'Smart subsidies'?

A critical review of the Malawi fertiliser subsidy programme

Initially hailed a huge success, Malawi's effort to boost agriculture with fertiliser subsidies appears to have met with failure. The author has a look at what went wrong, arguing that developments must be assessed against the backdrop of politics.

For several years since the 2005/06 growing season, Malawi hit the international headlines for pioneering the implementation of 'smart' subsidies which broke the vicious circle of chronic hunger and food shortage. For the first time in two decades, the country was able to feed itself without recourse to either food aid or commercial food imports.

Through the fertiliser subsidy programme, a smallholder farmer is given two bags of fertiliser, 50 kg each for basal and top dressing, 5 kg of hybrid seed and 2 kg of legumes. The smallholder farmers access these inputs through the use of vouchers which they redeem at designated marketing outlets. The programme targets at least half of the total farming families, estimated at three million. The subsidy programme earned the tag 'smart' because of the use of vouchers. The argument is that 'smartness' increases the likelihood of subsidy programmes avoiding the shortfalls that characterised the first-generation subsidies such as elite capture and political manipulation. Although the success of the subsidy programme has somewhat unravelled and there has been change of government following the death of President Mutharika in April 2012, the programme continues to be implemented.

An example to other countries in sub-Saharan Africa

In the inaugural season of implementing the subsidy programme, Malawi surpassed its annual food requirements, then estimated at 2.1 million tonnes, by 500,000 tonnes. This continued for six consecutive growing seasons, prompting the UN Secretary General, Ban Ki-moon, to remark that "Malawi has moved from hunger to feast in short years". The apparent success of the programme encouraged several sub-Saharan countries to consider a return to subsidies as a key strategy for revitalising their fledging agricultural sectors. In 2011, for instance, ten African countries spent roughly 1.05 billion US dollars (USD) on subsidy, amounting to 28.6 per cent of their public expenditures on agriculture.

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Ironically, the Malawi success story that triggered the subsidy frenzy across the continent is crumbling. This year alone, reports indicate that more than 1.63 million people, or eleven per cent of the population, are facing severe food shortages, and Malawi requires 30 million USD to meet the shortfall by the end of 2013. Consequently, the Head of the Comprehensive Africa Agriculture Development Programme (CAADP) was quoted as saying that "African agriculture needs strong local institutions to avoid the kind of bubble that we saw in Malawi which was largely driven by external energy".

There can be no better time than this to take a critical look at the Malawi fertiliser subsidy programme. It became a regular feature in critical international agricultural policy debates but has now given way to pessimism regarding the potential of 'smart subsidies' to avoid the ills of the first-generation subsidies.

The historical background

The history behind the subsidy programme is quite important. It arose out of democratic consensus of the nation. Following two devastating hunger episodes in quick succession since the turn of the new millennium, there was strong agreement across the political divide in the country that the implementation of a fertiliser subsidy was the only feasible strategy to get Malawi agriculture moving again. The use of vouchers promoted targeting of beneficiaries who could not genuinely afford to procure inputs on their own. Since poverty in Malawi is deep, widespread and severe, targeting the subsidy programme fairly efficiently and effectively greatly contributed to breaking the low maize productivity trap which makes the cultivation of maize in Malawi less profitable.

The low maize productivity trap prevails because nearly everyone grows maize even though many cannot access productivity-enhancing inputs, while those who can are constrained to invest more in the production of maize because of great variability in inter-year maize prices, making it a highly risky undertaking. The subsidy programme enhanced the prospects of the majority of Malawians breaking free from this trap by accessing inputs they could not otherwise have afforded.

Compared to most programmes that have since sprouted across the continent, the benefits of the subsidy programme were broad-based. Its early years were underlined by a willingness to learn and innovate. When, for example, the programme was threatened with elite capture, open community targeting was introduced to enhance transparency and accountability in the selection of beneficiaries. This was supported by a vibrant Logistics Unit in the Ministry that planned all aspects of the programme with a great deal of prudence and integrity.

The use of vouchers has contributed to the progressive expansion of private-sector involvement in the agricultural sector. For example, agro-dealers operating in the seed sector have ensured that farmers can access high-quality seeds almost at their doorstep. Prior to the launch of the programme, farmers had to travel long distances to procure seed, hence most of them ended up using local seed or recycling hybrid seed. Since the 2005/06 growing season, when the programme was introduced, the uptake of hybrid seed has improved from 43 to about 70 per cent.

Overall, the success of the programme endowed the nation with a sense of pride and dignity. For a while, Malawi could not beg for food. It was self-sufficient, and once even donated maize to Swaziland and Lesotho. This was further buttressed by the fact that the programme brought Malawi into the limelight as a pacesetter for a uniquely African Green Revolution.

What about sustainability?

With the benefit of hindsight, it is now possible to understand why the fertiliser subsidy programme was at first successful, but why this could not be sustained. The nature of politics in the initial years played a critical role and could therefore offer some useful lessons for countries that have already adopted subsidies or desire to.

The success of the subsidy programme in the initial years could principally be attributed to the political insecurity that the late President Mutharika faced during his first term of office. He had fallen out of favour with the party that sponsored his election as President and proceeded to form a new party that did not have any parliamentary representation.

It was difficult, if not impossible, for Mutharika to push any meaningful legislative agenda in an opposition-dominated Parliament. It is against this backdrop that he seized the fertiliser subsidy programme to build up political support outside Parliament, taking advantage of the fact that food security lies at the heart of Malawi's political economy. It virtually forms the basis for a social contract between citizens and government since maize can be said to be a national crop as it is grown by over 90 per cent of the households in the country.

The apparent collapse of the subsidy programme coincided with historic landslide victories for Mutharika and his party in the May 2009 polls. This was widely construed as his reward for ensuring food security through the fertiliser subsidy programme. The main question for Malawian voters is whether a government is able to enable them to have food on the table either through subsidised production or at market prices they can afford. The unprecedented electoral victory ironically altered the government's incentives for performance as far as the fertiliser subsidy programme was concerned. It quickly degenerated into a vehicle for dispensing rents, especially to those who had reportedly bankrolled the May 2009 electoral campaign. This has greatly contributed to undermining the continued success of the fertiliser subsidy programme.

In particular, according to a 2011 joint World Bank and Government of Malawi review, the major beneficiaries include Mulli Brothers and Simama General Dealers, who were very close allies of the governing party. These companies were given far larger fertiliser import contract volumes than they could manage and at prices almost double those of the most competitive bidders. These two companies further monopolised the distribution of the fertiliser at inflated prices, too. They were Malawian Kwacha (MK) 30–34/10 km, while the comparable rate for the private sector was MK 22/10 km, which greatly undermined the cost efficiency and effectiveness of the subsidy programme.

The Malawi case demonstrates that the nature of prevailing political incentives matters a great deal in determining whether subsidy initiatives succeed or fail. Thus no matter what the technical arguments for or against particular policy positions are, it is ultimately the configuration of political interests that determine policy outcomes on the ground.

The success of the Malawi fertiliser subsidy programme in the initial years was a direct result of the alignment of the political and technocratic incentives. The major challenge, however, is to discern these opportune moments, which appear to be associated with political fragility and insecurity of incumbent elites.