THE LANDSCAPE FOR IMPACT INVESTING IN SOUTHERN AFRICA
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We would especially like to thank our interview participants. Without their key insights this report would not have been possible. We include a full list of interviewees in the Appendix.

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COMMON ACRONYMS

AFD  Agence Française de Développement (French Development Agency)
AfDB  African Development Bank
BIO  Belgian Investment Company for Developing Countries
BoP  Base of the Pyramid
CEPGL  Communauté Économique des Pays des Grand Lacs (Economic Community of the Great Lakes Countries)
COMESA  The Common Market for Eastern and Southern Africa
CSR  Corporate Social Responsibility
DFI  Development Finance Institution
DFID  The Department for International Development (United Kingdom)
EIB  European Investment Bank
ESG  Environmental, Social, and Governance
FDI  Foreign Direct Investment
FMCG  Fast-Moving Consumer Goods
FMO  Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (Netherlands Development Finance Company)
GDP  Gross Domestic Product
GIIRS  Global Impact Investing Ratings System
GIZ  Gesellschaft für Internationale Zusammenarbeit (German Agency for International Cooperation)
HDI  Human Development Index
ICT  Information and Communication Technology
IFAD  International Fund for Agricultural Development
IFC  International Finance Corporation
IMF  International Monetary Fund
LP  Limited Partner
MDG  Millennium Development Goal
MFI  Microfinance Institution
MSME  Micro, Small, and Medium-Sized Enterprises
NGO  Non-Governmental Organization
OFID  OPEC Fund for International Development
OPIC  Overseas Private Investment Corporation (United States)
PE  Private Equity
PPA  Power Purchasing Agreement
PPP  Purchasing Power Parity
PTA  Preferential Trade Area Bank
RFP  Request for Proposal
SACCO  Savings and Credit Co-operative
SGB  Small and Growing Business
SME  Small and Medium-Sized Enterprises
SOE  State-Owned Enterprises
TA  Technical Assistance
UN DESA  United Nations, Department of Economic and Social Affairs
UNCTAD  United Nations’ Conference on Trade and Development
USAID  The United States Agency for International Development
VAT  Value-Added Tax
VC  Venture Capital
WASH  Water, Sanitation, and Hygiene
WHO  World Health Organization

COMMON TERMS

Early-stage business  Business that has begun operations but has most likely not begun commercial manufacture and sales
Focus countries  Countries under study wherein non-DFI impact investors are most active, namely Madagascar, Malawi, Mozambique, South Africa, Zambia, and Zimbabwe
Growth-stage business  Company has a functioning business model, and its current focus is developing new products/services or expanding into new markets
Mature business  Profitable company with a developed and recognizable brand
Non-focus countries  Countries covered by the study but that have limited non-DFI impact investor activity, namely Angola, Botswana, Lesotho, Mauritius, Namibia, and Swaziland
Venture-stage business  Sales have begun but cannot sustain the company’s operations. The business model is still being aligned with the realities on the ground
MALAWI
Densely populated, strategically located
TABLE OF CONTENTS

About this Report ................................................................. 2
Introduction .................................................................................. 3
Country Context ............................................................................. 3
   Gross Domestic Product .......................................................... 5
   Foreign Direct Investment ......................................................... 6
   Inflation and Exchange Rates ................................................... 7
Supply of Impact Investing Capital ............................................. 8
   Broader Investing Landscape ..................................................... 8
   Impact Capital Disbursed ........................................................ 9
   Investments Over Time ............................................................ 10
   Sector ..................................................................................... 11
   Deal Size ................................................................................. 13
   Instrument ............................................................................... 14
   Local Presence .......................................................................... 15
   Impact Tracking Standards ...................................................... 15
Demand and Need for Impact Investing Capital ..................... 16
   Entrepreneurs .......................................................................... 17
Enabling Impact Investing: The Ecosystem ............................. 18
   Regulatory Environment ......................................................... 18
   Ecosystem Players .................................................................. 21
Challenges and Opportunities for Impact Investors ............... 22
ABOUT THIS REPORT

MOTIVATION

The impact investing industry has grown in prominence over the last decade, and impact investors globally have developed substantial and particular interest in sub-Saharan Africa, given the region’s strong potential for investments to drive positive social and environmental impact. Despite strong interest, relatively little research has examined impact investing markets at the country level within the continent. This type of granular information is essential to investors currently operating in the region or considering investments there in the future.

This study provides detailed information on impact investing activity across 12 countries in Southern Africa. For each country, the report examines impact investing capital disbursed at the time of data collection in mid-2015 (by sector, size, and instrument), analyzes key trends in the industry, and describes the challenges and opportunities available for social enterprises and impact investors. Political and/or economic circumstances may have changed since initial data collection.

SCOPE

As defined by the GIIN, impact investments are “investments made into companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return.” A commitment to measuring social or environmental performance is considered a hallmark of impact investing. Investors who do not meet this definition have not been included in this report’s analysis.

Development finance institutions (DFIs) are important actors in the impact investing landscape, providing large amounts of capital both through direct impact investments and through indirect investments through other impact capital vehicles. Because of their large size and unique nature, this report analyzes DFI activity separately from the activity of other types of impact investors.

METHODOLOGY

This report relies heavily on primary research, including more than 60 interviews with local and international impact investors, social enterprises, ecosystem players, and government institutions. The research team also examined publicly available primary information, including analyzing investor documents and reviewing organizational websites and press releases to compile a comprehensive database of impact investing activity across all 12 countries in Southern Africa. Overall, this report includes data regarding the activities of 25 DFIs and 81 non-DFI impact investors, totaling over 8,600 transactions including substantial activity from DFIs based in South Africa.

More detailed information on methodology and scope is provided in the ‘Introduction & Methodology’ chapter. All chapters of this report can be found at www.thegiin.org.
INTRODUCTION

Malawi is a small, landlocked country of approximately 118 thousand square kilometers in Southern Africa, bordering Tanzania, Zambia, and Mozambique (see Figure 1). With a population of 16.36 million and at 142 people per square kilometer, Malawi is one of the most densely populated countries in the world. Malawi is classified as a “least-developed country,” with a 2013 gross domestic product (GDP) per capita of only USD 226.

Malawi has attracted limited international impact investment. The country has an underdeveloped private sector and suffered in 2013 from a high-profile public corruption scandal, known as “Cashgate,” in which public officials embezzled more than USD 32 million. Although Malawi’s economy is growing, it depends considerably on agriculture and suffers from a large trade deficit, as it lacks the industrial base necessary to produce many basic goods.

COUNTRY CONTEXT

In 2014, Malawi celebrated 50 years of independence, throughout which it has enjoyed political stability. Since introducing a multi-party system in 1994, the country has held five relatively peaceful presidential and parliamentary elections. Malawi’s most recent elections—in May 2014—featured 11 parties and resulted in the election of Professor Arthur Peter Mutharika of the Democratic Progressive Party (DPP) as President. Mutharika, the brother of a former president, defeated the incumbent, Joyce Banda. Ms. Banda’s loss in the elections was likely influenced by the Cashgate scandal.

Cashgate has had both economic and political implications, as many donor organizations withdrew monetary support for the Malawian government following the scandal: government grants fell from 14.5 percent of GDP in 2012-2013 to 4.4 percent in 2013-2014. Without this support, the government’s fiscal deficit in 2013-2014 exceeded 8.6 percent of GDP, a large increase from 1.3 percent in 2012-2015. Although the government has made some attempts to reduce its discretionary spending, overall expenditures have increased due to interest payments on domestic debt and an increase in the public-sector wage bill.

As a result of the scandal, donors report that many of the funds previously allocated directly to the government are now supporting specific projects instead. It is unclear if or when donors will restore their previous levels of direct financial support for the Malawian government. This has created uncertainty for the government, private sector, and overall economy alike. Consequently, the government has reduced its expectations of donor funding in its 2014-2015 budget, planning to receive aid funds equivalent to only 6.1 percent of GDP.

Malawi is a member of the Southern African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA). As a result, Malawi has minimal tariffs to trade with other COMESA and SADC members under the terms of the COMESA Customs Union and SADC Free Trade Area, though some tariffs with South Africa remain in place.

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8 Ibid.

9 Ibid.

10 Open Capital Interviews.
Gross Domestic Product

In 2014, Malawi’s GDP at purchasing power parity (PPP) was USD 13.7 billion.\(^{11}\) Malawi’s GDP has grown approximately eight percent year-on-year in PPP terms over the last decade (see Figure 2).\(^{12}\) This growth has been driven by expansion across sectors, primarily agriculture, and information and communication technologies (ICT), and wholesale and retail trade.

![Figure 2. GDP (PPP), 2005–2014](source)

Agriculture, which grew 6.1 percent in 2014, remains the dominant sector in Malawi’s economy.\(^{13}\) Although it accounts for only 30 percent of GDP, agriculture is responsible for 90 percent of exports and employs over 80 percent of the population.\(^{14}\) Tobacco, known as Malawi’s “green gold,” is the country’s primary export crop, accounting for over half of its total exports;\(^{15}\) tobacco was a major contributor to 2014 growth as production increased by 14 percent despite a reduction in price.\(^{16}\)

Recent growth in the agricultural sector is partly due to public expenditure, as the government continues to heavily subsidize farming activities. The Farm Input Subsidy Program, which subsidizes up to 97 percent of the cost of inorganic fertilizer for

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smallholder farmers, accounted for 70 percent of government spending on agriculture in 2014 and comprises 10 percent of the entire national budget. Such heavy public spending limits the ability for producers to diversify both within agricultural value chains and to other sectors, both of which are sorely needed.

Efforts to diversify Malawi’s economy have shown some success, with introductions of tea and cotton as new export crops and an increase in local manufacturing. The development of a uranium mine at Kayelekera accounted for 12 percent of 2013 exports and presented additional opportunities for diversification, though mining operations were suspended in February 2014 when fallen demand resulted in global uranium prices that were 50 percent lower. As a result, Malawi earned only USD 10 million from uranium exports in 2014, less than 10 percent of the value of uranium exports in 2013.

### Foreign Direct Investment

Malawi’s net foreign direct investment (FDI) has fluctuated significantly in recent years, from a high of USD 195 million in 2008 to a low of USD 49 million in 2009. The majority of FDI has been into the mining sector, with fluctuations largely driven by project finance requirements. As part of its 2011–2016 Malawi Growth and Development Strategy (MGDS II), Malawi seeks to encourage FDI in agriculture, tourism, energy, and transportation infrastructure. Within agriculture, priority crops include sugar cane, legumes, and all large-scale commercial crops, as well as irrigation projects across value chains. To further facilitate FDI, the government established a One Stop Service Center in 2012 at the Malawi Investment and Trade Center (MITC) to serve investors. Though still nascent, this entity’s goal is to streamline investor entry into Malawi and house all necessary information, functions, and registration procedures in one bureaucratic unit.

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Inflation and Exchange Rates

Until 2012, the Malawian kwacha was pegged to the US Dollar at a fixed rate of 166 to one. In May 2012, Banda’s government devalued the kwacha by 33 percent to meet donor demands prior to increasing donor funding. Immediately following devaluation, Malawians saw sharp increases in the prices of basic goods and fuel. Since 2012, the kwacha has continued to depreciate against the dollar, including 15 percent depreciation in 2014 (see Figure 3).

FIGURE 3. INFLATION AND USD/MWK EXCHANGE RATE, 2005 - 2014

Like the exchange rate, the inflation rate in Malawi has risen sharply over the past few years. Inflation tripled between 2011 and 2012 from seven to 21 percent. It reached a high of more than 27 percent in 2013 before falling to just over 24 percent in 2014. The African Development Bank projects that inflation will fall to 15 and 10 percent in 2015 and 2016, respectively, but as recently as February 2015, the World Bank estimated inflation at 19 percent. High inflation continues to impair household cash flows, especially among the poor, while increasing the cost of borrowing and creating uncertainty for investors.

SUPPLY OF IMPACT INVESTING CAPITAL

Impact capital is relatively limited in Malawi. Though many vehicles for impact capital based in South Africa and elsewhere include Malawi in their geographic mandate, few have operations in-country or staff on the ground, and only 68 known impact investments have been completed to date.

Broader Investing Landscape

Impact capital therefore represents a small portion of the total capital available in Malawi (see Figure 4). Banks, which control approximately 70 percent of total financial-sector assets, dominate the country’s financial landscape. Two privately owned banks hold more than half of total assets and deposits. Overall, banks have access to sufficient, affordable capital and are performing well financially.

![Figure 4. Impact Capital Relative to Other Financial Assets](image-url)

Source: World Bank Indicators


Nevertheless, access to finance is still a challenge for individuals and businesses, as only 54 percent of Malawi’s population had access to formal financial services in 2014.28 Interest rates are above 35 percent, making it challenging for companies with commercial debt to generate positive returns.29 In addition, banks often have high collateral requirements that many businesses are unable to meet,30 while local actors report that banks lack the understanding required to lend to small- and medium-sized enterprises (SMEs).31 There are few financial-service providers to support the capital needs of start-ups and growing enterprises.32

Donor organizations are a key source of capital in Malawi, but, according to some interviewed development organizations, they often target larger companies with higher turnover, which are perceived as less risky. However, donors increasingly recognize the need growing businesses have for funding.33 The United Nations Development Programme in Malawi launched the Malawi Innovation Challenge in 2014, a USD eight million facility providing up to 50 percent matching grants to innovative businesses in agriculture and manufacturing.34

**Impact Capital Disbursed**

Malawi’s small market size is reflected in the known impact investments to date. Only one percent of all non-development finance institution (non-DFI) impact capital disbursed in Southern Africa has been placed in Malawi, amounting to approximately USD 57 million in 30 deals (see Figure 5). Similarly, about one percent of all direct investment in the region by DFIs has been placed in Malawi, totaling just over USD 266 million disbursed through 38 direct investments (see Figure 6).

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31 Open Capital Interviews.


34 Malawi Innovation Challenge Fund, http://www.micf.mw/
Investments Over Time

One of the reasons for Malawi’s low rates of impact investing is the relative infancy of the market, particularly for non-DFI investors (see Figure 7). The first non-DFI investments in Malawi were made in 2006, with investment growth picking up in 2011. (Worth noting is that the year of investment is unknown for a high proportion of deals.)

Notes: Average deal sizes may not equal displayed capital disbursed divided by deal sizes. Capital disbursed rounded to nearest million, except where less than 1 million (rounded to nearest 100,000). Average deal sizes rounded to nearest 100,000.
Source: Open Capital Research
DFI investments have a longer history. Almost 40 percent of recorded investments were placed before 2005 (see Figure 8).

![Figure 8. DFI Impact Investments by Year](image)

Notes: Average deal sizes may not equal displayed capital disbursed divided by deal sizes. Capital disbursed rounded to nearest million, except where less than 1 million (rounded to nearest 100,000). Average deal sizes rounded to nearest 100,000.

Source: Open Capital Research

**Sector**

Of the sectors targeted by non-DFI impact investors, agriculture has received the most attention (around 30 percent of all known deals in Malawi), with strong interest from multiple investors (see Figure 9). These deals included investments in primary production and inputs. As is common with non-DFI impact investments throughout the region, investment in financial services represents a large share of total investment due to the larger ticket sizes possible when placing capital into established institutions. Financial-services investments in Malawi have been focused in banks and microfinance institutions (MFIs).
A large proportion of DFI direct investments have been in financial services (31 percent of all deals and 37 percent of total capital disbursed). These investments are predominantly in banks (see Figure 10). Meanwhile, tourism-related investments have mostly been made in hotels, and manufacturing investments have largely been focused in agro-processing.
Deal Size

Most non-DFI impact deals in Southern Africa are less than USD one million, and Malawi is no exception. In Malawi, almost 80 percent of deals have been below USD one million (see Figure 11).

**FIGURE 11. NON-DFI IMPACT INVESTMENTS BY DEAL SIZE**

<table>
<thead>
<tr>
<th>CAPITAL DISBURSED (USD MILLIONS)</th>
<th>NUMBER OF DEALS</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; 250k</td>
<td>0.2</td>
</tr>
<tr>
<td>250-500k</td>
<td>0.4</td>
</tr>
<tr>
<td>500k-1m</td>
<td>0.6</td>
</tr>
<tr>
<td>1-5m</td>
<td>1.5</td>
</tr>
<tr>
<td>5-10m</td>
<td>7.1</td>
</tr>
<tr>
<td>&gt; 10m</td>
<td>16.3</td>
</tr>
</tbody>
</table>

**Notes:** Average deal sizes may not equal displayed capital disbursed divided by deal sizes. Capital disbursed rounded to nearest million, except where less than 1 million (rounded to nearest 100,000). Average deal sizes rounded to nearest 100,000.

**Source:** Open Capital Research

DFI direct investments in Malawi are often significantly larger, averaging over USD six million, more than five times the average size of non-DFI impact investor deals (see Figure 12). This difference is primarily due to DFIs’ preference for investments in infrastructure and financial institutions. Malawi does, however, have a higher proportion of DFI deals under USD one million than does the region (25 percent of all deals compared to 12 percent regionally). This is likely due to the smaller opportunities in Malawi more broadly, with these small deals spread across a number of industries, including tourism, agriculture, manufacturing, and healthcare.

**FIGURE 12. DFI IMPACT INVESTMENTS BY DEAL SIZE**

<table>
<thead>
<tr>
<th>CAPITAL DISBURSED (USD MILLIONS)</th>
<th>NUMBER OF DEALS</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; 1m</td>
<td>0.4</td>
</tr>
<tr>
<td>1-5m</td>
<td>2.5</td>
</tr>
<tr>
<td>5-10m</td>
<td>6.7</td>
</tr>
<tr>
<td>10-20m</td>
<td>13.0</td>
</tr>
<tr>
<td>20-50m</td>
<td>30.5</td>
</tr>
<tr>
<td>&gt; 50m</td>
<td>-</td>
</tr>
</tbody>
</table>

**Notes:** Average deal sizes may not equal displayed capital disbursed divided by deal sizes. Capital disbursed rounded to nearest million, except where less than 1 million (rounded to nearest 100,000). Average deal sizes rounded to nearest 100,000.

**Source:** Open Capital Research
**Instrument**

Non-DFI impact investors in Malawi prefer debt instruments (see Figure 13). Anecdotally, many of those interviewed report that Malawian entrepreneurs do not understand equity instruments and, even when they do, are reluctant to relinquish company control to an external investor. Only two equity transactions have been reported, though these have been larger in size (averaging nearly USD 1.4 million) than debt transactions (averaging USD 0.8 million).

![Figure 13. Non-DFI Impact Investments by Instrument Type](image)

**Notes:** Average deal sizes may not equal displayed capital disbursed divided by deal sizes. Capital disbursed rounded to nearest million, except where less than 1 million (rounded to nearest 100,000). Average deal sizes rounded to nearest 100,000.

Source: Open Capital Research

The prominence of debt over other instruments is also seen in deals by DFIs, which have overwhelmingly used loans to make direct investments in Malawi (see Figure 14). These loans are, on average, substantially bigger in size (averaging nearly USD seven million) than the completed equity transactions (averaging USD four million).
Local Presence

Few impact investors have offices in Malawi. Only six impact investors have established a full-time presence in Blantyre or Lilongwe, none of which are headquartered in the country and four of which are DFIs. However, investing in Malawi often requires deep local knowledge and government connections in order to navigate the bureaucratic landscape and facilitate deals. Investors on the ground identified their local presence as a key factor in their success. Of those investors who are active in the country but do not have a local presence, interviewees identified finding local partners and hiring key management positions within their portfolio companies as alternative options to mitigate risk and facilitate success.35

Impact Tracking Standards

Across the region, most impact investors do not use a specific standard for measuring the impact of their investments. This is also true in Malawi. Instead, investors typically use flexible reporting that is customized for each new investment, which allows investors to reduce the administrative burden for their portfolio companies and focus on the most meaningful metrics.

35 Open Capital Interviews.
DEMAND AND NEED FOR IMPACT INVESTING CAPITAL

Malawi has a strong need for impact capital across a wide range of industries. Even in agriculture, where the majority of the population is employed, there is little commercialization or value-addition. Further, many basic services are lacking or underdeveloped in Malawi, creating an opportunity for entrepreneurs and their investors to meet these needs.

Despite recent economic growth, Malawi has seen minimal improvement in human development indicators and continues to lag global and regional averages (see Table 1). In 2013, Malawi ranked 174th out of 187 countries in the United Nation’s Human Development Index (HDI) with a score of 0.41, much lower than the regional average of 0.55. Of countries in the region, only Mozambique has a lower HDI score than does Malawi. The country’s low overall ranking indicates low performance across multiple measures, including measures of poverty, health, and education.

<table>
<thead>
<tr>
<th>DEVELOPMENT INDICATOR</th>
<th>Malawi</th>
<th>Regional Average</th>
<th>Global Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>HDI SCORE (RANKS 174th OF 187 COUNTRIES)</td>
<td>0.41</td>
<td>0.55</td>
<td>0.69</td>
</tr>
<tr>
<td>GDP PER CAPITA (USD)</td>
<td>750</td>
<td>6,874</td>
<td>17,975</td>
</tr>
<tr>
<td>UNEMPLOYMENT RATE (%)</td>
<td>8</td>
<td>13</td>
<td>6</td>
</tr>
<tr>
<td>POPULATION BELOW USD 1.25 / DAY (%)</td>
<td>62</td>
<td>51</td>
<td>25</td>
</tr>
<tr>
<td>UNDER-FIVE MORTALITY (PER THOUSAND BIRTHS)</td>
<td>71</td>
<td>75</td>
<td>47</td>
</tr>
<tr>
<td>POPULATION WITH SOME SECONDARY EDUCATION (%)</td>
<td>9</td>
<td>41</td>
<td>59</td>
</tr>
</tbody>
</table>

More than 60 percent of Malawi’s population lives on less than USD 1.25 per day, nearly three times the global average. Poverty disproportionately affects rural residents, as 95 percent of Malawi’s poor live in rural areas.37

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Malawi’s gross enrollment in secondary education is half the Southern Africa average. Only nine percent of the Malawian population age 25 and above has attended some secondary school, a figure lower than every other Southern African country for which data is available, except Mozambique. Improvement of Malawi’s educational system is critical for its future development. Much like its neighbors, Malawi’s population is disproportionately young, with 66 percent of the population under the age of 25. Without an adequate educational system, youth in Malawi struggle to find work, and entrepreneurs find it challenging to source talent with the skills needed to build their enterprises.

**Entrepreneurs**

Malawi has an underdeveloped private sector that is largely defined by current and former parastatals and family businesses. As an import-based economy with a large trade deficit, Malawi depends on foreign goods to meet many basic needs.

Despite these gaps, it is challenging for entrepreneurs to start businesses. The private sector is plagued by a variety of issues including poor infrastructure, limited available talent, and burdensome regulation. As mentioned above, access to capital remains another key constraint in Malawi, with banks lending at interest rates above 35 percent and few active impact capital vehicles. Entrepreneurs who lack adequate personal or family capital are often unaware of the process to follow to raise capital and struggle to find affordable financing.

Even if entrepreneurs are able to finance their businesses, government regulations make the process of starting a business challenging. Entrepreneurs interviewed report that the steps, costs, and requirements to register and launch a business are time-consuming and confusing. Interviewees report that the process is significantly more manageable for those who have professional or personal connections with government officials.

New enterprises also struggle to maintain profitability due to a lack of adequate infrastructure. Many report frequent power cuts and low-quality roads as factors that increase the costs of doing business. Those businesses producing physical goods for export cannot rely on the Malawi Bureau of Standards (MBS) to certify their products because it is not internationally recognized, so they must first send their goods to South Africa, which further increases their cost and time-to-market. Though donors have provided funding to increase MBS’s capabilities, the government has yet to invest in the necessary infrastructure.

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40 Open Capital Interviews.
ENABLING IMPACT INVESTING: THE ECOSYSTEM

Malawi’s ecosystem is challenging for entrepreneurs and investors to navigate, restricting business in the country. Opaque government regulations can stifle innovation, while high interest rates, volatile foreign exchange, and government intervention in the private sector limit profitability.

Businesses have limited options in the broader ecosystem when seeking support. While lawyers and accountants are available, few service providers or intermediaries are active in Malawi.

Regulatory Environment

Though the Malawian government continues to express openness to investment in government communiqués, the country’s current regulatory system makes it difficult to do business. The World Bank currently ranks Malawi 164th out of 189 countries on its “Ease of Doing Business” rankings, slipping Malawi one place since 2014.41 Unpredictable government regulations create an uncertain economic environment, which makes day-to-day operations and long-term strategic planning challenging for both businesses and investors.

There have been some recent improvements. Donors have provided support to improve the regulatory environment, and the Malawian government has made efforts to foster investment, including the One Stop Service Center mentioned above.42 Regulatory considerations include:

- **Land ownership:** Land ownership in Malawi is complex, with three types of land tenure—customary, leasehold, and public.43 It is vital that investors understand the tenure and legal implications of any land they are looking to acquire. Customary land is held by groups and individuals in the community.44 It cannot be sold outside that community.45 The most common form of land tenure in Malawi, customary

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42 Open Capital Interviews.


land accounts for 70 percent of the total land.\(^{46}\) The government has in the past leased out customary land to boost investment.\(^{47}\) Leasehold land can be held for a fixed period of less than 99 years or a freehold for more than 99 years, depending on the intended use.\(^{48}\) Leasehold land is available to foreigners, but first priority is given to Malawians.\(^{49}\) Public land is owned by the government and publicly accessible, usually comprising national parks and historical and cultural areas.\(^{50}\)

- **Government and private sector:** The Malawian government has given preferential treatment to certain State-Owned Enterprises (SOEs), which can make it difficult for private enterprises to compete. For example, some SOEs are allocated additional foreign exchange and receive subsidized financing from the central bank.\(^{51}\) Other SOEs benefit from taxpayer bailouts. In 2005, it was reported that the government spent about USD 70 million annually assisting loss-making parastatals.\(^{52}\) Nevertheless, the government has made some progress towards privatization. Over the past decade, 66 SOEs have been privatized, including the National Bank of Malawi, the National Insurance Company, Malawi Railways, and the Mining and Investment Development Corporation.\(^{53}\)

- **Exit opportunities / restrictions on exits:** Malawi allows full repatriation of investment capital, dividends, profits, interest, and principal on internationally sourced funding. The Reserve Bank of Malawi (RBM) authorizes commercial banks to approve funds for remittance if sufficient foreign exchange is available and if the accounts are audited. However, foreign funding must be registered with the RBM, which approves the terms of any investment.\(^{54}\)

- **Forex controls:** As discussed, the kwacha has experienced sharp swings since 2012. In a bid to ensure that the country has sufficient foreign exchange to cover imports, the RBM will sometimes withhold foreign exchange when scarce, typically from October to March, when the country does not receive foreign-exchange inflows from tobacco exports.\(^{55}\)

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48 Ibid.


• **Interest rate controls:** Currently, the RBM has no publicly stated interest rate controls; banks are free to set their own rates.\(^{56}\) Despite this lack of explicit controls, regulated lenders are typically prohibited from charging rates that are too low, which the RBM considers anti-competitive.\(^{57}\) In August 2015, Malawian commercial banks were charging interest rates above 35 percent per year. The high cost of borrowing is attributed to the RBM’s high interbank lending rate, currently around 25 percent.\(^{58}\)

• **Required local shareholding:** The Malawian government has very few regulations concerning foreign ownership in companies. The only restriction is that entities privatized under the SOE privatization program cannot be 100 percent foreign-owned.\(^{59}\)

• **Incentives:** The Malawian government offers a wide range of investment incentives that apply equally to both foreign and local investors.\(^{60}\) Some of these include:
  
  • Loss carry-forward of up to seven years.\(^{61}\)
  
  • A 100 percent investment allowance for new buildings and equipment.\(^{62}\)
  
  • A 40 percent investment allowance for used buildings and equipment.\(^{63}\)
  
  • A 50 percent investment allowance on qualifying training costs.\(^{64}\)
  
  • Operating expenses are 100 percent tax-deductible for manufacturing companies during the first 25 months of operation.\(^{65}\)
  
  • No duty is charged on raw materials used by manufacturers.\(^{66}\)

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\(^{57}\) Open Capital Interviews.


\(^{60}\) Ibid.


\(^{63}\) Ibid.

\(^{64}\) Ibid.

\(^{65}\) Ibid.

Ecosystem Players

Malawi has a limited network of support for entrepreneurs and businesses. The US Department of State notes that Malawi’s inadequate educational system has created a skills shortage in certain service-oriented professions, such as law and accounting.67

Local entrepreneurs report that Malawi does not have a community to foster support and collaboration and lacks the stable institutions that could encourage such a community to develop. Other than mHub and Flame Tree Initiative, few incubators or accelerators exist to help entrepreneurs start new ventures. There are a few business-advisory firms present in Malawi, such as Imani Development and Business Consult Africa, while others, like Greater Capital, serve the country from regional hubs in Kenya and South Africa (see Figure 15).

FIGURE 15. SELECTION OF CURRENTLY ACTIVE INTERMEDIARIES AND SERVICE PROVIDERS

Note: Chart focuses on those with local presence; international players are also active.
Source: Open Capital research, organization websites.

CHALLENGES AND OPPORTUNITIES FOR IMPACT INVESTORS

As Malawi continues to stabilize and grow, there are many areas where impact investors could generate both social and financial returns. Among other opportunities, these include the development and commercialization of agriculture, improved provision of basic goods and services, development of infrastructure, and diversification of Malawi’s export base. The current financial landscape presents a clear gap that impact investors could fill, supporting innovative, high-potential businesses in various stages of growth.

However, as they seek to do so, investors are likely to face numerous challenges, including:

- **Insufficient investment-ready deal flow**: Due to the underdeveloped private sector in Malawi, few businesses are ready and willing to accept external capital. Many businesses still operate informally and lack both clear historical accounts and forward-looking strategies and projections. Businesses that are owned and operated as family enterprises often have a longer track record but are wary of equity investments.

- **Government relations**: As mentioned above, public and private interests are sometimes at odds in Malawi. The government’s drive to increase revenues in light of its loss of donor funds due to the “Cashgate” scandal can come at the expense of the private sector. Onerous and unclear regulations make it challenging for entrepreneurs and investors to launch and sustain profitable enterprises in Malawi. Multiple interviewees expressed frustration at the lack of documentation regarding how to navigate government processes, mentioning this absence as a key inhibitor of their ability to start or grow a business. To succeed in this environment, investors must be patient and prepared to nurture relationships with government officials.

- **Corruption**: The status quo, in which businesses can struggle without government connections, lends itself to abuse and corruption by officials in power. As “Cashgate” demonstrates, the country continues to struggle with graft in the public sector, which can increase the cost of doing business and reduce operational efficiency. Malawi was ranked 110th out of 174 countries on Transparency International’s 2014 “Corruption Perceptions Index,” a substantial drop from its position at 91 the previous year.68

- **Competition with donor funding**: Donors have played an important role in Malawi’s development, but they can alter the prospects for commercial funders looking to enter the market. With donors offering grant financing, entrepreneurs may be less likely to seek commercial funding. Donors also affect potential

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markets for entrepreneurs: donor projects often provide goods and services the demand for which SMEs could otherwise fulfill, and businesses may struggle to convince customers to pay for products they previously received with subsidy. Finally, donors affect entrepreneurs’ ability to recruit skilled talent in Malawi. Historically, donor organizations and the government have been viewed as the prime employment options for educated Malawians. Entrepreneurs report they must overcome this perception in order to recruit talent, only to find they must also compete with the wages paid by donor organizations, which may be significantly higher than their businesses can support.  

- **Forex and interest risk:** Recent foreign-exchange uncertainty makes it challenging for businesses to bear foreign-denominated debt. Few investors are able to bear forex risk and struggle to disburse in kwacha. Consequently, investors must charge high interest rates to mitigate this risk and must abide by the Reserve Bank’s regulations, which may make it challenging to deploy capital.

- **Access to land:** Malawi is densely populated and has limited land. As mentioned above, approximately 70 percent of Malawi’s land is classified as customary, controlled by traditional leaders and their communities. Development requires the consent of these communities, who must be relocated and compensated. Through the Investment and Trade Centre, the government has launched initiatives to acquire and develop land for use by entrepreneurs and investors, but these are inconsistently available.

- **Inefficient borders and facilitation of trade:** Given its geographic location, Malawi is well-positioned to distribute goods to both East and Southern Africa, but regional trade accounts for only 30 percent of its current trade. Despite regional trade agreements, Malawi still has non-tariff barriers inhibiting trade, including export bans on some crops, an ineffective Standards Bureau, and road blocks on major transportation routes. Local actors also report inefficient operation of and corruption at border crossings.

Despite these challenges, impact investors have numerous opportunities to deploy capital in Malawi effectively in order to generate financial and social returns while fostering economic growth and job creation. Given Malawi’s current status, it is likely that investment in almost any sector—not just conventional impact areas—will generate social returns. For example, current impact investors have made investments in construction. Though not a traditional impact sector, these investments were made with the intention to grow jobs and improve infrastructure. Areas of opportunity include:

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69 Open Capital Interviews.


73 Open Capital Interviews.

• **Leverage TA facilities for building the pre-investment pipeline:** Many of Malawi’s growing businesses are not ready for investment and lack the tools they need to adequately navigate the investment process. Pre-investment support is needed to help businesses improve their operations and reach a stage where they can successfully raise capital and use disbursed funds effectively.

• **Diversify Malawi’s export base:** Malawi’s exports currently rely on agriculture, with tobacco alone constituting more than half of total exports.\(^75\) This makes the country vulnerable to external factors, such as fluctuations in the price of tobacco, and less robust to internal challenges, such as crop failures or unpredictable rains. The government recognizes the need to diversify the country’s export base and is actively encouraging investment in other crops, including sugar, tea, and maize.\(^76\)

• **Establish presence with limited competition:** Despite the need for financing, very few impact investors are currently active in the country. Impact investors willing to invest resources in Malawi today have the opportunity to source prime investments and establish a brand long before the market becomes more competitive.

• **Develop a local team and talent:** Investors and entrepreneurs interviewed stress that success in the Malawian market depends on a team that has experience and familiarity with the particular local context. Given the informal nature of business in Malawi and the challenging regulatory environment, it is vital that investors develop a local team with an active presence and the ability to navigate the market.

In addition, impact investors in Malawi see specific opportunities in the following sectors:

• **Agriculture:** Malawi’s agricultural output is heavily dependent on smallholder farmers. Most farming still occurs without irrigation or mechanization. Investors have the opportunity to support commercial farming of numerous crops, which can increase production and food security while boosting agricultural exports, especially to regional partners.

• **Agro-processing:** Concurrently, much of Malawi’s current agricultural output is exported to other markets for processing. Although reliable infrastructure is a challenge, investors and entrepreneurs have the opportunity to develop local agro-processing operations, which can reduce the country’s dependence on imports while simultaneously boosting exports.

• **Tourism:** Malawi is well-known for Lake Malawi, yet it struggles to consistently attract significant numbers of international tourists due to the high costs of travel, poor infrastructure, and an underdeveloped tourism sector. Interviewees report that tourists can find better value visiting other countries, such as Kenya and South Africa, but that additional investment could spur the tourist industry in Malawi.

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\(^76\) Ibid.
• **Manufacturing:** Malawi has an abundant supply of unskilled labor and a low cost base, both of which are conducive to the development of local manufacturing. Local markets exist, as well, since Malawi currently imports many basic goods. The country is also well-positioned geographically to reach markets across East and Southern Africa with locally produced goods.

• **Aquaculture:** Lake Malawi has an abundant supply of ornamental fish, yet few enterprises exist to export such fish. Opportunities in this sector also include fishing for local and international consumption.
ABOUT THE GLOBAL IMPACT INVESTING NETWORK

The Global Impact Investing Network (GIIN®) is a nonprofit organization dedicated to increasing the scale and effectiveness of impact investing. The GIIN builds critical infrastructure and supports activities, education, and research that help accelerate the development of a coherent impact investing industry. For more information, see www.thegiin.org.

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