



Malawi Policy Brief No. 2

Small and medium forest enterprises can reduce poverty

1. The importance of small and medium forest enterprises

1.1 Introduction

Almost 65% of Malawians live below the poverty line (Government of Malawi, 2002a). Some 86% of Malawi's poor live in rural areas (NSO 1998). To move beyond subsistence agriculture in such rural areas, enterprises based on natural resources are amongst the only options for income generation. Few other alternatives exist.

Significant policy attention has been paid to strengthening small agricultural enterprises – for example in the Malawi Poverty Reduction Strategy Paper (PRSP - Government of Malawi, 2002a). The subsequent Malawi Growth and Development Strategy (MDGS) also recognises the role of the forest sector in 'Theme One – Sustainable Economic Growth'. But it still places forestry under the 'Sub-theme four - Conserving the natural resource base' – with an aim of reducing environmental degradation. It omits forestry from 'Sub-theme one – Maximising the contribution to economic growth through the potential sectors of growth' (Government of Malawi, 2006).

We argue below that the conception of forestry as a resource conservation issue is fundamentally misplaced. Forestry has the potential to be a driver of economic growth – especially in the poor rural areas. Policy implementation and staff capacity within the Department of Forestry need to be reshaped. In line with the MDGS the Department needs to catalyse the creation and growth of sustainable small forest enterprises – not merely to police unsustainable practice. Indeed, forest conservation is almost impossible unless local

people obtain financial benefit from the standing forest. To use the maxim of a leading forest enterprise specialist – 'The forest stays if the forest pays!' (Gretzinger, 2006)

1.2 Internationally, small and medium forest enterprises are centre stage

At a global level, the area of community ownership or management now accounts for 25% of the forest area in developing countries. This figure has doubled over the last 15 years and is set to double again over the next 15 years (White and Martin, 2002). This global reality is echoed by the Malawian strategy of decentralisation of forestry towards greater local control.

If a broad definition of small and medium forest enterprises (SMFEs) is used – including both community forest enterprises and those not strictly owned and managed under a 'community' banner – rough extrapolations from existing information suggest the following (Mayers, 2006a):

- About 80-90% of forestry enterprises are SMFEs in many countries.
- Over 50% of all forest sector employment is in SMFEs in many countries.
- Over 20 million people are employed by SMFEs worldwide – but an estimated further 140 million are also employed by informal forest enterprises.
- Over US \$130 billion/year of gross value added is produced by SMFEs worldwide.

In favourable policy contexts, SMFEs help to secure basic needs, accrue wealth locally, empower local creativity, strengthen local environmental accountability, and preserve cultural identity/niche markets (Macqueen, 2006).

The potential for greater investment in, and returns from, SMFEs and community forest enterprises is great – and is widely considered a better option for poverty reduction than industrial forestry (see Mayers, 2006b).

But SMFEs are often perceived as amateurish – in the wrong location, producing the wrong products badly and with ugly packaging! (Macqueen 2006a) Lack of management capacity may lead to resource depletion. This is particularly true of ‘distress diversification’ where SMFEs without adequate technology and skill become options of last resort – often without long-term prospects (Arnold, 2006).

Many SMFEs operate outside the formal economy altogether – often because of over-regulation – perhaps the greatest single constraint to forest enterprise development (Kaimowitz, 2006).

Despite these difficulties, many SMFEs attempt to improve the viability, sustainability, and social impact of their operations. In many cases, they group together in associations or alliances to secure resources and cut costs, make strategic alliances, and shape policy. For example, more than 3,000 forest-based associations were recorded in Uganda alone (Kazoora et al. 2006) Enlightened external support from service providers and consumer groups can help to foster responsible business practice through such associations and alliances (Macqueen et al., 2006b).

Beginning in 2006, a host of international conferences and forest investment forums have put SMFEs and their associations firmly centre stage in policy initiatives aimed at poverty reduction. The international community considers small and medium forest enterprises to be pivotal for poverty reduction.

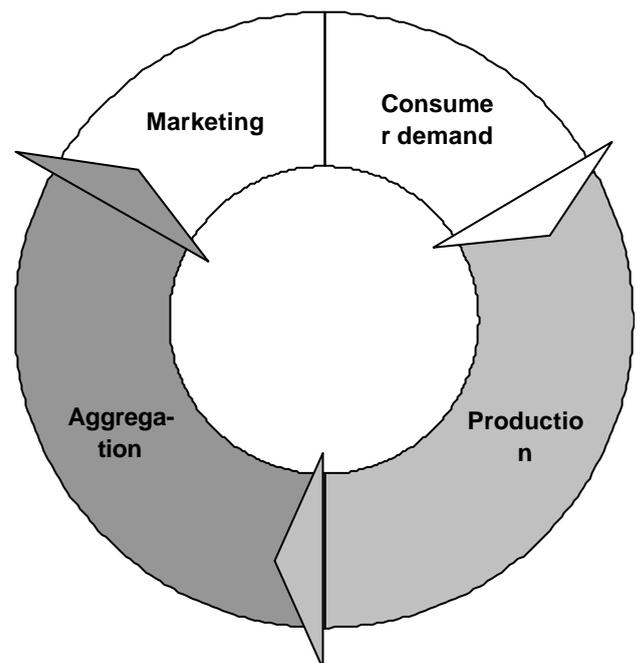
1.3 Experience exists of how to move from subsistence to business models

Decades of small enterprise development work has resulted in a good deal of clarity about what it takes to move from subsistence to business models. A central need is for capacity

development in business planning. The occasional sale of agricultural or forest surplus at the mercy of fickle markets must be replaced by careful planning in four main areas:

- Consumer demand (market intelligence) – Who wants what in terms of product quantity, quality and time – and how is this likely to change in the future bearing in mind likely competitors?
- Production – What resource access and production or procurement is needed and by whom in order to meet consumer demand in a way that is sustainable?
- Aggregation (processing and stock control) – What staffing, financial investment, technology, cash flow analysis and paper work is needed to ensure that legal obligations, customer information requirements, financial terms and product quality obligations are met?
- Marketing – What product quality, packaging, labelling, advertising and delivery (i.e. brand reputation) needs to be developed to distinguish a product or service from that of its competitors and win business?

Figure 1. Essential planning elements to move from subsistence to business models.



Source: Macqueen (2007)

A critical ingredient in developing business capacity is for local entrepreneurs to form associations around particular products – enabling one or two talented individuals to specialise in consumer relations, technical aspects of production, financial and business management, and marketing.

If forest policies are to support emerging SMFEs, they must not only support such emerging associations, but also recognise and address each of these essential planning elements that make up a 'business'. In other words, to support SMFEs, forest policies must go beyond 'production' concerns such as resource allocation and sustainable management. They must also address issues such as: the availability of forest credit and loan guarantees; the simplification of business registration, licensing, and transport permits; the establishment of marketing councils for forest products; the development of databases and communication systems to spread market information etc.

The analysis of the forest policy context in Malawi below shows that there is much work still to be done. The limited focus on resource access and management has sidelined practical initiatives to foster economic growth in the sector.

2. The Malawian context for small and medium forest enterprises

2.1 Growing awareness of the importance of small forest enterprises in Malawi

In 2000, the Gemini Baseline Study explored the extent of Micro, Small and Medium Enterprises within Malawi (ECI and NSO, 2000). It estimated the total number of such enterprises to be 747,363, 91% of which had 0-4 employees and 83% of which were located in rural areas. Approximately 75% of these enterprises were engaged in off-farm activities to do with manufacturing, trade and services – with only 22% in primary crop production and 3% in primary production of livestock, fishing, forestry and mining. In 2002, there were 10,407 forestry MSMEs recorded (linked to timber and firewood, but not charcoal or NTFPs). The potential for forest enterprises has been largely untapped and is likely to lie in value-added processing, trade and retail – not sustainable forest management.

Within the forest sector there are a number of functioning value chains and many successful examples of enterprises that are adding value to raw materials (Lowore, 2001). Examples of successful SMFEs include seedling production, carpentry, carving, cane furniture, brick making, paper, honey, beeswax, mushrooms, tree oils (for cooking, cosmetics and biofuel), fruit jams and juices, medicinal plants, butterfly farming etc. There are over 314 traditional-use plant products in Malawi – many forest-based – and some of them may have significant commercial potential (Greenburg and Irwin, 2005).

Most important of all is the thriving but currently informal charcoal trade. Preliminary findings from a recent study, carried out by FGLG, suggest that this is worth an estimated 4.2 billion Kwacha (approx. US \$30 million) per year. If this figure is correct, the charcoal trade is nearly as large as the tea or sugar industries.

These small enterprises not only produce and market products locally. There are also some examples of emerging business/community partnerships that may expand markets and help to build business capacity at the community level. Alliances between Maldeco, Shoprite and other private sector players and smallholders, a honey and beeswax smallholder commercialisation programme, and smallholder/producer group enterprise links with wild mushroom exporters are some examples of business/community collaboration with good potential (Sherchand, 2006).

2.2 The policy environment for small and medium forest enterprises

In the 2002 Malawi PRSP, there was a section on pro-poor growth. Natural resource use and forestry received specific mention with the intention to "encourage natural resource based enterprises (including value-adding activities) for generation of more income in rural areas" (Government of Malawi, 2002a). In addition, the PRSP devoted an entire section to support for Micro, Small and Medium Enterprises (MSMEs). It was noted that "with more emphasis on domestic MSMEs" the "following industry cluster groups are earmarked for active development... resource based industries (wood and wood products, gemstones handicrafts)". The intentions of the PRSP were prompted in 1999 by a Micro and Small Enterprise Policy of the Ministry of Industry, Trade and Private Sector Development (Government of Malawi, 1999)

subsequently developed into a MSME strategy in 2002. Yet, the evaluation of the impact of the PRSP noted that a major shortfall that hampered poverty reduction between 2002 and 2005 was the failure by the Ministries and Departments to translate such activities into their budgets (Government of Malawi, 2006)

As a result of these shortfalls, the Malawi Growth and Development Strategy (MGDS) again puts sustainable economic growth as its priority theme, with additional emphasis on social protection and disaster risk management, social development, infrastructure development and improving governance. The primary emphasis under good governance is: "Achieving and sustaining macro-economic growth". The Department of Forestry is not exempt from this emphasis. The first key strategy for forestry under the theme of sustainable economic growth is: "improving productivity and value added by the industrial forestry sector, while balancing it with sustainable practices". The emphasis on economic growth is unmistakable – even if stated under a theme of conserving the natural resource base.

The National Forest Policy and Forest Act provide opportunities for communities to gain full rights to forests on customary lands and limited costs and benefits arising from State Forest Reserves (Government of Malawi, 1996; 1997). These are important, but not sufficient, preconditions for enterprise development.

On customary land – as defined in the Malawi National Land Policy (Government of Malawi, 2002b) – certain forest functions and licensing have been devolved to District Assemblies and local forest organisations / Village Natural Resource Management Committees (VNRMCs). For example, trade of non-timber products, domestic use (not trade) of indigenous timber, and trade of indigenous or exotic planted timber no longer needs a licence from Government. Instead, it requires only a permit from the local management organisation or VNRMC and a conveyance certificate from the District Forest Office (Government of Malawi, 2007).

For commercial trade in indigenous timber a licence is required from the District Forest Office on behalf of the Director of Forestry – unless forming part of a management agreement entered into by the local forest organisation / VNRMC. To move such timber, a conveyance certificate is needed from the District Forest

Office. For processing and or export of indigenous wood, permits are required from the Director of Forestry (Government of Malawi, 2007).

If implemented in the field, these policy provisions would provide a good start for enterprise development in line with the MDGS. But there are still a number of constraints beyond legal resource access that the Department of Forestry needs to address.

2.3 The main constraints to small and medium forest enterprise development in Malawi

Despite the improving policy environment for SMFEs and developing entrepreneurship across a number of different product types, there remain a substantial number of challenges to enterprise development in Malawi (see Magai and Nthambi, 2002). Recently commissioned studies have assessed the main constraints to enterprise development for products such as honey and mushroom production (Sherchand, 2006).

A summary of the key constraints to forest enterprise development include:

- poor implementation of resource ownership and access rights,
- weak or non-existent organisation into associations to overcome scale and cost inefficiencies,
- lack of affordable finance, often due to financier concerns over risk of funding unsustainable forest activities,
- poor market information for forest products,
- lack of technological know-how, variable product quality and lack of quality grading,
- geographical isolation and poor infrastructure,
- lack of practical administrative and business experience.

3. Forest enterprise initiatives in Malawi

Within Malawi there are many initiatives that can help to address these constraints and build a thriving SMFE sector. A few examples of the bigger programmes are listed below:

3.1 Improved Forest Management for Sustainable Livelihoods Programme (IFMSLP)

This Programme - funded by the EU and the Government of Malawi - aims to improve household security through more sustainable management of natural resources. Communities are being empowered to take control of forests (both in Forest Reserves and on customary land) and to become involved in sustainable forest management and utilisation.

A key Programme strategy for improving the livelihoods of forest-dependent communities is to support forest-based enterprise development. This support, which follows a detailed livelihoods analysis undertaken at village level, is offered in various ways, such as promoting a savings-based microfinance model known as Village Savings and Loans. In this model, self-selecting groups meet regularly to pool their money, and members can take loans from the principal and repay it with interest based upon the agreed group constitution. Other support includes identifying and screening potential income-generating opportunities by promoting market-based entrepreneur values and systems; and by innovative capacity building through learning-by-doing, networking and exchanging information at all levels.

3.2 Community Partnerships for Sustainable Resource Management in Malawi (COMPASS II)

Funded by USAID, the principal objectives of COMPASS II are to support the Government to implement its policy and legislative framework for community management of natural resources, to build the local-level skills necessary to engage in better management, and especially to increase household incomes from sustainable natural resource use. The COMPASS II strategy for achieving small-scale commercialization of natural resource based products includes:

- focusing on marketable products – those which have demonstrated demand domestically and regionally, have the potential to achieve scale of impact by involving hundreds or thousands of households in the value chains, have a direct link between profitable enterprise and positive incentives for improved natural resource stewardship, and do not exclude marginalized households such as those which are HIV-affected or headed by women;
- marrying economic growth with conservation in key priority ecosystems – investing in natural capital assets where they occur; and
- encouraging sound business models – including organizing producer groups and linking them to markets, developing and disseminating high-quality technical information packages, brokering access to commercial finance mechanisms, and developing and implementing procedures for licensing and regulating natural resource harvests. (Johnson, pers.comm.)

3.3 Other national enterprise initiatives of relevance to SMFEs

Beyond the sustainable forest management emphasis of the Department of Forestry and the major programmes described above, various initiatives outside the forestry sector could also provide critical support to SMFEs. A few examples include:

- Micro-finance programmes for small enterprise include the Malawi Rural Finance Company (MRFC), the Foundation for International Community Assistance (FINCA), the Finance Trust for the Self-Employed (FITSE), Concern Universal Finance Organisation (CUMO) and Pride Malawi. In addition the National Bank of Malawi, the NBS Bank, and the Opportunity International Bank of Malawi (OIBM) all provide micro-finance services to the natural resources enterprise sector.
- The One Village One Product (OVOP) programme supported by JICA in the Ministry of Local Government and Rural Development provides training in business development, marketing support and finance for technology and infrastructure. Support has already been given to groups producing carpentry

products, tree seed oils, honey, mushrooms, paper cards and packaging (OVOP, 2006).

- The Malawi Agriculture Commodity Exchange (MACE) provides price information on a range of commodities through printed lists of bids and summaries, a short message service using mobile phones and a weekly radio programme. MACE also runs a transport service for small enterprises (MACE, 2007).

In addition to these national initiatives there are numerous local projects with enterprise components – often run by Non-Government Organisations (NGOs).

Despite these initiatives, Foan et al (2006) conclude that there is no sustained delivery of business services to enterprises such as honey producers in the rural areas of Malawi. They go on to note that while historic donor-sponsored technical training and limited business training in these rural areas have been given, interventions have been typically one-off and only provided at the start-up of a particular donor-sponsored project.

4. Urgent priorities for action by the Department of Forestry

In the light of the main constraints identified above, and the substantial gaps in forest enterprise support within Malawi we make a number of recommendations. Four priority actions by the Forestry Department are needed:

- *Install a small forest enterprise unit and strategy within the Department of Forestry.* It is meaningless to pursue the MDGS strategy for sustainable economic growth without such institutional reorganisation.
- *Make the formation of enterprise associations easy and fair:* in Malawi formal registration of association is still overly bureaucratic and centralised.
- *Subsidise information, training and association networks:* for example investing further in the many useful initiatives listed above. Finding ways to ‘connect’ potential forest entrepreneurs with these services is a critical issue.

Supporting more regular Forest Enterprise Fairs, workshops, seminars etc. could be very useful.

- *Develop market mechanisms that distinguish and reward community forest products in the market:* market access is a perennial problem for local forest-based associations. Creating mechanisms that allow SMFEs to distinguish their products and get better prices for them is a central issue – for example, developing a ‘Proudly Malawian’ initiative.

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