from the smallholder farmers in short- and medium term. MFIs, however, have greater potential in penetrating the rural areas but need to modernize and invest in rural bank infrastructure. The modernization may be important for savings products to even facilitate the handling of tobacco proceeds from auction floors. The current situation in which withdrawals are made within a week provide disincentives to savers.

There are opportunities for NASFAM associations to collaborate with some formal and semi-formal financial institution on the location of services and in improving the design of products that are smallholder farmer friendly. For instance, though it did not succeed,

13 The loans are guaranteed by a fund established with First Merchant Bank by the Department for International Development (DFID).
14 FINCA is also planning to established container bank infrastructure in some of the areas.
NASFAM and MSB piloted a partnership in which MSB handled tobacco proceeds for association members in Ntaja. There is greater willingness from formal and semi-formal financial institutions that are planning expansion into rural area to cooperate with NASFAM as they view the members as a potential critical demand for rural services.

Banks and microfinance institutions consider lending to the agricultural sector as a risky investment due to the seasonality of the income stream and the unpredictability of the natural environment particularly for rain-fed agriculture that is practiced in Malawi. Thus, most financial institutions are willing to lend to non-farm activities. Commercial banks are more risk-averse in lending to smallholder farmers or the poor. Some microfinance institutions are taking the risk of lending to the agricultural sector. However, due to the fungibility of credit, some MFIs are offering agricultural credit only as a second concurrent loan to clients that are operating a non-farm business. The non-farm activity is therefore expected to minimize the risk of default on agricultural loans in bad states of nature.

3.3 Telecommunication Facilities and Services

3.3.1 Situation in Rural Areas

Telecommunication facilities and services are still concentrated in the urban areas, although with the liberalisation of the sector some rural areas around district towns and major trading centres have access to telecommunication facilities. The expansion into rural areas has benefited from the overall reforms that are taking place in the communications sub sector. It is worth noting that communication facilities and services, prior to economic reforms, were provided by public institutions as public social goods. However, more recently the sector has been opened up to new competition from private enterprises. For instance, the number of radio stations has increased from one to more than five stations; the number of telecommunication operators has increased from one to three with the fourth already licensed. The telecommunication services, nonetheless, remain urban biased and the information content is not geared for agricultural development.

The Government of Malawi, following the Communications Sector Policy and the Communication Act of 1998 established a regulatory body, the Malawi Communications Regulatory Authority (MACRA) to oversee the development the sector and to regulate the service providers in the sector. One important aspect about the Communication Act is that it empowers MACRA to issue licenses to service providers based on the agreed expansion plans within specified periods. However, since most of the service providers are commercial, most of these expansion areas are in urban areas and district towns. Hence, the extent to which the present license holders can expand their services to rural areas where services are not commercially viable is limited. As a result of this MACRA is formulating a Rural Communications Policy that will lead to the establishment of a Rural Communication Fund and that will provide guidelines on how services can be extended into the rural areas.

3.2.2 Existing Service Providers and Rural Services

There are three main providers of telecommunication services in Malawi: Malawi Telecommunications Limited providing fixed line services, Telekom Networks and Celtel providing mobile phone services. The Malawi Communications Regulatory Authority (MACRA) has issued a license to a third mobile operator, Malawi Mobile, yet to launch its operations.
3.2.2.1 Malawi Telecommunications Limited

Malawi Telecommunications Limited (MTL) is 100 percent owned by the Government of Malawi and is the only provider of fixed line telecommunication services. MTL was initially part of the Department of Posts and Telecommunication in which services were offered as public social goods without necessarily seeking profits. The location of telecommunications facilities and services was directed by Ministry of Information, mainly responding to requests from Members of Parliament. This resulted in investment in postal and telecommunications facilities in the rural areas, particularly post offices and postal agencies. The telecommunications activities were highly subsidizing postal activities. In 1996, the Government of Malawi changed the Department of Post and Telecommunications into Post and Telecommunications Corporation, offering the same services except that it was operating as an autonomous body. In 2000, postal and telecommunications services were separated leading to the creation of the Malawi Post Corporation and the Malawi Telecommunications Limited.

Although MTL is a government owned enterprise, it has been mandated to operate commercially. This has implications for the provision of services in rural areas; commercialisation is the overriding goal and social projects cannot be funded from MTL resources. However, due to previous policies and investment decisions, MTL offers services in some rural areas. On a limited scale, MTL is also providing services in rural areas through radio shot services, although such services are highly subsidized by the services in urban areas.\(^\text{15}\) While radio shot services are suitable for rural areas, the problem is that they only accommodate two lines. However, these radio shot phone services may be appropriate in rural areas as community phones and provides a potential collaboration area between MTL and farmers’ association. MTL is also willing to provide radio shot services if the customer can pay for the cost of equipment and installation.

3.2.2.2 Telekom Networks Malawi and Celtel Malawi

Telekom Networks is the first mobile phone provider in Malawi as a joint venture between MTL and foreign investors and started its operations in early 1990s.\(^\text{16}\) Celtel Malawi is the second mobile phone provider and started its operations in the late 1990s. Most of the infrastructure is in urban and peri-urban areas, but under the licensing requirements the services are being extended to major towns, thereby covering more rural areas. Since the installations transmit within a radius of 35 kilometres, depending on the terrain, some rural areas have access to mobile services. The location of mobile services is determined by the commercial viability of the services in particular areas. Both mobile service providers started their services in the urban areas but are now expanding into rural areas.

There are no policy induced constraints in the sector, and the duty free waiver on capital equipment has helped the providers to expand services. The availability of complementary services and infrastructure, such as electricity and road network in rural areas, are major constraints in the provision of services in rural areas. In some cases, the availability of fixed line services from MTL make it difficult for mobile operators to invest in the rural areas.

\(^{15}\) These projects are carried out as social projects to serve the remote rural areas, and are not commercially viable.

\(^{16}\) This was the period when MTL was the only provider to offer telecommunication services by law, and it had to invest in the mobile phone services and the first internet service provider, MalawiNet.
because installations without MTL fixed lines is more expensive than installations with fixed line services.

Both Telekom Networks and Celtel are planning to launch new products to cater for the rural population and smallholder farmers. Three developments may have implication for rural communities. First, both Telekom and Celtel have Rural Community Service Phone projects, in which the community owns and manages a mobile phone bureau with specially designed sets. Celtel is already piloting the project in Chingale (Zomba), Cape McClear (Mangochi) and Lirangwe (Blantyre); and the unit costs MK45,000. Telekom has ordered the special handsets and are planning to provide the initial 50 sets free to rural communities, particularly to their most active agents in rural areas. The cost of the Telekom rural phone system is MK70,000. The community phone service provides opportunities for farmer organizations to operate a bureau service as an income generating activity. Secondly, Telekom is planning to introduce low cost mobile phones that will be affordable by some in rural communities. Thirdly, both Telekom and Celtel are participating in the establishment of a virtual market system in collaboration with the Initiative for Development and Equity in Agriculture in Africa (IDEAA). Telekom and Celtel will host agricultural market information collected by IDEAA which will be accessed by potential buyers and farmers through text messages. This initiative provides marketing opportunity for smallholder farmers and NASFAM could feed its marketing information in the system.

3.2.3 Issues in Telecommunication Services

There are no policy related constraints in the telecommunications sector. The existing legislations and regulations are conducive to expansion of services. The licensing requirements are conducive to expansion of services into rural areas. The licenses require that providers expand their services into specified areas, and this has provided incentives for providers to expand into some rural trading centres.

With liberalisation of the economy telecommunication services, even those previously provided by the government, are becoming more commercialized. This implies that the decision for the private or commercial operators to locate services in particular areas is determined by the commercial viability of establishing services in a particular area. The effective demand for telecommunication services given the low incomes makes it difficult for private providers to establish services that are commercially viable. For instance, most of the MTL’s installed capacity in rural areas is under-utilized. There are cases where feasibility studies had indicated potential demand for telecommunication services in rural areas but effective demand usually falls short of expectations.

Increased vandalism of facilities in rural areas is another factor that potentially limits the expansion of services. This is the case for MTL solar installed telecommunications networks in rural areas. The lack of complementary infrastructure in rural areas is another limiting factor. Telecommunications facilities, fixed line and mobile services, require electricity. Where there is no electricity, providers have to make substantial investments in diesel generated power, thereby increasing the operational costs of providing the services.

The sector is increasingly expanding into the rural trading centres. Mobile services have the potential to reach the rural areas, particularly rural areas that are within 35 kilometres radius of the major roads and towns in Malawi. Mobile service operators are planning to introduce

17 The revenues generated will be shared between mobile providers and IDEAA.
products that are tailored towards the rural communities and smallholder farmers, such as Community Mobile Phone Services and virtual commodity agricultural market information. MACRA is formulating a Rural Communication Policy that seeks to establish a fund to finance the provision of telecommunication services in rural areas where it is not commercially viable for providers to invest in such areas. These initiatives provide greater opportunities for collaboration between service providers and farmers’ associations, particularly in influencing the location of the services. In addition, the rural services also provide income generating opportunities for farmers’ associations.

3.4 Storage Facilities and Utilities for Agro-Processing

3.4.1 Situation in Rural Areas

The lack of storage facilities, electricity and piped water in the rural areas limit the extent to which smallholder farmers can increase value-added on their agriculture produce through further processing. Warehousing facilities are almost non-existent in the rural areas and this creates problems of storage for both agricultural inputs and outputs. Electricity is readily available in urban centres and district towns and the national grid is not extended to the rural areas. NSO (2000) finds that in the rural areas 98 percent of Malawians use firewood and only 0.004 percent use electricity for cooking and 93 percent use paraffin and only 0.01 percent use electricity for lighting. Similarly, only 21 percent of Malawians (rural and urban) use piped water or communal standpipes as the main source of drinking water. Piped water is mainly available in urban centres and district towns. Piped water is still provided by government enterprises, the three regional water boards, which took over the activities of the District Water Supply Funds (DWSF) which operated as a government department.

3.4.2 Existing Service Providers and Rural Services

3.4.2.1 ADMARC Warehousing Facilities

The Agricultural Development and Marketing Corporation (ADMARC) is under-going restructuring following the liberalisation of smallholder produce marketing activities. Since 1987, private traders are free to trade in all smallholder agricultural produce. This has implied that ADMARC infrastructure in rural and peri-urban areas has largely remained under utilized. This provides warehousing facility potential for farmers’ association in areas where ADMARC has warehouses. With the restructuring and commercialisation, ADMARC has made warehousing as one of its commercial products available to the public. This is likely to alleviate the problems of storage in some areas for smallholder farmers’ association that may require such services. The costs of storage are MK100 and MK75 per square metre in urban and rural areas, respectively. ADMARC also offers handling services at MK150 per tonne and fumigation services at MK170 per tonne. The cost of storage includes security and other risks attributed to the infrastructure, but the client has to bear the other risks outside the control of ADMARC. Most of the warehousing facilities are, however, in urban and peri-urban areas.

3.4.2.2 Department of Energy Affairs

More than thirty-years after independence, electricity power supply remains confined to the urban and district town centres in Malawi. Although there have been efforts to electrify the rural areas under the rural electrification project initiated in 1980, the activities have moved at a very slow pace, with a few trading centres connected to the national electricity grid.
MEPD (1996) notes that rural electrification programme administered by the Electricity Supply Commission of Malawi (ESCOM) was relatively slow because ESCOM depended on commercial loans to fund the programme whose projects are largely non-commercial. Since 1995, the Rural Electrification Programme is being implemented by the Department of Energy as a development project. Its main source of domestic funding is the Energy Fund financed by the petroleum levy. Under the rural electrification programme, the Energy Fund meets part of the capital cost of providing the grid at a trading centre from which business enterprises and households are expected to connect at commercial rates. In 2002, the Department of Energy mobilized funding from the Japanese Government and identified 54 sites across the country for Phase IV of rural electrification at a cost of MK595 million (NEC, 2002).

Table 3 Selected Grid Connection Trading Centres in NASFAM Operating Districts

<table>
<thead>
<tr>
<th>District</th>
<th>Phase IV</th>
<th>Phase V</th>
<th>Phase VI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Karonga</td>
<td>Ngala, Nyungwe, Vovwe, Majaro, Tibira, Songwe, Pusi, Kiwe</td>
<td>-</td>
<td>Iponga</td>
</tr>
<tr>
<td>Rumphi</td>
<td>-</td>
<td>Katowo</td>
<td>Chitimba-Chiweta</td>
</tr>
<tr>
<td>Mzimba</td>
<td>Kafukule, Mbalachanda, Jenda, Champhira</td>
<td>Edigeni, Euthini</td>
<td>Mpherembe</td>
</tr>
<tr>
<td>Kasungu</td>
<td>Nkhameny, Chulu, Chisempemere, Mkhotu, Dwangwa</td>
<td>Chamama, Mpela</td>
<td>Matenje, Simlemba</td>
</tr>
<tr>
<td>Mchinji</td>
<td>Mchinji Orphanage</td>
<td>Mkanda, Chiosya</td>
<td>Mikundi, Nkhwazi</td>
</tr>
<tr>
<td>Nkhotakota*</td>
<td>Mwansambo</td>
<td>Mkaika, Dwambazi</td>
<td>Msenjere, Kasitu</td>
</tr>
<tr>
<td>Salima*</td>
<td>Khombeza</td>
<td>Kandulu, Chilambula</td>
<td>Kambiri, Khwidi</td>
</tr>
<tr>
<td>Lilongwe</td>
<td>Nchezi, Kamphata, Malingunde</td>
<td>Chilobwe, Nyanja</td>
<td>Kasiya, Chawantha</td>
</tr>
<tr>
<td>Ntcheu</td>
<td>Tsangano, Border</td>
<td>Ntonda, Kasinje</td>
<td>Kdzakalowa, Kandeu</td>
</tr>
<tr>
<td>Balaka</td>
<td>Senzani, Manjawira</td>
<td>Phalula, Chendausiku, Kwitanda</td>
<td>Phimbi</td>
</tr>
<tr>
<td>Mangochi</td>
<td>Cape Maclear, Jalasi, Malembro</td>
<td>Makanjira, Chilipa</td>
<td>Chiponde, Majuni</td>
</tr>
<tr>
<td>Zomba</td>
<td>Chingale, Mowo</td>
<td>Jenale, Sunuzi</td>
<td>Zane, Muwa</td>
</tr>
<tr>
<td>Phalombe*</td>
<td>Chiringa</td>
<td>Mlomba</td>
<td>Phaloni, Chitekese</td>
</tr>
<tr>
<td>Thyolo</td>
<td>Thekerani</td>
<td>Nansadi, Fifite</td>
<td>Lalakani, Thomasi</td>
</tr>
<tr>
<td>Mulanje</td>
<td>Abunu, Nasomba</td>
<td>Chinyama, Nkando</td>
<td>Namthombozi, Chambe</td>
</tr>
<tr>
<td>Chikwawa*</td>
<td>Kasisi, Chapananga, Njereza, Mitekete, Nkhate, Mwamphazi</td>
<td>Mitondo, Linvunzu</td>
<td>Kakoma, Tomali</td>
</tr>
</tbody>
</table>

Notes: * NASFAM expansion areas; Phase IV is being implemented; Phase V has been funded by JICA debt relief; Phase VI sites are identified but not funded.

Source: Department of Energy, Rural Electrification Programme
Some of these trading centres and the intermediate places are already connected to the national electricity grid. Table 3 provides a list of trading centres that fall under different phases of implementation in existing and expansion NASFAM districts. For example, in Karonga most of the trading centres will be connected to electricity under Phase IV. This should open up opportunities for agro-processing activities in some rural areas. However, realizing the capacity problem of the national electricity grid, the Department of Energy is also looking into the feasibility of establishing mini-hydro stations on some rivers in Malawi with technical assistance from Japanese Agency for International Cooperation (JICA).

The Department of Energy is also involved in the promotion of other forms of energy, especially for lighting, in collaboration with communities. Two projects exist for rural communities: the Solar Project at individual level and the Solar Project in schools and clinics. Under the first project the Department of Energy is negotiating with microfinance institutions to provide funding to individuals in rural areas to acquire solar panels. Under the second project, each district has been allocated funding for solar installations at two schools or clinics in which the community will equally share the cost of installation with government funding. The schools or clinics solar project is community driven through the district assemblies.

While the Department of Energy is making tremendous efforts in lighting-up rural areas, there are constraints that may affect their outreach to rural areas. First, the lack of funding is a major constraint to the expansion of rural programmes. The Energy Fund is small and donor funding forms a significant part of the cost of installations. Hence, the expansion of the programme depends on the continued willingness of donors to provide funding to the sector. Secondly, in the short to medium term, the capacity of the only supplier of grid electricity, ESCOM, given the many problems it is experiencing may hamper the extent to which the national grid may be extended to other rural areas.

3.4.2.3 Regional Water Boards

Three regional water boards in Malawi are responsible for piped rural water supply after taking over the activities of the DWSF in 2000. Two water boards were included in this study: the Central Region Water Board (CRWB) and the Southern Region Water Board (SRWB). The objective of regional water boards is to bring commercial aspects in the provision of water in the district towns and rural areas. The surplus generated is expected to finance the expansion of water services into rural areas. The CRWB is already installing piped water in some rural trading centres as part of its expansion program as presented in Table 4 while the SRWB is basically upgrading and operating in areas inherited from the DWSF.

The CRWB has also finalized feasibility studies for the supply of piped water mostly in rural trading centres while several points have been identified as potential areas for installation of piped water. This has been possible because the CRWB have been able to move from a loss making position to a profitable organization. The CRWB is willing to collaborate with communities to install water facilities provided there is critical and effective demand – especially where there is potential for agro-processing or industrial activities. This collaboration may extend to management contracts with the communities in which communities run water facilities as an income-generating activity under contract with CRWB.
In contrast, the SRWB is still struggling – it continues to make losses and has not expanded the water infrastructure beyond what it inherited from the DWSF. In addition, many of the existing water supplies experience problems of poor water quality, inadequate water and dilapidated pipe network. For instance, in Balaka the water source is Mpira Dam and the water quality is low while in Namwera the borehole yield is quite low and additional boreholes are required to provide adequate water to the area. In Luchenza, the SRWB is sharing water intake with rural water supply and in most cases the demand is not met. In addition, the finance charges, resulting from a loan inherited from DWSF, are affecting the bottom line and the extent to which they can upgrade the existing system and expand into new areas.

Table 4 Region Water Boards’ Current and Proposed Water Supply 2004

<table>
<thead>
<tr>
<th>District</th>
<th>Existing Piped Water Supply</th>
<th>Proposed Water Supply</th>
</tr>
</thead>
<tbody>
<tr>
<td>CRWB</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nkhota-kota-Nkhota-kota, Dwangwa</td>
<td>Benga, Mwansambo</td>
<td></td>
</tr>
<tr>
<td>Kasungu</td>
<td>Kasungu</td>
<td>Nkhamenya, Chulu, Chamama, Santhe</td>
</tr>
<tr>
<td>Ntchisi</td>
<td>Ntchisi</td>
<td>Malomo, Mwangalanga*</td>
</tr>
<tr>
<td>Salima</td>
<td>Salima, Chipoka, Senga Bay</td>
<td>Chinsepo*</td>
</tr>
<tr>
<td>Dowa</td>
<td>Dowa, Madisi, Mponela, Mvera</td>
<td>Chinsepo*</td>
</tr>
<tr>
<td>Mchinji</td>
<td>Mchinji, Kochilila</td>
<td>Mkanda, Kamwendo, Kapiri,</td>
</tr>
<tr>
<td>Lilongwe</td>
<td>Likuni, Mitundu, Area 25</td>
<td>Namitete, Nthenje, Lumbazi, Nambuma, Kasiya*, Nsar*, Nsundwe*</td>
</tr>
<tr>
<td>Dedza</td>
<td>Dedza,</td>
<td>Lobi, Mayani, Thete, Mtakataka</td>
</tr>
<tr>
<td>Ntcheu</td>
<td>Bembeke, Nkhande,</td>
<td>Lizulu, Kampepuza/Nsipe</td>
</tr>
<tr>
<td>SRWB</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mangochi</td>
<td>Namwera, Monkey Bay, Mangochi</td>
<td>Maldeco*</td>
</tr>
<tr>
<td>Balaka</td>
<td>Balaka</td>
<td></td>
</tr>
<tr>
<td>Machinga</td>
<td>Liwonde, Machinga</td>
<td></td>
</tr>
<tr>
<td>Zomba</td>
<td>Domasi, Zomba</td>
<td>Malosa*, Thondwe*</td>
</tr>
<tr>
<td>Chiradzulu</td>
<td>Namadzi, Chiradzulu, Mikolongwe</td>
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</tr>
<tr>
<td>Mwanza</td>
<td>Mwanza</td>
<td></td>
</tr>
<tr>
<td>Thyolo</td>
<td>Luchenza, Thyolo</td>
<td></td>
</tr>
<tr>
<td>Mulanje</td>
<td>Mulozo,</td>
<td></td>
</tr>
<tr>
<td>Phalombe</td>
<td>Phalombe</td>
<td></td>
</tr>
<tr>
<td>Chikwawa</td>
<td>Chikwawa, Nchalo, Ngabu</td>
<td></td>
</tr>
<tr>
<td>Nsanje</td>
<td>Nsanje</td>
<td></td>
</tr>
</tbody>
</table>

Note: * Feasibility studies have not yet been conducted in these sites.
Source: Central Region Water Board

Water services, like other utilities, in Malawi are becoming commercialized and providers are likely to rank commercial viability first rather than the social objective in their decision to install piped water services. One problem, with water services in rural areas is that the effective demand is low and very few households can install individual connections. Furthermore, most houses in the rural areas are not designed for in-house connections, and at best individual connections will be in form of outside taps. Thus, in many cases the presence of agro-processing or industrial activities or a large service institution (such as a school and a health facility or mission) can justify the installation of water services.
The second problem that constrains the expansion of water services is the increasing arrears the government institutions have with the water boards. The major consumers of water from the regional water boards are government institutions such as education institutions, prisons, health facilities, police and defence. These have mounting debts with water boards, but are institutions in which water boards find it politically sensitive to terminate services. However, the failure to pay water bill substantially affect the revenue of the water boards and may limit the expansion of water services into other rural areas. The third problem is the lack of complementary infrastructure such as electricity. Most of the water facilities in rural areas use ground water in which boreholes are drilled and the water from boreholes is pumped into a reservoir tank using electricity and distributed into various areas. Thus, availability of electricity is critical in the supply of piped water in rural areas.

3.4.3 Issues in the Utilities Sector

The utilities sector is under-going reforms and utilities are moving away from being provided by government as public goods towards private sector participation in the provision of services. This transformation implies that the overriding objective is shifting from social provision of services towards commercial viability. Although, currently water and electricity are being provided by government owned enterprises, there is greater emphasis in providing services with a view of achieving commercial viability. This has implication for expansion of utilities in rural areas. Thus, for rural areas to attract these services, like any other commercial service, there must be critical effective demand to warrant installation of electricity and piped water.

There are no policy induced constraints in the provision of utilities in the rural areas. The major constraint is lack of adequate resources and low effective demand in the rural areas. The problem of lack of resources is exacerbated by the huge arrears government institutions have with service providers, particularly regional water boards. However, electricity services are being expanded to rural areas through the rural electrification programme and subject to continued donor funding most of the major trading centres and intermediate areas will be connected to the national electricity grid. Similarly, water services are being extended to the rural areas by the regional water boards, particularly in the central region by the CRWB. The expansion of electricity to major rural trading centres will also facilitate the installation of piped water in the major rural trading centres, providing income-generating opportunities for farmers’ associations. There is high potential for collaboration with rural communities or farmers’ associations in the provision of piped water if there is potential for agro-processing in the area.

4. Donor Support and Programmes towards Rural Services

Several donors are providing financial and technical support towards rural infrastructure and services, although in some cases donor co-ordination has been less optimal. We identified four main donors with programmes which support the development of rural infrastructure.18

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18 This is by no means an exhaustive list of donors that are supporting rural infrastructure and services. There are other donors that support the development of rural services such as United Nations Capital Development Fund (UNCDF) in rural finance and Department for International Development (DfID) in rural feeder roads.
First, the World Bank is providing support in rural roads rehabilitation and is planning to provide support towards communications and distribution sub-sectors. The World Bank has been supporting rural roads infrastructure through MASAF – a project that has now entered into Phase III. MASAF road rehabilitation and construction works are community-driven and are implemented in all the three regions. The World Bank is also supporting the MRTTP in the Department of Local Government. The World Bank is also financing the land reform programme that will strengthen property rights through titling of customary land as customary estates which could in turn be used as collateral by smallholder farmers.

The World Bank is also formulating the Rural Livelihoods and agricultural Development Programme (RLADP) that is targeting smallholder farmers – with the aim of improving access to infrastructure for agricultural development. The components will include access roads for agricultural development, private sector-led communication facilities and distribution facilities (markets and warehousing). This programme is at formulation stage, and there are opportunities for stakeholder to provide input on how the project could benefit smallholder farmers.

Secondly, the European Union (EU) provides support towards rural feeder roads rehabilitation in the central region under the GoM/EU Public Works Programme. The completion date for the current programme is April 2005. The EU is also formulating a programme for Phase II in which funding will also be provided to communities to construct grain banks in addition to the current programmes under Phase I.

Thirdly, the United States Agency for International Development (USAID) is implementing several programmes in support of the development of rural infrastructure. The programmes are in areas of microfinance, road and other physical infrastructure. First, smallholder farmers are going to benefit from the promotion of the microfinance sector under the Microfinance Sector Support Programme that is being formulated. The Microfinance Sector Support Programme is at the planning stage and an assessment study of the microfinance sector has just been completed. The objective is to support four financially sustainable microfinance institutions with the potential of expanding financial services to the rural areas. Secondly, USAID is also formulating a five-year programme, Development Assistance Package, in which 8 non-governmental organisations will be given food aid to implement food for work projects. The food for work projects will concentrate on infrastructure development and environmental projects such as feeder roads, water harvesting structures and soil conservation structures.

Finally, the Japanese International Cooperation Agency (JICA) is currently providing support in rural electrification. The Japanese Government completed a Rural Electrification Master Plan that forms the basis for the phased programme of connecting major trading centres to the national electricity grid. The Rural Electrification Master Plan also plans to install mini-hydro stations on several rivers in Malawi.

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19 USAID is currently providing funding for OIBM and had previously provided funding to FINCA – Malawi.
5. Conclusions and Recommendations

More than forty years after independence, the road network remains poorly developed and most of the essential services for the development of the agricultural sector remain inaccessible to the majority of the population that contribute significantly to national wealth. The services tend to be concentrated in the urban areas where less than 8 percent of the population lives. Without essential infrastructure development and appropriate services in the rural areas, the task of reducing poverty or improving livelihoods will be a daunting one. This study set out to investigate the extent to which essential services for agricultural development reach out the rural areas and understand the factors, including policy-induced factors, which influence service providers in locating services in rural areas. The study focuses on five sub-sectors including rural road infrastructure, financial services, telecommunication services, distribution and utilities for agro-processing.

5.1 Conclusions

The main conclusion from the study is that there are no major policy impediments for the extension of services to the rural areas. In sub-sectors where policy-induced constraints exist, they are not a major limiting factor in the provision of efficient services in the rural areas. This study, however, shows that there are opportunities in which farmers’ associations can enhance accessibility to services through collaboration with private providers of services. Some of these opportunities may provide avenues for diversifying the income bases of associations through service-based income generating activities.

Most of the services that were previously provided by the government are being provided by private entrepreneurs whose main objective is to seek profits. The decision to provide services in a particular area is therefore determined by the commercial viability of the services. It therefore implies that services in the rural areas can only be attracted if there is a critical mass for the demand of the services provided by private entrepreneurs. This critical effective demand in many rural areas is lacking due to the high levels of poverty and the low population density. In the long-run, it will be the success of farmers’ association in terms of enhanced livelihoods of its members and investments in agro-processing activities that will provide a conducive environment for the provision of services.

Rural Road Infrastructure

- With respect to rural road infrastructure, the government is still the main provider of rural feeder roads rehabilitation services in partnership with various donors. The implementation of road rehabilitation and maintenance projects is becoming decentralized and all projects must undergo through the local government planning structures. All rural road infrastructure programmes are being channelled through the District Assembly. MASAF and EU/GoM Public Works projects and the MRTTP of the Department of Local Government will only focus on projects that are contained in the three-year District Development Plans.

- There are concerns, however, about variations in the quality of roads and maintenance plans under public works by different sponsoring agents. Rural roads under EU/GoM PWP appear to be of higher quality and better maintained than those under MASAF PWP.
Financial Markets

- Financial markets remain highly segmented and formal financial institutions have limited outreach in rural areas. Most financial institutions seek to maximize profits and will only provide services in areas where it is commercially viable. The rural areas are associated with low savings and economic activities that are highly seasonal with unpredictable risks. These factors combined with insecurity in the rural areas affect the extent to which financial institutions expand into rural areas. However, some financial institutions are willing to collaborate with farmers’ organizations in designing products that are best suited to smallholder farmers.

- The development of microfinance institutions tends to ease the financial constraint among smallholder farmers where such institutions exist. However, the services that they provide are limited and savings services are highly inefficient with withdrawals being restricted or taking weeks. With inefficiencies in savings products offered by microfinance institutions, efficient delivery of tobacco proceeds can only be accomplished by banks whose savings withdrawal services are immediate on demand and without undue restrictions.

- Most commercial banks are highly risk-averse towards lending to the agricultural sector. Similarly, microfinance institutions tend to focus on off-farm credit, and where seasonal agricultural credit is available the loans are given on the basis that the off-farm enterprise would be able to cover agricultural loan obligations in case of eventualities in agriculture. Most lack adequate capital for expansion a situation that is exacerbated by restrictions on intermediation of savings that they mobilize from customers. While this is justified on prudential grounds such as the protection of depositors, it limits the revenue base for the expansion of services in the rural areas.

- There are no major policy impediments in the financial sector. The Banking Act of 1989 provides several exceptions on prudential requirements that could be made for microfinance institutions such as the minimum reserve requirements, capital adequacy, inspections and reporting and the regulatory framework.

Telecommunications

- Telecommunication services are more commercialized and expansion of services into the rural areas depends on the effective demand for services, which is often low to support the massive investment expenditure in installing telecommunications facilities.

- There are no policy related impediments in the provision of telecommunication services in the rural areas. However, there is no policy on the provision of telecommunication services in rural areas where it may not be economically viable to install a facility. MACRA is drafting a Rural Communications Policy that will address the issue of funding for services in the rural areas. Nonetheless, the sub-sector has benefited from duty exemptions on equipment; and the licensing conditions that require providers to agree on an expansion programme have contributed to the improvements in accessibility of telecommunication services, particularly from mobile service providers.
Mobile telecommunications providers are designing products that will increase access of mobile services by rural communities through bureau services and increase access to market information through text messages.

**Distribution**

- Storage facilities to support holding of agricultural products and inputs and agro-processing activities are virtually not available in most rural areas. However, the recent commercialization of ADMARC offers opportunities for renting warehousing space in their underutilized warehouses where available. However, most of their warehouses are in urban or peri-urban areas.

**Utilities**

- The utilities, water and electricity, are provided by government owned enterprises with commercial orientation. The location of utilities by service providers depends on the effective demand for services in an area that can make investment commercially viable. The regional water boards are responsible for provision of piped water in district and rural towns, but there are variations to which the various water boards are expanding water services into the rural areas. The Central Region Water Board is expanding outreach beyond what it inherited from the DWSF and covers more rural trading centres than the Southern Region Water Board that is just rehabilitating the water supplies it inherited from DWSF.

- There are no policy distortions that affect the expansion of water services into the rural areas, but the main problem is the huge arrears that government departments (as major consumers) in small towns have with the water boards.

- Rural electrification is facilitated by the Department of Energy Affairs in which major trading centres are being connected to the national electricity grid. Implementation is based on the Rural Electrification Master Plan which has identified several rural trading centres for electrification in different centres. Under the current phase, Phase IV, more that 54 trading centres are being connected to the national grid. Availability of funding, especially donor funding is critical for the expansion of electricity into rural areas, thereby creating opportunities for agro-processing activities.

### 5.2 Recommendations

The economic environment in Malawi has changed from a situation where essential services were being provided by the government to one where essential services are provided by private entrepreneurs. Within this context, it is improvements in rural incomes that will attract services to rural areas. However, since the development of basic physical infrastructure remains the responsibility of government, investment in the road network is critical for the regeneration of rural areas as centres of agricultural development. Overall, NASFAM should place itself strategically to take advantage of the various opportunities that exist in development programmes and rural services. The study recommends the following:

- Since the development of rural road infrastructure is increasingly being decentralized and implemented by DAs through District Development Plans that place emphasis on community driven projects, farmers’ associations should set up Development
Committees within its committee structures. The Development Committee, *inter alia*, should be responsible for identification of infrastructure development, mobilization of the community in development of project proposal and submission of projects for consideration in the District Development Plans.

- NASFAM should lobby for representation on the District Development Committee of District Assemblies to ensure that development programmes are sensitive to the needs of smallholder farmers. This will also ensure that NASFAM members are aware of the procedures that need to be followed in submitting infrastructure development proposals to the DAs.

- Government should ensure that, regardless of the funding, there is a common standard for rural feeder roads rehabilitation and maintenance. For roads constructed under public works programme, the standards used by the EU/GoM Public Works Programme and the club based maintenance plans should be adopted by the DAs even on MASAF funded projects. This also requires capacity building in DAs for those responsible for the implementation of public works programmes.

- NASFAM should lobby the government to establish clear banking policies with respect to microfinance institutions, including tiered regulation and unambiguous provisions for microfinance institutions in the Banking Act with respect to prudential guidelines and intermediation of savings.

- NASFAM should promote a savings culture among its members and diversification into off-farm activities. One way to achieve this is to link association members to microfinance institutions that have forced savings products and offer off-farm credit. This will also help smallholder farmers to diversify their livelihoods.

- NASFAM should strategically collaborate with various service providers in locating services in particular areas and in the design of services that meet the needs of smallholder farmers. NASFAM should collaborate with
  - Financial institutions that are operating or expanding into rural areas or rural trading centres such as National Bank, New Building Society Bank, Malawi Savings Bank and microfinance institutions FINCA, MRFC and MUSCCO.
  - Mobile phone service providers in two areas: hosting of NASFAM market information on output and input prices and in the Rural Community Phone Projects as possible income generating activities for associations. Some of the pilot projects could be hosted by farmers’ associations.
  - Water service providers in order to influence the location of piped water supply especially where there is high potential for agro-processing activities.
References

NCG (Nordic Consulting Group) Rural Transport Needs Assessment Study: Road Maintenance and Rehabilitation Project, Final report presented to Department of Local Government, Malawi Rural Travel and Transport Programme.

SweRoad and Bua (2002) Consultancy Services for the Preparation of a Five-Year Business and Strategic Plan, Final Report submitted to the National Roads Authority.


### ANNEX TABLES

Table A1 List of Key Informants’ Interviewed in the Study

<table>
<thead>
<tr>
<th>Sector and Name</th>
<th>Designation and Organisation</th>
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<tr>
<td><strong>NASCENT</strong></td>
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</tr>
<tr>
<td>Mrs. B. Chinyamunyamu</td>
<td>Director, NASCENT</td>
</tr>
<tr>
<td>Mr. T. Shawa</td>
<td>Policy and Programs Manager, NASCENT</td>
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<tr>
<td><strong>Rural Roads</strong></td>
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<tr>
<td>Mrs. I. Manjolo</td>
<td>Director Public Works Programme, MASAF</td>
</tr>
<tr>
<td>Mr. T. Mahoney</td>
<td>Environmentalist, GoM/EU PWP Management Unit</td>
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<tr>
<td>Mr. M. R. Mumba</td>
<td>Deputy Irrigation Manager, GoM/EU PWP Management Unit</td>
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<tr>
<td>Mr. J. Chagunda</td>
<td>Manager, Malawi Rural Travel and Transport Programme</td>
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<tr>
<td><strong>Financial Markets</strong></td>
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<tr>
<td>Mr. B. Mkandawire</td>
<td>Operations Manager, MUSCCO</td>
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<tr>
<td>Mr. S. Mgwadira</td>
<td>Operations Manager, OIBM</td>
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<tr>
<td>Mr. S. Mlotho</td>
<td>General Manager, Malawi Rural Finance Company</td>
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<tr>
<td>Mrs. M. Kamoto</td>
<td>Area Business Manager, Stanbic Bank</td>
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<tr>
<td>Miss. M. Malunga</td>
<td>Executive Director, National Association of Business Women</td>
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<tr>
<td>Mr. W. Mijiga</td>
<td>Market Analyst, National Bank of Malawi</td>
</tr>
<tr>
<td>Mr. B. Boby</td>
<td>Manager, Operations, National Bank of Malawi</td>
</tr>
<tr>
<td>Mr. I. Bonongwe</td>
<td>General Manager, Malawi Savings Bank</td>
</tr>
<tr>
<td>Mr. J. Banda</td>
<td>Operations Manager, Malawi Savings Bank</td>
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<tr>
<td>Mr. J. Mononga</td>
<td>Managing Director, FINCA Malawi</td>
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<tr>
<td>Mr. S. Mkwamba</td>
<td>Marketing and Business Development Manager, NBS</td>
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<tr>
<td><strong>Telecommunications</strong></td>
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<tr>
<td>Mr. S. Ulemu</td>
<td>Deputy Director General, MACRA</td>
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<tr>
<td>Mr. A. Joabe</td>
<td>Marketing Manager, Telekom Networks</td>
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<tr>
<td>Mr. K. Sambo</td>
<td>Marketing Manager, Celtel Malawi</td>
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<tr>
<td>Mr. M. N. Katsala</td>
<td>Finance Director, Malawi Telecommunications Limited</td>
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<td><strong>Distribution</strong></td>
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<tr>
<td>Mr. Kaima</td>
<td>Logistics Manager, ADMARC</td>
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<td><strong>Utilities</strong></td>
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<tr>
<td>Mr. H. W. Chitenje</td>
<td>Deputy Director, Department of Energy Affairs</td>
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<tr>
<td>Mr. D. Nyasulu</td>
<td>Engineer, Rural Electrification Programme, Energy Affairs</td>
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<tr>
<td>Mr. C. K. Zulu</td>
<td>General Manager, Central Region Water Board</td>
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<tr>
<td>Mr. Beza</td>
<td>Operations Manager, Southern Region Water Board</td>
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<tr>
<td>Dr. K. Wiyo</td>
<td>Program Development Specialist (Agriculture), USAID</td>
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<tr>
<td>Mr. S. Hiwa</td>
<td>Senior Agricultural Economist, World Bank</td>
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<tr>
<td>Mr. A. Chikuni</td>
<td>Programme Officer, NORAD</td>
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<td><strong>Smallholder Farmers</strong></td>
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<td>MAC Members</td>
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