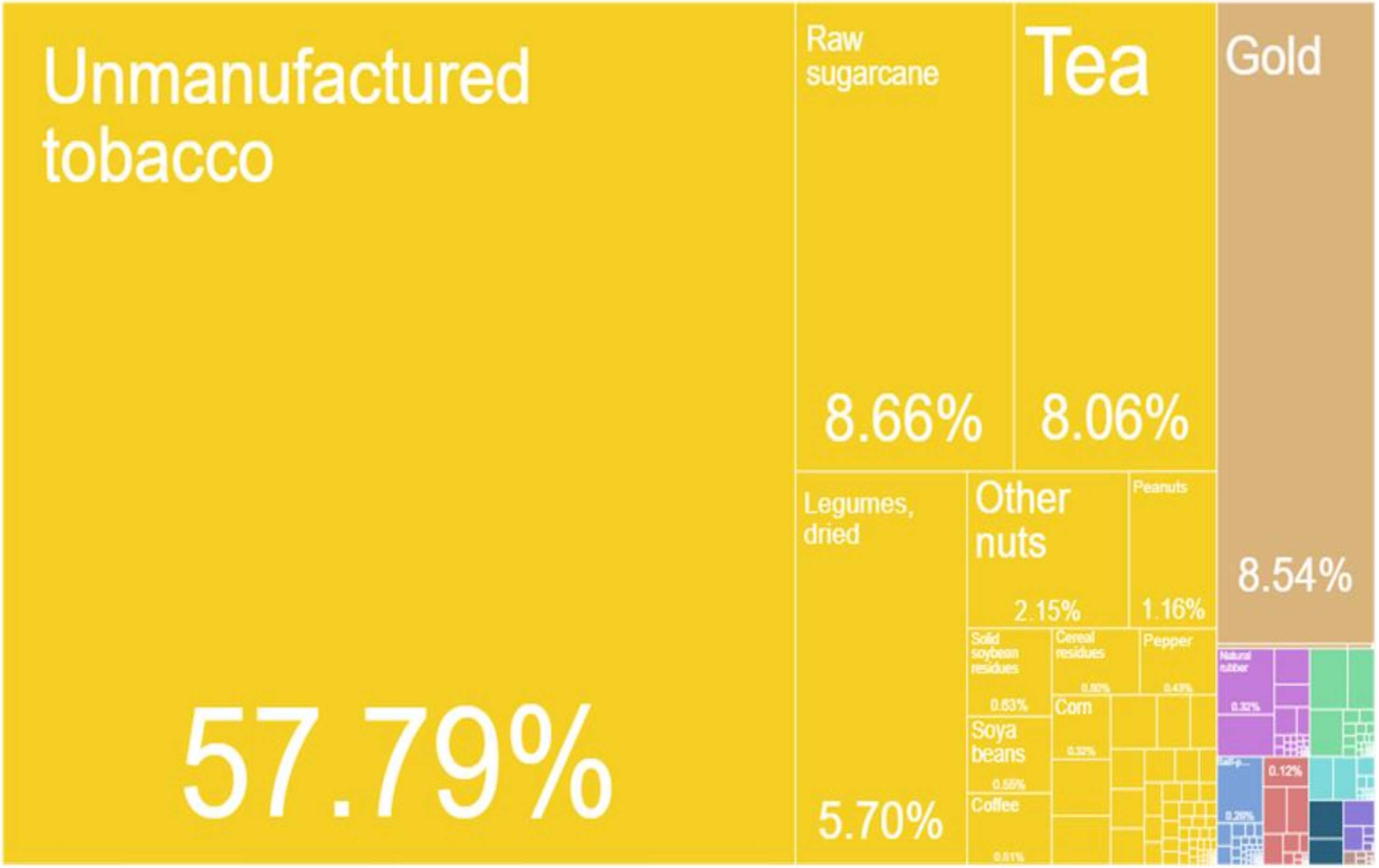
Agricultural Transformation Initiative: reshaping Malawi's agriculture sector

December 4-5, 2018

Foundation for a Smoke-Free World

Malawi’s reliance on tobacco

Contributions to Malawi exports, by value, 2016 (US$917m)

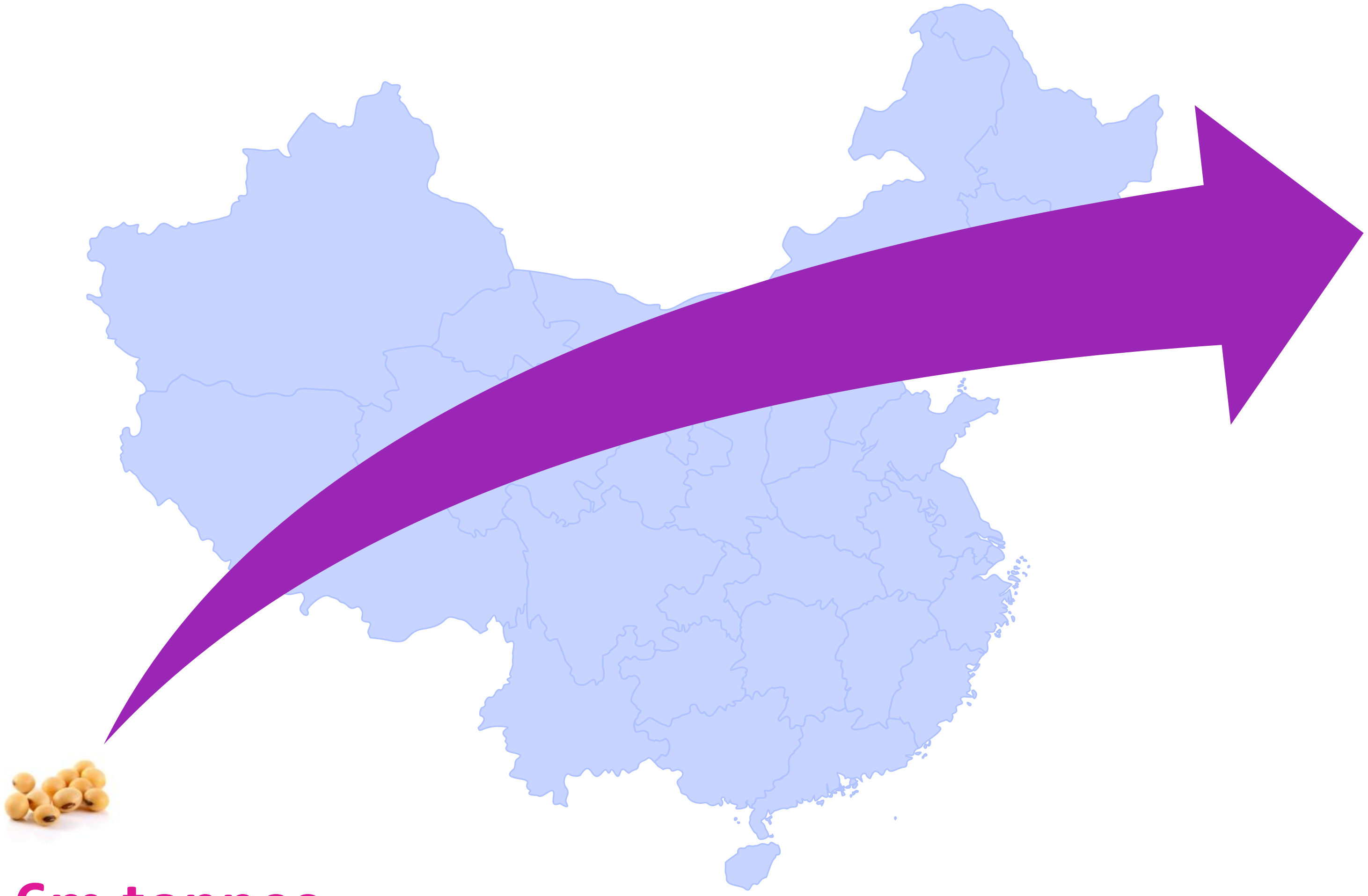


Source: Atlas of Economic Complexity, 2018

- Malawi is one of the most tobacco-dependent economies in the world
- In 2012, tobacco – Malawi’s most important cash crop – accounted for $654m in foreign exchange earnings for the country
- Tobacco exports accounted for 58% of all merchandise exports in 2016, 53% in 2015, 51% in 2014 and 46% in 2013 (BACI, 2018)
- The first step on the value chain, employed an estimated 451,000 people in 2016. This represented 2.5% of the population (World Bank, 2018)

Alternative universes: China’s soybean imports

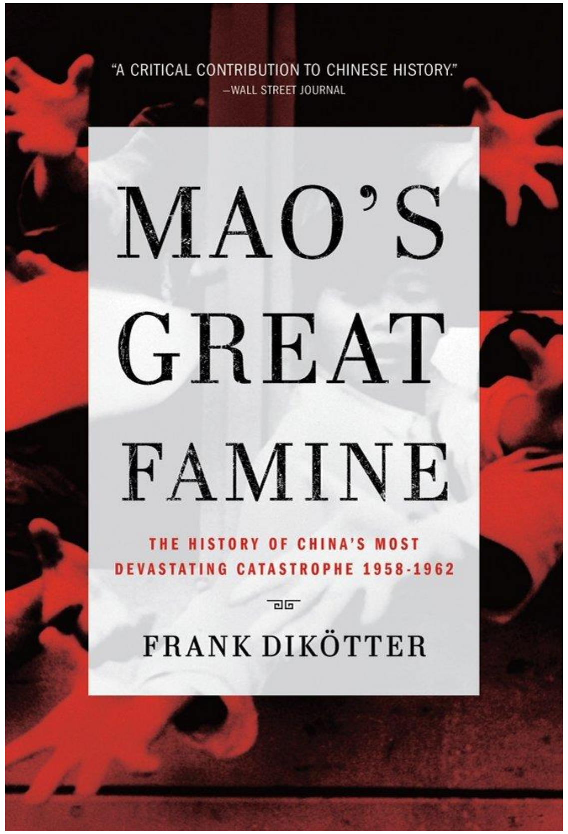
2018: **94m tonnes**



1996: **0.6m tonnes**

Source: USDA

China’s past, present and future

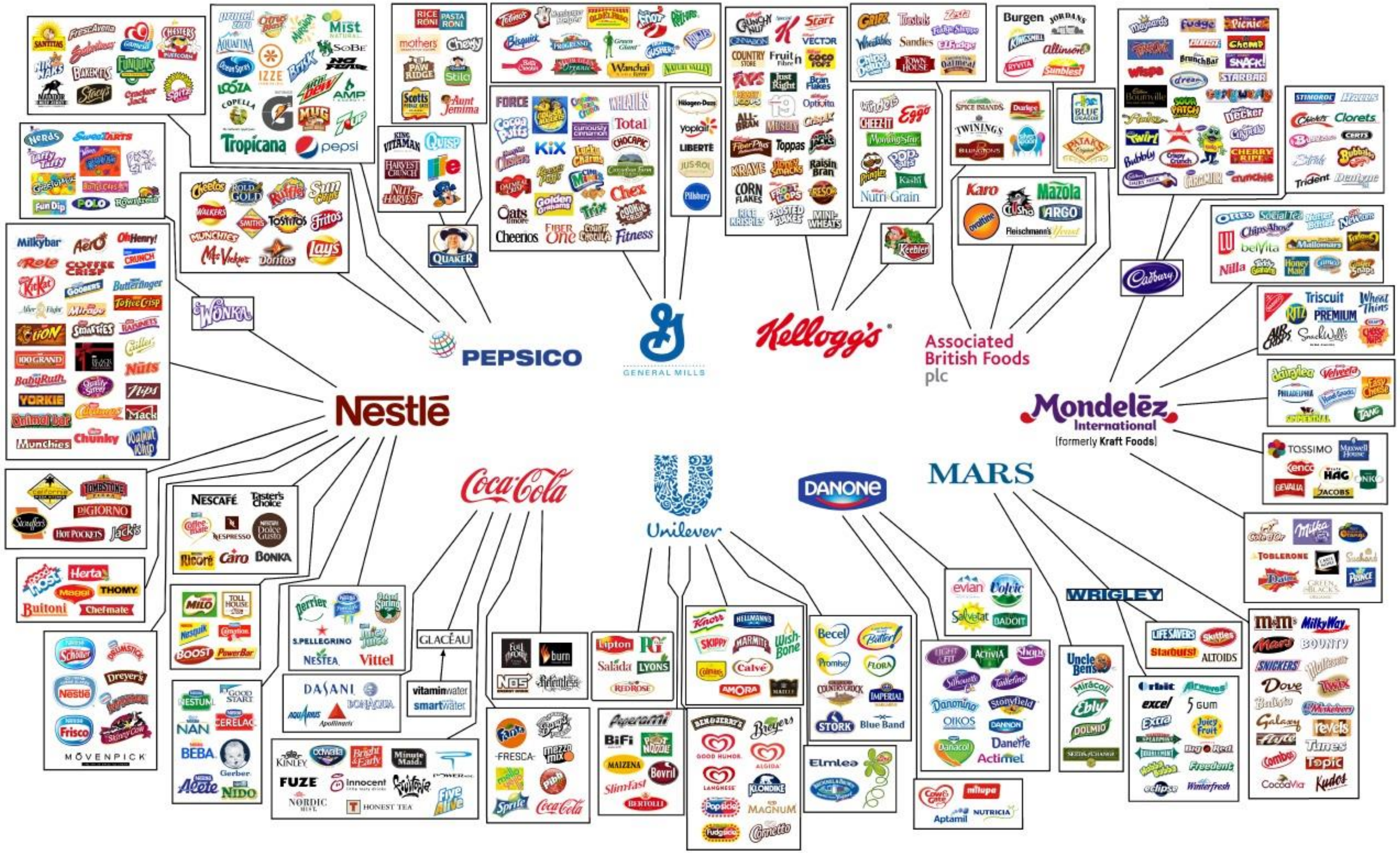


Past

Present

Future

The owners of everything



Understanding global trends in agriculture

Leading trading houses' shifting strategies

- Trading houses face structural threats due to:
  - The emergence of larger farming groups, and
  - The emergence of cheaper information
- In response, many are diversifying across the value chain

Well capitalized new players emerging

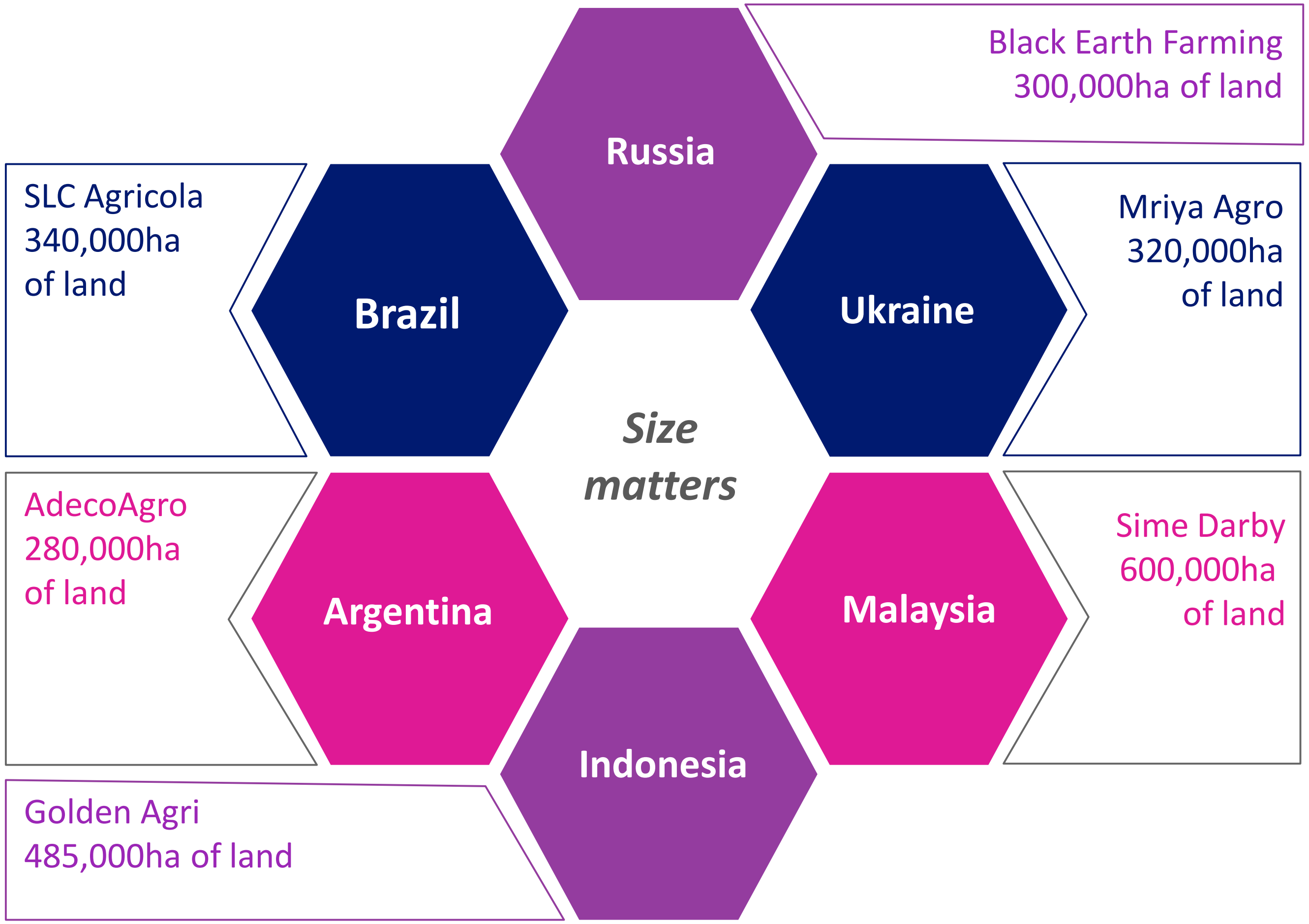
- New players emerging, challenging the dominant ABCD group, especially from Asia
- Strategic buyers from food deficit/capital surplus countries such as China, Japan and the Middle East will gain even more prominence in the years ahead

Food companies guaranteeing supply

- Stability of supply, integrity and provenance is becoming ever more relevant for international consumer good companies
- Expect major strategic shifts from many well recognized household names as they shift upstream

Farms are getting larger

- Capital targets scale and liquidity. Thus investors will not invest directly in smallholders. Farms are getting bigger
- Mechanisation, improved productivity and irrigation are all easier for large-scale farms
- Replacing Nigerian rice imports of 3-4m tonnes would require 400,000+ hectares of land; a conduit to capital requires a corporate solution
- Across the CIS and Brazil, corporate farming groups and large co-operatives of 200,000-300,000 hectares are the norm
- When Brazil’s Libero Commodities was founded it consisted of 33 farming groups and 5m hectares of land
- Malawi’s tobacco companies and food processing companies are uniquely positioned to become the new Libero Commodities



New thinking on investment models

The fund approach needs to fit	➢ A typical "2/20 model" means that approximately 10% of funds are given to asset managers in the first five years of an investment ➢ This places unrealistic pressures on hurdle rates during periods when operational execution is at its most fraught; fee structures will likely evolve
Intermediaries are too expensive	➢ Placement agents demanding 6% fees for placing funds have acted as a drag on investment in the agriculture sector ➢ The lack of clarity in fee structures and hidden charges acts against agricultural investment
Time horizons of PE houses are too short term	➢ Expected exit routes of 4-6 years in a sector, which is only beginning to industrialise, are unrealistic and ignore the long lead in times in agriculture ➢ The long-term businesses of palm oil, rubber and other plantations are especially uncorrelated with the financing cycle; 10-year lock ups should be the norm
Need for diversification	➢ Agricultural assets are still at the earliest stage of development and offer little in the way of geographical diversification ➢ It is unlikely that financial investors can create a diversified portfolio, simultaneously execute complex greenfield programmes and exit within four years of start up
Real assets versus financial assets	➢ The funding methods that characterised the period 1979-2008 will likely evolve over coming decades ➢ The era of financial assets driven by financial innovation and the higher velocity of money will likely be replaced by real assets