



Strengthening Structured Markets in Malawi Securing Sustainable Markets for Farmers

Workshop Report

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Implemented by



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1. Rationale for the Workshop

Compared to most African countries, Malawi is at the forefront of structured trade and markets developments, with two agricultural commodity exchanges providing structured market services, such as warehouse receipts, access to finance, market information and trade facilitation. Furthermore, in 2019 a new legal and regulatory framework, the Warehouse Receipt Act and the Commodity Exchange Directive, will come into effect, further strengthening the sector.

The developments in Malawi have not come about without their challenges; exchanges are struggling to become financially viable by scaling up operations and creating a sustainable structured trade environment evidenced by minimal participation of smallholder farmers and SMEs on the commodity exchanges. In March 2018, AICC presented a report to the DCAFS¹ group of development partners, outlining challenges facing commodity exchanges in Malawi, which threaten the sustainability of exchanges. An outcome of this discussion was a joint sense of urgency and need for such challenges to be discussed in and tackled by a wider group of stakeholders. The discussion also emphasized the timeliness of an ongoing IFPRI study on the Malawian commodity exchange landscape including the Warehouse Receipt System. In addition, in June 2018, USAID's Southern Africa Trade and Investment Hub and INTL FCStone organised a regional structured trade seminar in Zambia, which sparked a new interest in regional structured markets, i.e. to support and promote regional trade flows by creating linkages between the existing Exchanges. The AfDB requested AGRA to initiate a process in Malawi to ensure that smallholder farmers and MSMEs are integrated in these regional activities and developments.

Given the urgency and timeliness of the developments, AGRA and the GIZ KULIMA MIERA programme together with the Government of Malawi through the Ministry of Industry, Trade and Tourism (MoITT) partnered to kick-start a wider conversation by organising the workshop themed **“Strengthening Structured Trade in Malawi – Securing Sustainable Markets for Farmers”, with an initial focus on the role of commodity exchanges and the warehouse receipt system.**

Planned as a participatory workshop including more than 60-70 participants from government, research and development partners, smallholder farmers, key value chain actors as well as service providers (e.g. banks and commodity exchanges), the seminar examined structured markets, institutions and their value added, informed by expert key notes and empirical data. Specifically, participants at the conference discussed challenges and opportunities facing structured markets in Malawi and in the region and brainstormed opportunities to coherently strengthen the commodity exchanges and the warehouse receipt system.

Ideas for future interventions and collaboration will be further discussed by interested parties within Malawi in the near future. The outcomes of the workshop have also been presented at the African Green Revolution Forum (AGRF 2018) in Kigali at the Commodity Exchange Breakout Session and the Policy Symposium on Trade and Markets.

The event was attended by more than 80 stakeholders from private sector, banks, exchanges government, research, development partners, farmers and civil society organisations.

¹ DCAFS: Donor Committee for Agriculture and Food Security



2. Opening Speeches

2.1 Welcome Remarks by Regional Head for AGRA – Mr. Dyborn Chibonga

Mr. Chibonga started by acknowledging the strides that Malawi is making in enhancing productivity and the need for proper agricultural markets to propel productivity. He highlighted that,

‘Malawi has made significant strides in enhancing productivity which is growing although not at the pace that we all want. This emanates from the huge investments that all of us, led by government, are making towards the sector. However, while the production trends for major crops such as maize, rice, soya and groundnuts has been growing over the past year, the major concern for farmers is agricultural markets. Functioning agricultural markets, poses as a major hindrance to the growth of the sector among other challenges (NAP, 2016) as they continue to fail to inspire agricultural production and spur economic growth as farmers remain frustrated by poor marketing systems.

Despite the numerous marketing opportunities that exist within and across the region, studies show that,

- a) Dominant informal marketing system for most crops
- b) Poor implementation of market regulatory frameworks
- c) Lack of market information/information asymmetry and
- d) Disorganization of farmers ...

...are some of the major marketing blocks preventing our communities from realizing full rewards to cause the transformation we all would want to see in our country. A Study by the Legumes Development Trust revealed that there are weak linkages between our farmers, who are producers and foundations of our value chains, and major buyers, which is a big cause for worry, calling us all to this meeting this morning.’

In his speech, he appreciated all partners’ efforts in supporting linkages of farmers to markets, which has given birth to two commodity exchanges and Government enacting the Warehouse Receipt Act, which has not happened in many countries. However, he lamented reports that stakeholders cannot fully utilize the Commodity Exchanges 8 and 5 years since their establishment.

At the end, he encouraged participants to engage in an honest discussion to find lasting solutions to help farmers access better markets.

2.2 Welcome remarks by German Embassy / German Cooperation – Ms. Dagmar Krenz

Ms. Krenz welcomed all the guests and started by mentioning the fact that

‘compared to many other African countries Malawi has been at the fore front of developing structured trade services and institutions such as commodity exchanges and a warehouse receipt system.



We and many other development partners still believe that a commodity exchange as well as the warehouse receipt system can play an important role in increasing the access of smallholder farmers and micro, small and medium enterprises to better markets and prices as well as to key value chain services such as market information and warehousing that are otherwise lacking. However, so far these trade services and institutions have not come without their challenges and have not reached a stage of sustainability. We have to acknowledge that exchanges so far have failed to sustainably link farmers to their services such as the warehouse receipt system and to clearly show their potential economic.'

Ms Krenz stressed that this seminar was a great opportunity for all relevant stakeholder groups to discuss challenges and opportunities of structured markets focussing on commodity exchanges and the warehouse receipt system and to develop a joint vision for a way forward. These discussions were of utmost importance to inform interventions promoting the structured markets system in Malawi for the coming years.

'The German Government together with the EU has been supporting structured trade and markets for the last three years through their jointly funded KULIMA More Income and Employment in Rural Areas Programme (MIERA). In supporting structured markets, the Agricultural Commodity Exchange for Africa – ACE – has been a key partner for KULIMA MIERA. Our contribution has been taking a long-term approach of supporting ACE institutionally, most notably by supporting ACE to develop and implement its own 5-year organizational development strategy, the Rural Strategy 2020, that aims at sustainably and beneficially linking farmers and MSME to demand-driven services and ultimately better markets. This strategy is now being implemented and the first results are promising. After piloting the newly developed ACE Marketing School, uptake of services by smallholder farmers has increased significantly. At the same time ACE has been improving its services to be more demand-oriented and has overhauled its internal M&E systems to capture client satisfaction as well as the economic impact of its service offer.

We however also acknowledge that exchanges are still highly dependent on support and have not yet developed a viable business model, which puts their long-term development at a risk. With ACE we are therefore also working on a strategy to become a commercially viable entity with a clear-cut business model and a stringent vision of the role it should be playing in the wider ecosystem of structured markets and value chains.

Beyond that, there are a lot of challenges and questions remaining regarding the macro-economic climate as well as the policy and framework conditions for the emergence of a successful national and regional structured trading system that will bring Malawi forward. Next year a new legal and regulatory framework, the Warehouse Receipt Act and the Commodity Exchange Directive, will come into effect, further strengthening the sector but also putting additional pressure on its actors to become compliant.

The views on the value of structured markets systems are wide ranging. Some stakeholders even question the overall viability and developmental benefit of commodity exchanges as well as the warehouse receipt system, warning of the systems' imminent collapse and questioning the role the institutions are playing or are made to play (often by us the development partners) within



structured markets, warning of an over-stretch of their mandate. On the other hand support and interest, for instance by the development banks, but also by private sector actors and the government, remains high.'

Ms. Krenz ended her speech stating that she believed that a wider dialogue and constructive discussion among all involved stakeholders, on the future role of commodity exchanges and the warehouse receipt system and on how together we can ensure a coherent and harmonized approach to strengthening structured trade and markets in Malawi and the region can lead structured trading to a sustainable success.

2.3 Opening Speech by The Guest of Honour – Dr Joseph Mkandawire, Director of Administration and Finance, MoIT

The workshop was opened by Dr Joseph Mkandawire on behalf of the Principal Secretary for Ministry of Industry, Trade and Tourism. In his speech, he reiterated the Government's commitment to promoting structured markets in Malawi.

'As you are aware, the Malawi Government is committed to the welfare of our beloved farmers right from production up to where farmers sell their produce. Government has always created a conducive environment for the farming businesses to be competitive and sustainable as demonstrated through several policy reforms and programs that government is implementing. Among these policies and programs include the revision of the Control of Goods Act which was enacted two months ago, the Warehouse Receipt Act, the National Agriculture Policy just to mention a few.'

Dr Mkandawire highlighted some pragmatic policy reforms that put Malawi on the right path to Agricultural Commercialization and Transformation.

'The Government has a network of trade officers and agribusiness officers stationed in every district in this country to support farmers' access to profitable markets, which forms the bedrock of the theme for this workshop. Government realizes the critical role that markets have in the economic growth and development of this country. As a nation we heavily depend on agriculture and will continue to do so, hence the need to thoroughly reflect on how markets are working for our community.

Government is also aware of rent seeking and unscrupulous behaviour by some players on markets especially grain markets which indeed has a huge impact on the future of this important sector in the country's economic development.

As you may all be aware incomes of the majority of our country's population is heavily dependent on how markets perform. In addition, prevailing prices have a direct impact on subsequent production as farmers shift their production to alternative means.

It is against this background that the Ministry works in close collaboration with our colleagues in the Ministry of Agriculture, Irrigation and Water Development to regulate agricultural markets to encourage good agribusiness practice by all players on grain markets.'



Dr Mkandawire emphasized that better prices are very critical to economic empowerment of many farmers spread across this country. However, government also realizes that while farmers need better prices we need to make sure that we do not hamper our businesses that rely on grain commodities for raw materials.

He encouraged stakeholders to discuss the openly:

‘So as we all seek solutions on how we can strengthen structured trade and mitigate the impact of price fluctuations on the sector, let us discuss the issue with sober minds and come up with lasting solutions that will move the sector forward. I am aware of the thought provoking report that the African Institute for Corporate Citizenship compiled on challenges facing Commodity Exchanges in the country. As we discuss some of those issues raised in the report, I encourage you to brave the reality and identify solutions that will guide all of us for the betterment of our farmers that need better and lucrative market services.’

He ended his speech by once again reiterating government’s commitment to promoting structured trading and that as a Ministry they would be looking forward to the report from this workshop to guide next steps in planning the implementation of recently enacted regulations.

3. Keynote Presentation by Dr Bob Baulch (IFPRI)

Dr Bob Baulch, IFPRI Malawi’s Country Program Leader, gave the seminar’s keynote speech, which highlighted findings from IFPRI’s ongoing Commodity Exchange Landscape study. This study conducted semi-structured interviews with a range of key stakeholders – farmers associations and groups, small and large traders, processors and feed manufacturers, financial institutions, and food agencies to understand how to best to maximize the performance of the commodity exchanges and collateral financing back by warehouse receipts. The presentation underscored that commodity exchanges and warehouse receipts are only one component of a structured market, and that there is still considerable confusion among key stakeholders about what functions commodity exchanges can and cannot fulfil. Baulch also highlighted quick wins, medium-term policy recommendations, and some more controversial proposals for improving the functioning of the commodity exchanges and warehouse receipt system in Malawi:

Summary and Recommendations

- Like many other Africa Comexes, the volumes and turnover on Malawi two Comexes are low and volatile.
- Many farmers associations/larger traders/processors have an unrealistic desire to use the Comex as an aggregation mechanism.
- Some Food Agencies/DPs also have unrealistic desire to use the Comex to increase/stabilise prices received by farmers.
- Unrealistic for financial institutions to demand physical margin calls on WRS (haircut) financing.
- Systemic problems with collateral management and own account trading.
- Structured markets are NOT an answer to everything.



Quick wins for the commodity exchange would include the

- harmonisation of grading standards,
- delinking the promotion of warehouse receipts and haircut financing,
- To limit financial exposure, commercial banks should set 'strike prices' (triggers) for sale of stocks and establish term limits for collateral-based loans (whether backed by official WRS or other forms of receipts).

Medium and longer-term options include

- the rationalisation of ACE and AHCX operations to promote synergies and reduce overlaps,
- the establishment of an independent body to oversee the operations of the exchanges while representing the interests of key stakeholders in the industry,
- the use of Zambia's recently established maize and soya future contracts for hedging in Malawi,
- removal of withholding tax on food commodity transactions (currently only food transactions under MWK60,000 are exempt for withholding tax, which creates an incentive for many, very small transactions),
- establishing a single electronic warehouse receipt system for the entire country.
- ACE and AHCX should be merged into a single exchange.



(Bob Baulch (IFPRI) during his keynote; find the presentation in the Annex)

Questions and Remarks

Q: Regarding the statement indicating, “structured markets are not the answer to everything” would it be possible to indicate which issues they can answer and which issues they cannot answer?

A: The study was focused on commodity exchanges and warehouse receipts, not structured trading in general. As such the comment to say structured markets are not an answer to everything was in relation to the commodity exchanges and the warehouse receipt system.



Q: Grace Mhango (GTPA) - 550 farmers and traders were interviewed re their use of the commodity exchanges. Was there an effort to understand what they meant by use of “commodity exchange?”, because traders consider the commodity exchanges as a platform where they can access finances.

A: Most of farmers and traders do not understand the functions of commodity exchanges: they look at the comex as spot markets and ways to access collateral financing (via the warehouse receipt system) but do not understand comex operations as a whole.

Q: ADMARC was not recognized in the presentation, yet ADMARC is being mentioned in the presentation and the information being presented is not a true reflection of ADMARC. Why was ADMARC not consulted?

A: IFPRI contacted and tried to interview ADMARC several times, but could not manage to have a meeting with their CEO. The questionnaire was sent to the CEO but there was no feedback from ADMARC.

4. Panel Discussion

(summary of key speaking points made)

Panellists were encouraged by the facilitator to briefly present

- Their organisation’s respective role in the agricultural sector.
- Their role in strengthening structured trade/ markets.
- Their challenges, experiences and insights in regard to structured trade/ markets.

Kristian Moller (CEO of ACE)

(presentation and key points in the annex)



(Kristian Moller of ACE presenting facts and figures)



Betty Chinyamunyamu (CEO of NASFAM)

- NASFAM was established to further the interests and economic benefits of smallholder farmers to increase yields and enable them to access better and reliable markets.
- NASFAM had been talking of structured trade for a very long time, which led to the establishment of ACE.
- Farmers are critical in the Malawi agricultural value chains and commodity exchanges.
- If farmers are not utilizing the comexes and participating in structured trade then there is a problem as farmers constitute a significant proportion of producers in the agricultural VC.
- Challenges faced by farmers;
 - **Policy inconsistency:** Affects decision-making of both smallholder farmers and private sector. Market availability and prices are affected. This makes legumes and grains highly risky crops. Diversification efforts have also been affected as farmers run back to tobacco since there is some guarantee with tobacco with regard to markets and prospective prices.
 - **Growth and existence of the informal sector (especially legumes):** The vendors address the immediate needs of the smallholder farmers. Farmers need their cash instantly and vendors can provide this.
 - **Infrastructure challenges:** Make it hard for smallholder farmers to logistically organise their crop and produce. Farmers opt for informal markets as they are more easily accessible.
 - **Market risks:** farmers face a huge challenge when it comes to determining what to grow and satisfy a specific market as they are not sure of the outcomes of market demands.
 - **Coordination:** This is a challenge amongst projects. Different approaches aimed at achieving the same thing confuse farmers.
 - **Some farmers are still not organised:** Other institutions have gone further to develop their own organisations, i.e. other projects/ private companies set up their own farmer groups instead of working with existing structures.
 - **Trainings are often inadequate.** This has led to other farmers not adequately understanding the concept of structured trade. As such once farmers have failed to benefit from structured trade/commodity exchanges they decide not to be involved in structured trade again. If there was better awareness that markets can go both ways (good or bad) there wouldn't be such challenges.
- Farmers as business players are looking for
 - Reduced transaction costs.
 - Ease of doing business.
 - Reduced risk.
- If these are not addressed, then it is hard for them to move from the known to the unknown.
- **Access to information:** Quality standard and timely premium markets
- **Environmental issues and climate variations:** farmers are not very much informed regarding weather changes and rainfall patterns leading to poor preparations and low adoption to mitigation options



(Betty Chinyamunyamu during the panel discussion)

Robert Nazitwere (Finance Manager of Auction Holdings Commodity Exchange)

- AHCX as a commodity exchange provides a platform for trading. The platform offers assurance on quality, quantity and payment.
- WRS: traders deposit commodity in warehouse operators and issues with a receipt for access to finance.
- AHCX is a warehouse operator which also provides the following services:
 - Settlement;
 - Warehousing;
 - Trading of WRS;
 - Provision of WRS;
 - Grading;
 - Market information;

Challenges:

- **Infrastructure:** AHCX is operating 12 warehouses, but Malawi has 25 districts. Furthermore, most of these warehouses are shops rented from third parties. Thus, they are not tailor-made infrastructure. The weigh bridges & laboratory equipment necessary for grading are not available. There is a lack of certification space for quality assurance.
- **Quality:** The exchange puts emphasis on quality. There are 3 grades (1-3). In the informal sector there are no grades and one price is offered for any grade or any crop. Farmers do not understand the concept of grading and its relation to prices.
- **Prices:** Quality issues are not paid attention to. High costs associated with handling cash for payments at the point of commodity aggregation.
- **Demand for instant cash by farmers:** initially the exchange was trading and paying farmers on T+1 mode of payment (i.e., when a transaction occurs today, the payment is processed the next day). AHCX is looking at settlement cycle that occurs on the same day.
- **Information asymmetry:** commodity pricing and quality management are still not clear to many farmers, hence there is mixed information regarding commodity marketing and quality demands.
- **Land holding size for smallholder farmers:** The land holding size of the farmers is still limited, thus the land that can be allocated to a specific crop is very limited, and this results in very small



volumes available for trading. Farmers should be encouraged to participate in markets via cooperatives.

- **Need to accelerate uptake of WRS:** The system has not failed but there is a need to ensure that there is a high uptake.

Possible solutions to the challenges:

- Infrastructure development (Rural warehousing)
- Land holding size for production (Promotion of groupings for easy marketing of both inputs and commodity)

Bashir Sama (RAB Processors)

- RAB is an Agro based company- with major offices in LL, BT, Mzuzu and many other markets with KULIMA Gold outlets.
- The company procures locally grown commodities (grains and legumes from stallholder farmers) for processing (peanut butter, soy pieces), as well as traded locally and regionally.
- Link between RAB and smallholder farmers is strong. The 85 Kulima Gold rural outlets are also utilized to supply inputs. RAB supplies inputs and fertilizer to farmers.
- The company has been involved in WRS with ACE and AHCX. RAB is also running a project with USAID. This aims at ensuring small scale agro processing, aggregation, grading and WRS.
- As a company, RAB is excited in working with ACE and AHCX. There are challenges in getting information of the volumes and prices, but the exchanges offer more transparency and help in decision making.

Annie Mbabu (Director of Markets, AGRA)

- Agra is an NGO established in 2006 and is currently working in 11 African countries. Its aim is to promote a green revolution in Africa to ensure farmers increase production and income.
- **Key view:** markets drive investments; policy must be transparent, reliable and evidence based
- AGRA implements via partners national wide
- **Roles of AGRA in regards to WRS:**
 - Policy review to create a fair trade across borders or loans with banks;
 - Support to structured trade and markets.
- AGRA Focuses on market drive process that cultivates coordination and partnerships with government in ensuring that all the players can follow and develop an enabling environment that businesses can operate in.
- There is a need for predictive policies. Unpredictable policies are a challenge in other countries as well, for instance in Zambia and Kenya. Hence, there is a need for predictability. For instance, if government sets prices that are very high, there is no incentive to trade.
- The commodity exchanges have to also structure policies and guidelines that are reliable. They have to open up to banks for loan access.
- The comexes also have to work with the government to open borders.
- Partnerships that will help smallholder farmers have to be established with stakeholders.



- Implementation of policies is a challenge by African governments. There is need for more partnerships to ensure that policies are put into action (all hands on deck).

Gomezgani Kakhuta (FMB)

- **Primary role:** Offer finance to all value chain players – from production to consumption.
- Structured markets provide comfort for commitment to investment.
- In relation to structured trade, banks are willing to finance. This has been the case even prior to the WR bill.
- Research results and commitment of organisations are key to making proper decisions around financing VC players.
- The challenges facing the FOs in failing to produce a collateral when demanding loans from banks is hindering progress and development of the farmer organisations in investing in infrastructure like warehouses.
- Collapse of the markets in 2016 (pigeon peas market) has led to banks distancing themselves from the WRS.
- Predictability of policies and prices is the key issue. In this modern age, models that can aim at predicting prices need to be explored and give surety to farmers as well as banks.
- Coordination and enabling environment are key to banks for committing to investment and minimization of the risks.
- The other value chains (grains) can learn from the tobacco sector where one bank can finance MWK 50 million due to price predictability.
- In structured trade, FMB had 1 billion for farmers: 7% only benefited due to the issues of collateral.
- Transaction cost reduction has to be looked at. Inflation has gone down and the economy is more stable. Nonetheless, issues of risk have to be looked at. Banks are willing to reduce the transaction costs but there has to be assurance of reduction of risk from the CXs.
- Banks are willing. There is need for vertical integration and having all stakeholders in one place and moving together.

Comments from the audience

- **AICC:** The focus of the panel discussion has been mainly on the WRS which is a component of the structured trade. This limits the discussion to WRS, but WRS might not be the only solution to the problems in marketing. Thus, we need to broaden the discussion. If the WRS is the sole focus of the discussion, there is also need to look at options. **There is also a need to set and look at which parameters we can measure progress of structured trade on**, so that when we meet again we can check ourselves against the parameters. AICC suggested to host an M&E effort on this.

5. Group Discussions

Group 1: How to sustainably engage smallholder farmers in structured markets?

(facilitated by Andrés Mella, GIZ)



Challenges

- Capacity at the farmers organizational level to understand comexes´ and other business models of structured markets
- Lack of awareness about market opportunities (comex, WRS)
- Identification of the bestselling opportunity in the “market”
- Liquidity of farmers and strong preference of farmers for cashing out
- Fragmented commodity market – low productivity volumes and small plot sizes affect the business space where businesses operate
- Coordination among stakeholders is low with different priorities
- Trust between SHF and businesses participating in structured markets
- Regulations/ policy inconsistency, including government interventions on markets and prices in maize and pigeon peas.
- Logistics, rural infrastructure of comexes does not reach the far away rural areas because uptake of WH services is low
- Complex concepts (WRS, structured trade, comex) are hard to explain to SHF
- Price vs. quality → benefits of grading? SHF do not understand grading as this is different between comexes´ and are sometimes not explained why they are graded in a certain way. Premiums for higher quality many times do not compensate the extra effort.
- “bankability” of SHF (credit history, collateral) is low, thus limiting their access to finance
- Unclear “definition” of comexes (FI, market, marketing platform?)- there are similar organizations with different services and models which complicates the understanding of farmers

Quick Wins

- Generate evidence of benefits / profits and disseminate
- Awareness campaign and training (→ e.g. ACE Marketing School)
- Use champions to communicate benefits clearly
- Harmonise grading system between comexes and regional standards
- Address risks of clients and limit their losses through constant monitoring of

	<ul style="list-style-type: none"> prices Present all “options” available through structured markets with clear explanations on what services suit best each client’s situation Pilot different interventions
<p>Long-term solutions</p>	<ul style="list-style-type: none"> Capacity development of FOs so members feel represented by their management and operate as working organisations Find/ have guaranteed buyers or markets (before depositing?) Comexes find “market makers”, i.e. leading companies which establish long term agreements to supply from local markets Coordination and supervision could be done by an independent “body” which would coordinate activities/ awareness on comexes Use app/ ICT to walk through comex/ structured trade process as well as other marketing solutions Integrated policy framework, which would establish rights and obligations clear for all parties involved and a straightforward mechanism that would settle disputes in a timely manner. Incentive based contract system which offers a wider set of services to clients that fulfil their contractual obligations Forward contracts for SHFs/ FOs Linkage to long-term food programme which addresses food shortages and surpluses in the country

Group 2: Exchange sustainability and commercial viability

(facilitated by Dennis Ochieng (IFPRI) and Niall Haughey (ACE))



<p>Challenges</p>	<ul style="list-style-type: none"> Limited aggregation ⇔ low volumes Immediate/ spot payments demanded by farmers Informal market vibrancy Policy inconsistency (ad hoc, not sequenced well across seasons and successive years, and inadequate to address issues holistically without conflicts) Lacking market infrastructure Lack of professional management (at lower levels of commodity aggregation i.e. cooperatives: knowledgeable personnel on exchanges at the regulatory bodies , which
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	<p>triggered discussion about formation of CX control commission/committee)</p> <ul style="list-style-type: none"> ▪ Limited PS engagement ▪ High fixed costs ▪ Collateral management issues (WRS) ▪ Commitment to sustainability ▪ Thin markets ▪ Quality differentiation, value for quality: no premium for quality grains supplied to any of the markets and grading system are not standardised across the CEs. 'Quality' needs to be uniformly defined in both comexes and clearly communicated to suppliers.
Quick Wins	<ul style="list-style-type: none"> ▪ Formal trading <ul style="list-style-type: none"> ▪ Commodity exchange directive ▪ Introduction of export mandate for commodities to be strictly sold through the comexes, to learn from the ECX model ▪ Timely information to farmers ▪ Production increase (demand driven), focus on commercial production ▪ ACE to provide collateral management services (WRS) ▪ Diversification of commodities traded ▪ Conducive policy: Predictable policy environment and need for government to have models that predict market scenarios to aid in proper policy decisions.
Long-term solutions	<ul style="list-style-type: none"> ▪ Innovation to expand resource base ▪ Electronic warehouse receipt ▪ Balance between commercial and developmental objectives ▪ Independent commission to govern comexes ▪ Guaranteed market, contractual arrangement (forward contracts) ▪ infrastructural improvements to facilitate trade in general and access to markets i.e. roads, warehouses, weighbridges ▪ Policing informal sector to level playing field with comexes (competition) ▪ Incentivize "quality" produce

Group 3: Private sector and bank engagement

(facilitated by Justice Chimgonda (IFPRI) and Chikumbutso Mtwemwa (AgDiv)





<p>Challenges</p>	<ul style="list-style-type: none"> ▪ Capacity for exchanges to meet PS demand ▪ Mismatch on price expectation of depositors and buyers ▪ Risks associated with comex (financial risk, price unpredictability, policy unpredictability – e.g. export ban) ▪ Cost of finance (interest rates) and time to access finance are too high ▪ Withholding tax of 3% high, low margin crops (maize) → go through vendors/prefer cash sales ▪ High cost of exchanges' storage charges ▪ Lack of awareness of existence and products of comexes ▪ PS has invested in parallel vertical intervention which tries to fulfil the same functions ▪ Inability to secure volume ▪ Delay in provision of cash: When traders deposit commodities and sales take place there are instances where payments take long time to be effected thus delayed payments to the sellers. ▪ PS not buying through the exchange as it is more expensive than buying from the farmer ▪ Some offtakers not always interested in quality, just need bulk quantity ▪ Trust between financial institutions and private sector due to default rate ▪ Political interference and policy inconsistency (Export/Import bans) ▪ Unpredictability in prices
<p>Quick Wins</p>	<ul style="list-style-type: none"> ▪ Awareness on cost benefits to use comex as a trade platform: Traders are able to calculate profits easily when they use comex since they are able to know the charges before they make deposits. At the same time, the bulk sales ensure cost minimisations (scale of economy). ▪ Market information (on prices), transparency ▪ Easily available tool that calculates profits and costs from options ▪ Harmonised grades and standards ▪ PS buy in to WR services (e.g. cleaned and graded stock) → reduce deductions → service worth paying for. If the traders buy commodities through the comex, they are assured of good quality and the required quantities in accordance with the amount of money paid. ▪ Buyers get both good quality and quantities commensurate with money paid. ▪ Removal of withholding tax on food transaction over MWK 60,000
<p>Long-term solutions</p>	<ul style="list-style-type: none"> ▪ NFRA buying for the strategic reserves through comex. ▪ Comexes to diversify to other value chains other than cereal/ grains, e.g. horticulture



Group 4: Alternatives to commodity exchanges and the warehouse receipt system

(facilitated by Cuan Opperman and Towera Jalakasi (MOST))



<p>Which other models exist?</p>	<ul style="list-style-type: none"> ▪ Specialty contract farming- focussed on high value crops such as paprika. ▪ Incentive based contract farming system ▪ Direct purchase from farmers ▪ Value chain integration, ensuring that all market actors in the VC have access to finance in order to perform. ▪ In-grower contract system ▪ Aggregator approach (SME) ▪ Vertically integrated system – in which the off-taker/ processor includes production in their business model – e.g. the tea estates that produce their own tea but also bring in crop from outgrowers.
<p>Challenges</p>	<ul style="list-style-type: none"> ▪ Low production volumes – an insufficient volume moving through the system which leads to inefficiencies ▪ High cost of implementation of contract growing schemes ▪ High risk exposure, e.g. price volatility, interest rates high, crop failure ▪ Inadequate political will to ensure contract compliance ethics are adhered too. ▪ Competing programmes on market that potentially distort or disrupt contract farming arrangements. ▪ Lack of trust between producers and contractors as well as the other way round. ▪ Policy and regulatory environment- e.g. Withholding Tax mitigates against contract farming arrangements as the off taker needs to deduct this and the farmer has little or no way of recovering it. ▪ Low enforcement of policies
<p>Quick Wins</p>	<ul style="list-style-type: none"> ▪ Value chain financing ▪ Flexible pricing mechanisms ▪ A mechanism for price discovery → public sector role or through a private sector actor who charges for the service.
<p>Long-term solutions</p>	<ul style="list-style-type: none"> ▪ Export mandates – single channel exports? <ul style="list-style-type: none"> ▪ this could be problematic, as it would require exporters to relinquish their intellectual property (buyers contact details) and potentially be cut out of the trade. ▪ The other issue about export mandates is that, paradoxically, they may actually encourage informal, cross-border trade by traders who do not want to go through the exchanges. Also, if you follow through on the logic of the export mandates imposed by ECX, then if Malawi were to adopt export mandates the first 2 crops that should be mandated are tobacco and maize – in the interested of getting volumes traded on the exchange(s) up.



- Regionally linked markets
- More value addition in Malawi to utilise increased volumes.

Final comments after group presentations and key take-aways

- There is a need for coordination on reports and research.
- These recommendations raised should be taken seriously and put in practice.
- This is a good development and understanding of the issues that are being raised. WRS and structured trade are not a solution to everything. But the more options for farmers the better.
- The need to help smallholder farmers understand commodity exchanges, warehouse receipts systems, and structured markets more generally, and present them with a menu of viable options from which to choose.

6. Closing Remarks

6.1 Regional Head for AGRA – Mr. Dyborn Chibonga

On behalf of AGRA, GIZ and the Ministry of Industry, Trade and Tourism, Mr. Chibonga expressed his sincere gratitude to the participants for sparing their time to be part of this important Workshop. He noted

‘It is evident from the discussions that we have had here that market access in Malawi remains a huge challenge that we can no longer keep going around it thinking it will sort itself out someday. Our farmers need lucrative markets now to earn that important income which they can use to send their children to school, meet household needs and re-invest in their farming businesses. Our farmers need markets now to plan their next production. Government will be very critical in driving the recommendations that we have made together. As such it will be important to carry on our engagement with all of us involved. We have come up with several recommendations. We will sit down to synthesize the suggested solutions which should be able to guide our investments as stakeholders. And just to mention that the output from this meeting will feed into a Side Event at this year’s African Green Revolution Forum taking place in Kigali from 5th to 8th September.’

6.2 GIZ, KULIMA MIERA Team leader, Florian Bernhardt

Mr. Florian Bernhardt, team leader of the KULIMA MIERA programme, added that

‘this workshop has only been a starting point of a longer process. We see the need of more and closer stakeholder dialogue on the wide topic of structured markets. We are therefore ready to move the agenda forward with all the different stakeholders present. There needs to be a more regular dialogue on the future of the commodity exchanges, the warehouse receipt system and other relevant issues concerning the strengthening of structured markets in Malawi and the wider region and how this a common vision can be supported by the various actors with their respective capacities and mandates. On the topic of contract farming KULIMA MIERA is for example already engaging with the private sector and other stakeholders to design and implement a more coherent approach to the facilitation of such inclusive business models across private sector partners.’



6.3 EU Delegation, Joseph Bakkeren

The seminar was then officially closed by Joseph Bakkeren of the EU Delegation. He stated that

‘The EU is happy to note that structured trade and markets, and with that the potential of commodity exchanges, is increasingly gathering interest from many stakeholders in Malawi, one of the few countries in Africa where commodity exchanges are active. Issues around markets, trade and finance, in particular for the many smallholders are complex and cannot be solved by isolated interventions, but through collaborative and coordinated efforts by government, private sector including the financial institutions and farmer organisations as principal stakeholders. It is our hope that Malawi will further progress towards securing sustainable markets within and beyond its borders that respond in particular to the specific needs of its many smallholder farmers.’

7. Annex

- Presentation by Bob Baulch (IFPRI)
- Presentation by Kristian Moller (ACE)



MALAWI

COMMODITY EXCHANGE LANDSCAPE STUDY

Bob Baulch (IFPRI Malawi)

with inputs from Adam Gross (Southern Africa Trade and Investment Hub)

Chikumbutso Mtemwa (AgDiv) and

Justice Chingonda Nhkoma (IFPRI consultant)

Lilongwe, Malawi | 28 August 2018

Introduction and Scope of Work

- Study aims to understand:
 - the landscape in which Malawi's two agricultural commodity exchanges operate;
 - how best to maximize their performance and benefits to key stakeholders
- Malawi has not one, but two, commodity exchanges (Comex):
 - Agricultural Commodity Exchange (ACE) established in 2006
 - Auction Holdings Commodity Exchange (AHCX) established in 2013
- Malawi and Nigeria are the only countries in Africa with two Comex



Methods

- Interviews with 45 key market participants in May/June 2018 including:
 - ACE and AHCX
 - Farmers Associations and Groups in 11 districts
 - Traders (large and medium-scale)
 - Processors and feed manufacturers
 - Food agencies
- Analysis of secondary data (where available) from Malawi & other African Comex
- Questions on use of Comex added to IFPRI structure-conduct- performance study of maize marketing (June/July 2018)
- *Market analysis is ‘an art not a science’*

Lessons from International Experience (1)

North America and Europe

- Historically most Comex developed from forward contracts with negotiable warehouse receipts
- open outcry trading floors → electronic trading platforms



- Established Comex have market participants (brokers and ‘market makers’) who do not exist in most developing countries
- Derivatives trading (futures, options) forms the bulk of trade (physical deliveries on futures contracts is very rare)

Lessons from International Experience (2)

Latin America

- Like North America, Comex and WR developed in parallel
- Unlike North America, warehouses and WRS were Government-run

Transition and Developing Countries

- Have tried to develop comex based on spot (auction) markets.
- Many of these attempts have failed
- Most successful Comex have been in 'large' countries



Africa's Experience with Comex

- Only two well-established Comex in Africa:
 - South African Futures Exchange (SAFEX) – now part of the Johannesburg Stock Exchange
 - Ethiopian Commodity Exchange (ECX)
- SAFEX is the only derivatives-based exchange in Africa
- ECX is government established and promoted exchange, made financially viable by export mandates on coffee and sesame
- Most other African Comex are nascent or thinly-traded

Volume and Turnover on Selected African Comex

Exchange	Volume (MT) 2016	Volume (MT) 2017	Turnover (US\$ millions) 2016	Turnover (US\$ millions) 2017
SAFEX, S. Africa	130,700,000	128,600,000	68.1	40.8
ECX, Ethiopia	669,877	672,980	1,034	1,311
AFEX, Nigeria	47,780	28,377	15.1	12.4
EAX, Rwanda	15,000*			TBC
ACE, Malawi	60,232	16,373	24.6	3.8
AHCX, Malawi	48,756	3,622	17.5	TBC

Volumes (turnover) on the other 14 African commodity exchanges is collectively less than 150,000 MT (US\$ 52 million)

Sources: African Development Bank 2018; ACE, AFEX, AHCX, ECX, SAFEX

Note: * 2015

Alternatives to Commodity Exchanges

- Forward contracts through large commodity traders (Cargill, Continental, ETG, Farmers World) are commonly used by processors
 - And large traders can use future contracts on established Comex to hedge price risks
- Direct collateral financing of physical stocks is available from commercial banks for processors and large traders. Comex-backed WRS financing must compete with direct collateral financing.
- Vertically integrated supply chains (nucleus estate and contract farming) provide many of the benefits of Comex without the need for an exchange

Preconditions for Establishing a Comex

- Jayne et al. (2014) identify five of these:
 1. A pre-existing vibrant spot market;
 2. The potential to achieve sufficient volume traded across the exchange to cover its fixed costs;
 3. The presence of ancillary marketing services being offered which enable a commodity exchange to be instituted at relatively low cost;
 4. Modes of institutional governance and appropriate incentives sufficient to motivate rapid learning on the part of the Comex's management;
 5. A commitment from government to desist from unpredictable and discretionary forms of intervention in commodity markets.

Q. Were any of these conditions met in Malawi in 2006 or 2013?

A. Not really

Malawi's Commodity Exchange Landscape



- Established 2006
- Followed the traditional model: gradually diversifying from physical spot auctions, to an electronic bulletin board, to a WRS with certified warehouses, to forward contracts.
- ACE and ACE Trust are not-for-profit and have received substantial donor support

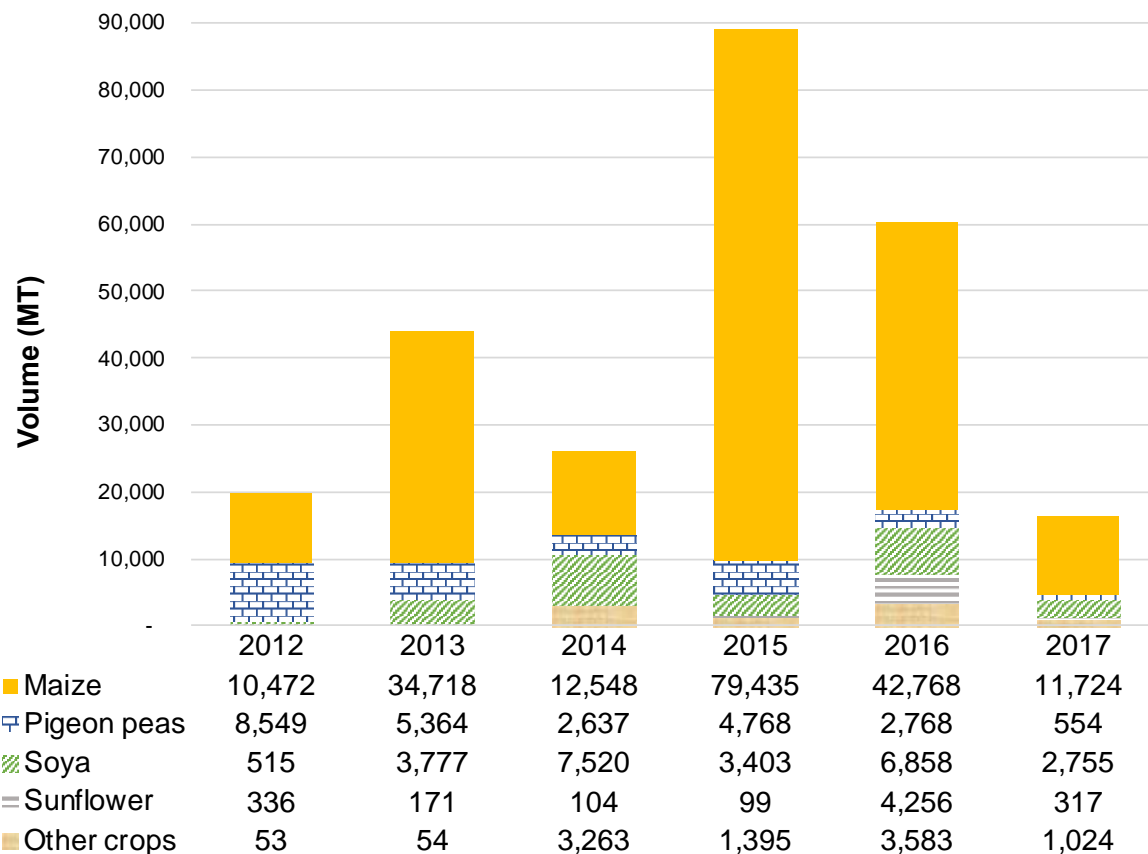


- Established 2013
- Followed an alternative model: investing heavily in e-trading infrastructure and exchange-owned warehouses followed by high profile launch
- ACHX is a 'fully commercial platform' owned by Auction Holding Ltd and enjoys considerable gov't support

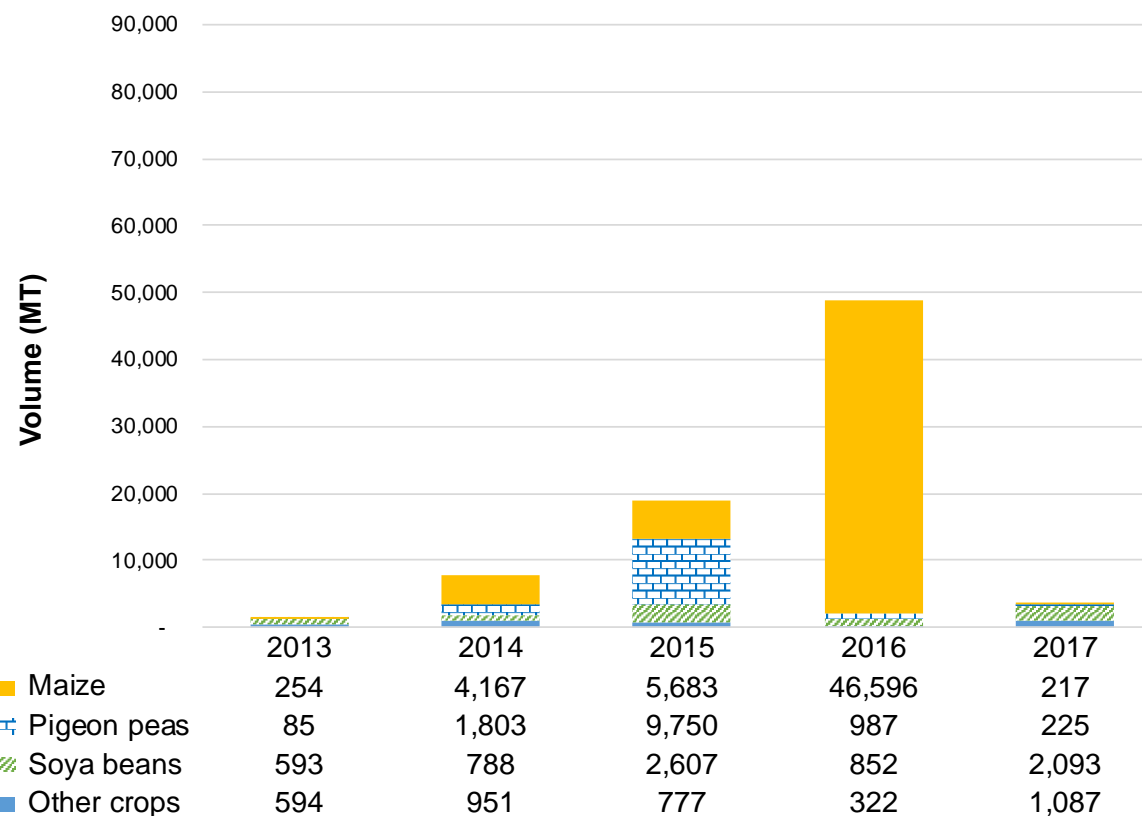
ACE and AHCX trade similar commodities and offer similar products (spot and forward contracts plus and WR financing) but have different geographical coverage

Volumes Traded on ACE and ACHX, by commodity and year

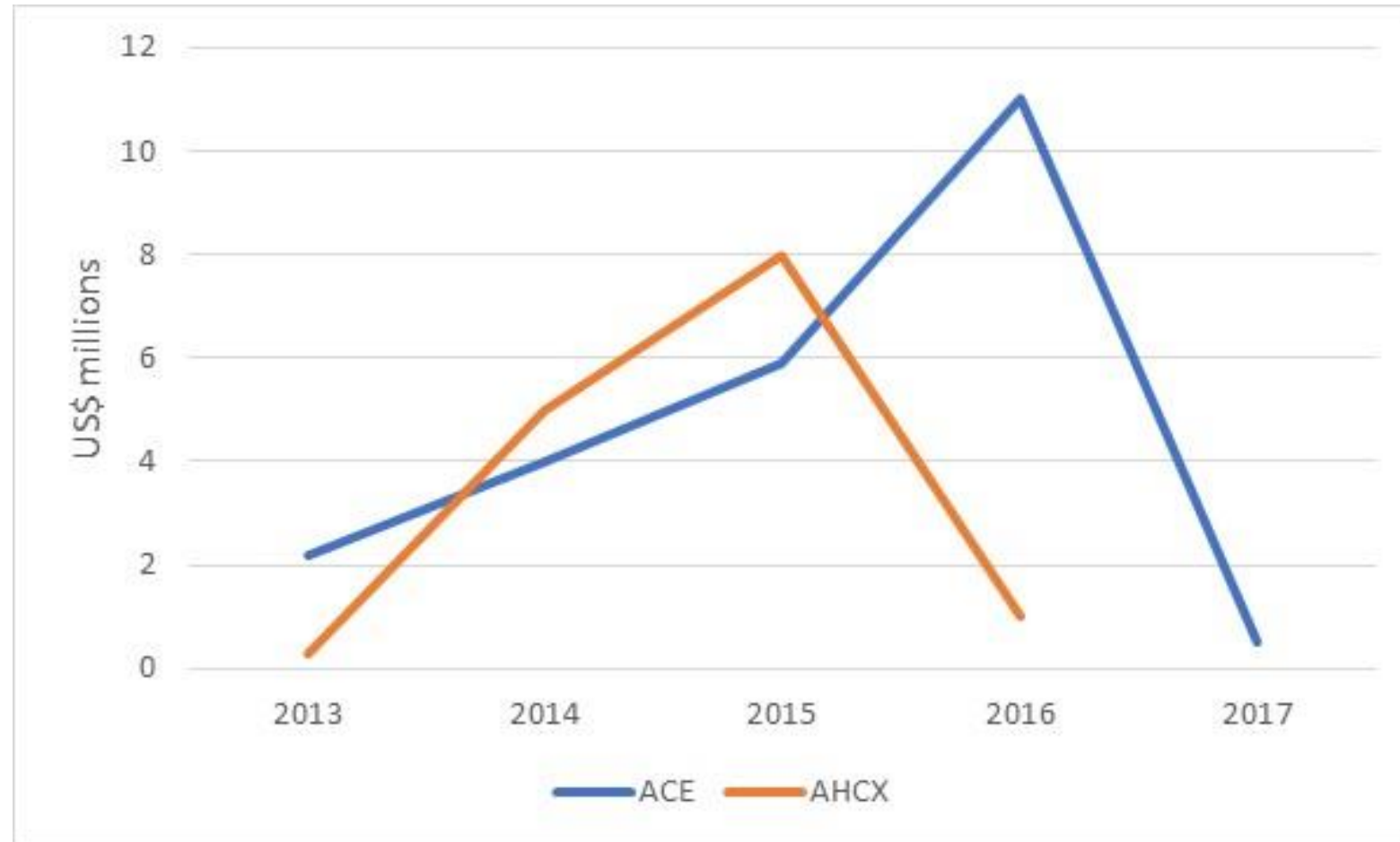
ACE



ACHX



Collateral Financing Advanced by ACE and AHCX



Perspectives of Farmers' Associations & Groups

- Trust in Comex's equipment (esp. scales) and expertise in commodity storage
- Link to financing via WRS valued
- However:
 - Strong preference for cash-based spot transactions
 - Costs regarded as high compared to spot sales to traders by 80% of farmers associations
 - Costs of handling and storage are not transparent
 - Collapsing prices in late 2016 have deterred many from using WRS again
 - Most farmers associations have only traded on Comex once or twice
 - A (politically) independent body is needed to regulate the Comex

Perspectives of Traders

- Two-thirds of small traders are unaware of the Comex
- Those that aware of them, generally do not sell to the Comex
- 'High' charges and fees, distance to warehouses, and grading issues (esp. for rice) deterred many small traders from using the comex
- Most small traders strongly prefer cash-based transactions
- Larger traders do use the Comex to supplement their established direct marketing channels
- Most large traders have their own warehouses but use WRS to obtain collateral financing or supplement their own warehouse capacity

Perspectives of Processors/Feed Manufacturers

- Frequent default on spot contracts on ACE and AHCX
- Forward contracts more reliable
- Contract farming and vertically-integration of supply chains offer alternative to Comex for securing supplies
- Processors with their own warehouses can obtain direct collateral financing more cheaply than through WRS, and therefore only use WR financing occasionally
- Comex registered warehouses also used to supplement processors own storage during peak procurement season
- Some processors like ACE's ability to structure forward contracts in accordance with Islamic banking principles

Perspectives of Financial Institutions

- Seven financial institutions (FI) have offered collateral-based financing via the Comex (mostly 'haircut' financing of WR) in the last five years
- Two FI have experienced substantial defaults on such loans, despite attempts of 'marking to market' with physical margin calls
- Direct collateral financing is also offered to large traders/processors by most commercial banks
- Comex backed WRS preferred to direct collateral financing by some banks, as no need for expensive collateral managers
- Warehouse Receipt Act of 2017 now provides legal framework for recovery of non-performing loans

Perspectives of Food Agencies

- Have used Comex periodically for procurement of supplies in ‘bad years’
- Procurement via Comex (usually BVOs) regarded as more transparent than direct procurement (by NFRA)
- BVO auctions have not performed as expected (by WFP), benefiting large traders and rarely reaching farmers associations
- Believe that Comex can help stabilize farmgate prices (this is dubious with current volumes/turnover!)
- Little use/appreciation of the value of forward contracts (let alone options on futures)

Legal framework

- When both ACE and AHCX were established, Malawi had no legal framework to govern their operations beyond general contract law.
 - Warehouse Receipt Act enacted in late 2017
 - RBM's Commodity Exchange Directive, approved 3 April 2018, will come into force on 3 April 2019
 - Corporate Governance Directive gives RBM the right to veto Comex board members
- Interviews with financial institutions and different market players, indicate that the provisions of the WR Act and Comex Directive are not widely understood
- Nonetheless the Act and Directive provide a solid legal basis for the development of Comex

Summary and Conclusions

- Like many other Africa Comex, the volumes and turnover on Malawi two Comex are low and volatile
- Many farmers associations/larger traders/processors have an unrealistic desire to use the Comex as an aggregation mechanism
- Some Food Agencies/DPs also have unrealistic desire to use the Comex to increase/stabilize prices received by farmers
- Unrealistic for financial institutions to demand physical margin calls on WRS (haircut) financing
- Systemic problems with collateral management and own account trading
- Comex (and WRS) are NOT the answer to everything

Recommendations: “quick wins”

- Harmonize ACE and AHCX’s grading systems
- Promote storage using WR to farmers’ associations/small traders without linking them so closely to collateral (‘haircut’) financing
- To limit financial exposure, commercial banks should set ‘strike prices’ (triggers) for sale of stocks and establish term limits for collateral-based loans (whether backed by official WRS or other forms of receipts)
- Promote collateral management as an alternative income stream for Comex to commissions and fees (Note: this requires indemnity (or fidelity) insurance.)
- Comex should strictly enforce regulations on own-account trading in Commodity Exchange Directive (by both themselves and their employees)

Recommendations: Medium-term + Some Controversial Proposals

Medium-term

- Rationalize ACE and AHCX operations to promote synergies and reduce overlaps
- Offer ZAMACE/JSE futures contracts on Comex in Malawi
- Establish an independent body to oversee the Comex, in addition to financial regulation by the Reserve Bank of Malawi

Some controversial proposals

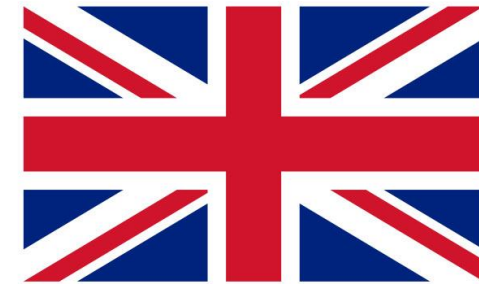
- Set-up a single WRS for Malawi
- Merge ACE and AHCX into a single exchange
- Remove withholding tax on food commodity transactions > MK60,000

Acknowledgements

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USAID
FROM THE AMERICAN PEOPLE



UKaid
from the British people

Data and Inputs:

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Some Key Terms

Auction: a process where potential buyers place competitive bids on assets or services

Basis: the difference between the spot price and the futures price of a commodity

Commodity Exchange: A legal entity that determines and enforces rules and procedures for the trading standardized commodity contracts and related investment products.

Derivative: a financial instrument, such as a futures or options contract, whose value is based upon a physical commodity (or on other financial instruments)

Collateral Manager: A company that ensures the integrity of warehouses and the quality of commodities held therein

Forward contract: A private, cash-market agreement between a buyer and seller for the future delivery of a commodity at an agreed price. (Unlike futures contracts, forward contracts are not standardized and not transferable.)

Future contract: a standardized contract for the purchase and sale of physical commodities (or financial instruments) for future delivery on a regulated commodity futures exchange.

Hedging: Taking a position in a futures market opposite to a position held in the cash market to minimize the risk of financial loss from an adverse price change

Marking-to-market: to debit or credit on a daily basis an account based on values the close of that day's trading session.

Options contract: a standardized contract that gives the bearer the right, but not the obligation, to buy or sell a futures contract at a specified price within a specified time period

Spot market: a market physical commodities are bought and sold for cash and delivered immediately

Warehouse receipt: a document which guarantees the quantity and quality of a commodity stored within an approved facility

Key References

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Total investment into ACE

USD 8.5 Million

Some perception that this investment is wasted since ACE is not commercially viable.

Warehouse Receipt System

USD 0.8 Million
Depositors

USD 0.4 Million
Storage Operators

USD 0.7 Million
Banks

USD 1.9 Million

Profit – Cash -



Risks – Price Volatility – Alternatives

Warehouse Receipt System

USD 1.7 Million

USD 300,000

Value of Rural
Warehouses Built –
Essential to gain upside
of WRS

Value of ACE investment
in electronic trade, MIS
and warehouse receipt
system.

Rural Warehouse Business Model slow
uptake – Operational sustainability hard
to reach

Warehouse Receipt System

USD 3 Million

Value of interest generated on warehouse receipts forward contracted to approved offtakers

USD 600,000

Value of ACE commissions generated in warehouse receipts and trade.

Demand for finance and bank appetite to provide finance is volatile and the environment changes every season. Hard to define the role of the exchange.

Chithumba -Access to input finance

USD 500,000

Value of yield increase
for Chithumba

USD 400,000

Value of input on
input finance

Chithumba clients still low up-take
for structured markets

Total investment into ACE

USD 8.5 Million

Tangible Added Value Generated

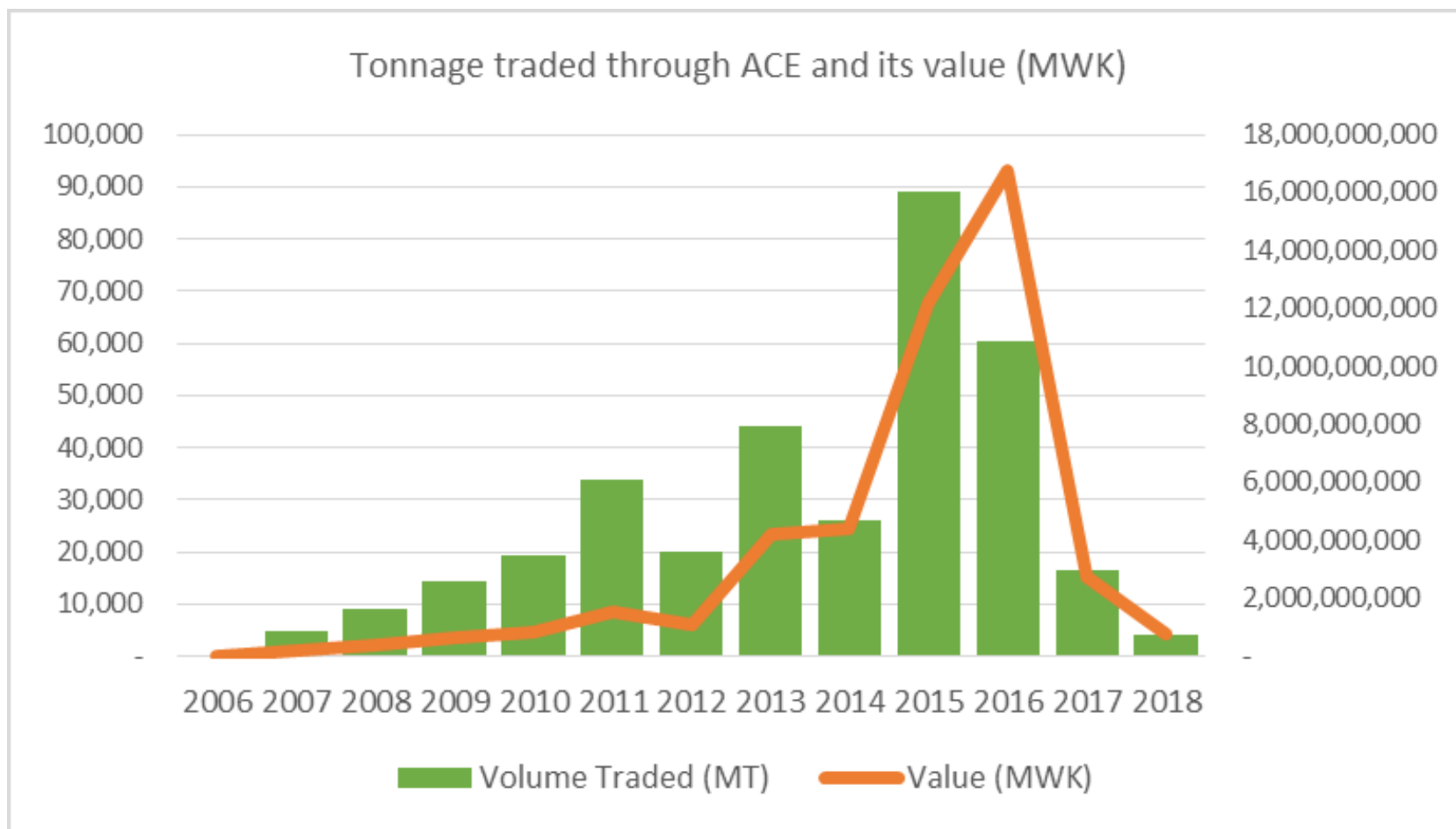
USD 8.4 Million

Intangible Value and Achievements

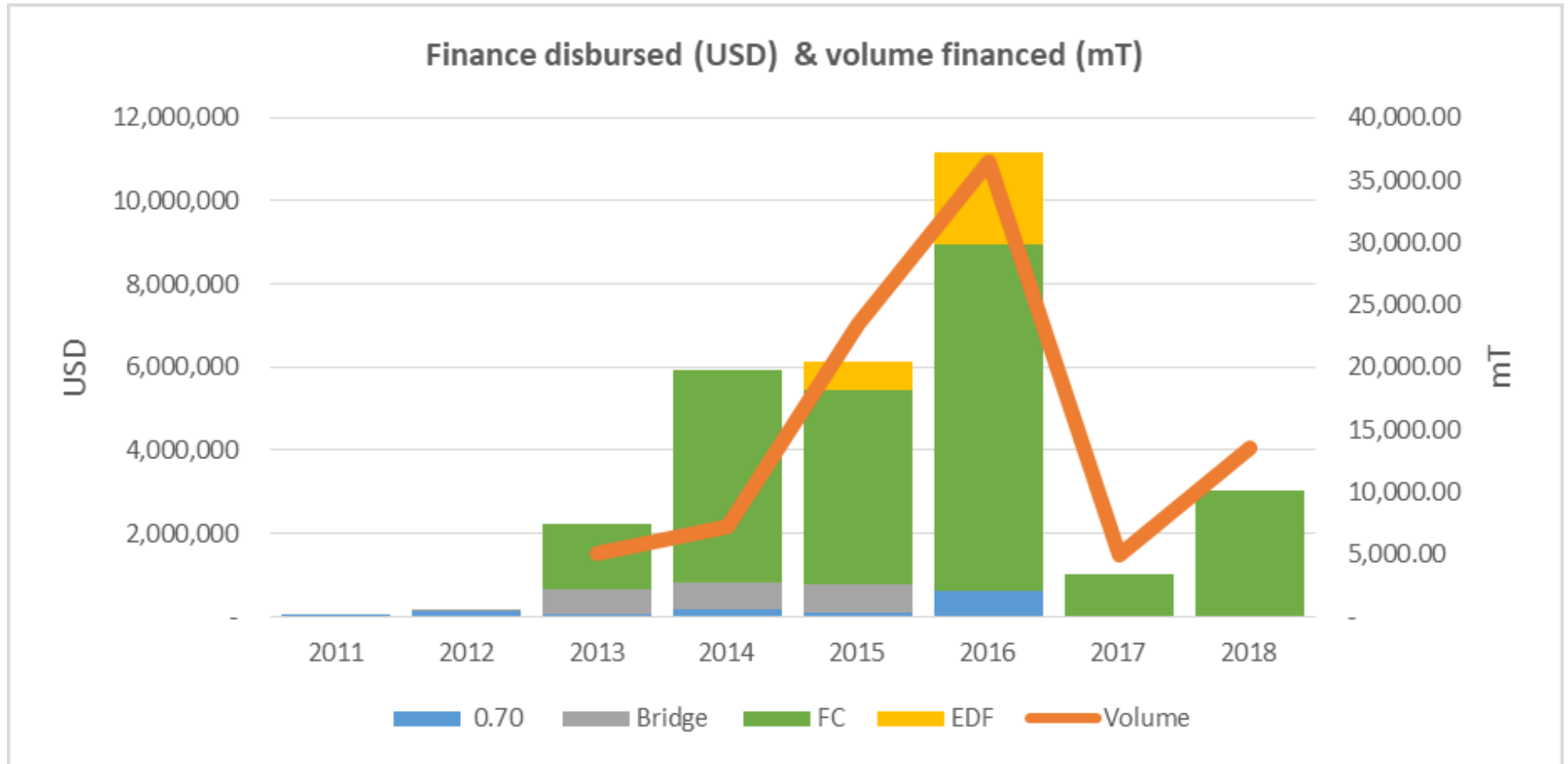
- Function operating WRS, MIS and Trade system
- 1370 receipts issued for 123.000 MT of commodity on WRS
- 2830 contract issued for 349.000 MT traded
- USD 29.7 million in finance disbursed
- 150.000 sensitized/trained in structured trade
- 98.000 profiled on MIS
- Regulatory Framework

We have an infrastructure

If its so good – why are we all here!



First signs of turning point!



So, what's next

- Structured trade was always an industry transformation – that is not achieved through a handful of projects
- Multiple partners coming together with a holistic and strategic approach.
- Enabling environment and trade policies are crucial
- The exchanges to (re)define their commercial role