



Government of Malawi
Ministry of Industry, Trade and
Private Sector Development

Brief on Malawi's efforts to improve the business environment as measured by the *Doing Business* indicators

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Background

The Ministry of Industry, Trade and Private Sector Development (MITPSD) is leading efforts to formulate and implement a Private Sector Development (PSD) Strategy and Reform Programme, consistent with the Malawi Growth and Development Strategy (MGDS) which envisages private sector led growth in Malawi.

The objective is to increase private sector investment and jobs, and raise economic growth by building more effective partnerships between the public and private sectors that address constraints to enterprise development in Malawi and put the private sector at the heart of national economic development.

Malawi's PSD programme draws upon two pieces of analytical work: (i) the 2006 *Investment Climate Assessment*; and, (ii) the annual *Doing Business* surveys.

The PSD programme is proceeding along two complementary tracks. Firstly in a direct response to Malawi's poor ranking in the 2006 *Doing Business* report, the Government of Malawi launched five technical working groups in May 2006 on the five *Doing Business* indicators where, at the time, Malawi's performance was worst, and therefore offered the greatest scope for improvement¹. The five groups were drawn from sector specialists in both the public and private sectors. The groups recommendations are divided into policy and administrative reforms that do not have resource implications ("quick wins"), and recommendations that require longer term and more resource intensive activity. Government has already begun implementation of several of the "quick wins", while many of the longer term and more resource intensive activities are being addressed under a five year US\$18.7 million Business Environment Strengthening Technical Assistance Project (BESTAP), co-financed by the World Bank and the European Commission.

In the 2007 *Doing Business* survey, Malawi's overall ranking was 110 out of 175 countries. The Government of Malawi is committed to an ongoing process of improving the business environment, as measured by the *Doing Business* indicators. The following sections of this brief cover the ten indicators in turn, describing current reforms which aim to have a demonstrable impact on the costs of doing business, including the likely impact of such reforms.

It is estimated that full implementation of Malawi's Private Sector Development Reform Programme will result in an improvement of Malawi's *Doing Business* ranking from 110 to 53.

¹ Getting credit, trading across borders, paying taxes, dealing with licences and closing a business.

1. Starting a Business

Indicator	Malawi	Region	OECD	Reforms	Expected results ²
<i>The challenges of launching a business are shown below. Included are the number of steps entrepreneurs can expect to go through to launch, the time it takes on average, and the cost and minimum capital required as a percentage of gross national income (GNI) per capita.</i>					
Procedures (number)	10	11.1	6.2		
Time (days)	37	61.8	16.6	Computerisation of the business registry	10
Cost (% of income per capita)	134.7	162.8	5.3	Reduced costs	70
Minimum capital (% of income per capita)	0.0	209.9	36.1		
Malawi's ranking for starting a business	89			→	48

Under the BESTAP project, Malawi is addressing the costs of starting a business by providing assistance to the Registrar General's Department—the body responsible for all company and business name registrations in the country. The project will provide for systems diagnosis, specification, implementation and user training for a computer system to replace the current manual procedures. This will result in significantly reduced time and cost to register a business, and will also allow business registration to take place online throughout the country, rather than just at the current one location.

Furthermore, the costs and time taken to start a business are two of the key indicators included under the US Millennium Challenge Account is assessing whether or not Malawi will be able to progress from “threshold” to “compact” status.

2. Dealing with Licenses

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>Shown below are the procedures, time, and costs to build a warehouse, including obtaining necessary licenses and permits, completing required notifications and inspections, and obtaining utility connections.</i>					
Procedures (number)	22	17.7	14.0		
Time (days)	185	230.2	149.5	Introduction of Single Business Permit and introduction of “account executive” model in MITC	30
Cost (% of income per capita)	236.2	1,024.5	72.0		
Malawi's ranking for dealing with licenses	117			→	73

Reforming the business licensing regime was the first priority to be implemented by Government following the recommendations of the technical working group on “dealing with licenses”. The Ministry of Industry, Trade and Private Sector Development has already drafted new regulations that will provide for the collapse of eight trading licenses into one, provide for a simplified, non-discriminatory and transparent fee structure based purely on the costs of licence administration, and move to a process of

² Here, and in the following sections, the same methodology as used by the *Doing Business* team has been used by MITPSD to compute Malawi's expected ranking following reforms that will reduce the costs of doing business.

assumed private sector compliance with random rather than compulsory inspection of premises.

Although this reform may not have a significant impact on the actual “dealing with licences” indicator (since the ranking methodology is based on the process of building a warehouse), Malawi believes that the first priority should be to address an area that is particularly contentious in the private sector, and one that is known to have a damaging impact on private sector investment.

Secondly one of the key components under the BESTAP project is support to the establishment of a one-stop-shop at the new Malawi Investment and Trade Centre using the “account executive” model as a means of improving the efficiency of investment facilitation.

3. Employing Workers

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The difficulties that employers face in hiring and firing workers are shown below. Each index assigns values between 0 and 100, with higher values representing more rigid regulations. The Rigidity of Employment Index is an average of the three indices.</i>					
Difficulty of Hiring Index	22	44.3	27.0		
Rigidity of Hours Index	20	52.0	45.2		
Difficulty of Firing Index	20	44.9	27.4		
Rigidity of Employment Index	21	47.1	33.3		
Non-wage labour cost (% of salary)	1.0	12.7	21.4		
Firing costs (weeks of wages)	84.3	71.2	31.3		
Malawi's ranking for employing workers	68			→	68

Malawi's performance under the “employing workers” indicator is actually one of the better of the ten indicators. While the Government of Malawi is committed to reforming across the entire spectrum of private sector development, specific activities in the first instance have been focused on the more weaker indicators.

4. Registering Property

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The ease with which businesses can secure rights to property is shown below. Included are the number of steps, time, and cost involved in registering property.</i>					
Procedures (number)	6	7.0	4.7	Elimination in ministerial discretion on land sales	5
Time (days)	118	109.9	31.8	Computerisation of the lands registry	60
Cost (% of property value)	3.4	11.6	4.3		
Malawi's ranking for registering property	90			→	55

Support will be provided to the Lands Registry under the BESTAP project to provide for a diagnostic, systems specification, implementation and user training programme that will provide for the computerisation of the current manual land titling system. Coupled with planned reforms to the simplify the procedures for transferring land titles, this initiative will significantly reduce the time taken and costs to register and transfer private property.

By improving the system for registering title to land, this activity will also improve private sector access to credit through encouraging the use of land as collateral.

5. Getting Credit

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>Measures on credit information sharing and the legal rights of borrowers and lenders are shown below. The Legal Rights Index ranges from 0-10, with higher scores indicating that those laws are better designed to expand access to credit. The Credit Information Index measures the scope, access and quality of credit information available through public registries or private bureaus. It ranges from 0-6, with higher values indicating that more credit information is available from a public registry or private bureau.</i>					
Legal Rights Index	8		4.2	6.3	
Credit Information Index	0		1.3	5.0	
Public registry coverage (% adults)	0.0		1.5	8.4	
Private bureau coverage (% adults)	0.0		3.8	60.8	
Malawi's ranking for getting credit	65			→	65

Although Malawi's ranking for "getting credit" is actually the second best of all ten indicators, access to credit is widely recognised in Malawi as the leading constraint to private sector development (this result was also confirmed in the 2006 *Investment Climate Assessment*). Hence, Malawi is committed to improving access to credit, especially for micro and small enterprises.

At the macro-economic level, the Government of Malawi has made significant progress since 2004 in restoring stability and fiscal discipline. Interest rates have fallen consistently with the base rate dropping from 45 percent in mid 2004 to 20 percent in November 2006, with further reductions expected shortly. Domestic borrowing by Government has fallen significantly, and as a result private sector credit growth is already growing strongly as public sector crowding out is reduced.

At the micro level, Government is in the process of establishing an SME investment fund / venture capital facility with the support of the World Bank, which will aim to provide loans, guarantees and equity to business start-ups. Government's capital contribution to the fund will be capped at 20 percent, with the remainder being invested by the local and international private sector. Management of the fund will be in private sector hands. Under the BESTAP project, a US\$ 4 million matching grant scheme will also be launched to subsidise SME investment in soft infrastructure.

While the banking sector in Malawi is looking to establish a credit reference bureau, this is constrained by the lack of a national identification system in Malawi. In the meantime, the banks (in cooperation with the Reserve Bank of Malawi) are in the process of launching a voluntary credit information sharing system.

6. Protecting Investors

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The indicators below describe three dimensions of investor protection: transparency of transactions (Extent of Disclosure Index), liability for self-dealing (Extent of Director Liability Index), shareholders' ability to sue officers and directors for misconduct (Ease of Shareholder Suits Index) and Strength of Investor Protection Index. The indexes vary between 0 and 10, with higher values indicating greater disclosure, greater liability of directors, greater powers of shareholders to challenge the transaction, and better investor protection.</i>					
Disclosure Index	4		4.4	6.3	
Director Liability Index	7		4.5	5.0	

Shareholder Suits Index	5	5.2	6.6		
Investor Protection Index	5.3	4.7	6.0		
Malawi's ranking for protecting investors	60			→	60

Malawi's best ranking under the *Doing Business* indicators is for "protecting investors". Again while the Government is committed to reform across all areas, the initial efforts are focused on the indicators where there is greater scope for improvement.

7. Paying Taxes

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The data below shows the tax that a medium-size company must pay or withhold in a given year, as well as measures of the administrative burden in paying taxes. These measures include the number of payments an entrepreneur must make; the number of hours spent preparing, filing, and paying; and the percentage of their profits they must pay in taxes.</i>					
Payments (number)	29	41.0	15.3		
Time (hours)	878	336.4	202.9		
Total tax rate (% profit)	32.6	71.2	47.8		
Malawi's ranking for paying taxes	90			→	90

Private sector participation in the pre-budget process in the last two financial years has improved significantly compared to in previous budgets. However due to the lack of easy-to-tax natural resources, Government is dependent of a relatively narrow tax base for revenues. The Government is currently working with the IFC to explore areas where the processes and procedures for tax administration can be streamlined.

8. Trading Across Borders

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The costs and procedures involved in importing and exporting a standardized shipment of goods are detailed under this topic. Every official procedure involved is recorded - starting from the final contractual agreement between the two parties, and ending with the delivery of the goods.</i>					
Documents for export (number)	8	8.2	4.8		
Time for export (days)	44	40.0	10.5	Risk based customs administration	22
Cost to export (US\$ per container)	1,565	1,561	811		
Documents for import (number)	16	12.2	5.9		
Time for import (days)	60	51.5	12.2	Risk based customs administration	30
Cost to import (US\$ per container)	1,590	1,947	883		
Malawi's ranking for trading across borders	153			→	138

As a land-locked, least development country, reducing the costs of trade facilitation are a key component in Malawi's efforts to support export development. As a direct result of the recommendations of the technical working group on "trading across borders", the Malawi Revenue Authority is piloting the introduction of a "risk based customs administration system". Based on the successful experience in VAT administration, whereby firms with a proven track record of VAT compliance are issued with a one-year certificate which results in less onerous responsibilities, the system is being extended to customs processes. Customs compliant companies will similarly be issued

with a one-year certificate which results in physical inspections of only a random proportion of shipments passing through Malawi's international borders. This system will provide an incentive for private sector compliance, reduce the burden of inspections on the customs authorities, and result in speedier transit times for trading across borders.

9. Enforcing Contracts

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The ease or difficulty of enforcing commercial contracts in is measured below. This is determined by following the evolution of a payment dispute and tracking the time, cost, and number of procedures involved from the moment a plaintiff files the lawsuit until actual payment.</i>					
Procedures (number)	40	38.1	22.2		
Time (days)	337	581.1	351.2	Commercial Division	180
Cost (% of debt)	136.5	42.2	11.2	Commercial Division / ADR	30
Malawi's ranking for enforcing contracts	134			→	82

The largest constraint to the enforcement of contracts in Malawi (and with regard to closing a business) has been, until now, the lack of dedicated commercial courts. It is unsurprising that with the cost of enforcing a contract greater than the value of the debt, few companies result to the courts. In the current system, commercial cases tend to receive low priority compared to criminal and political cases.

However, Government is currently in the final stages of establishing the Commercial Division of the High Court. Four judges have already been appointed to the Division, rules have been drafted and premises identified. Full operations are expected to begin by the second quarter of 2007 and this will have a major impact on improving access to timely and cost-effective commercial justice. The BESTAP project will be providing significant support to the establishment of the Commercial Division including capacity building, cast audit management and introduction of case management systems, and training for judges, registrars and Alternative Dispute Resolution administrators.

10. Closing a Business

Indicator	Malawi	Region	OECD	Reforms	Expected results
<i>The time and cost required to resolve bankruptcies is shown below. The data identifies weaknesses in existing bankruptcy law and the main procedural and administrative bottlenecks in the bankruptcy process. The recovery rate, expressed in terms of how many cents on the dollar claimants recover from the insolvent firm, is also shown.</i>					
Time (years)	2.6	2.6	1.4	Commercial Division	2.0
Cost (% of estate)	29.5	16.0	7.1	Commercial Division / ADR	20.0
Recovery rate (cents on the dollar)	13.2	17.7	74.0	Commercial Division / ADR	40.0
Malawi's ranking for closing a business	132			→	46

Similarly the establishment of the High Court, Commercial Division will also speed up processes and reduce the costs of enforcing bankruptcy.

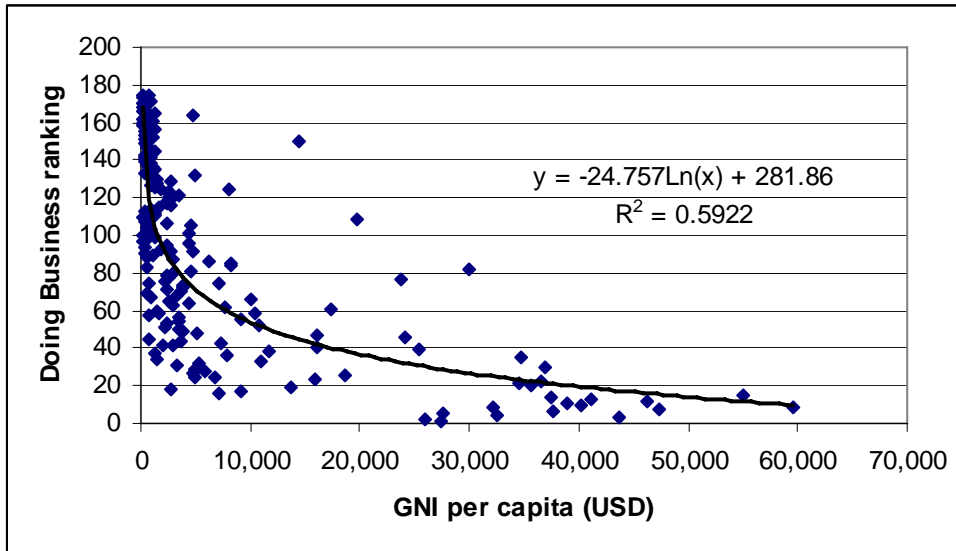
The development of new rules of commercial arbitration by the High Court will also result in faster and lower cost commercial justice where a dispute can be settled out of court.

ANNEX

CROSS-COUNTRY ANALYSIS OF MALAWI'S RELATIVE PERFORMANCE ACCORDING TO THE DOING BUSINESS INDICATORS

Figure 1(below) shows a plot of rankings against GNI per capita for the 176 countries included in the *Doing Business* survey. Unsurprisingly the results are difficult to interpret given the majority of countries are clustered in the low income range with a GNI per capita of less than USD 2,000 per annum.

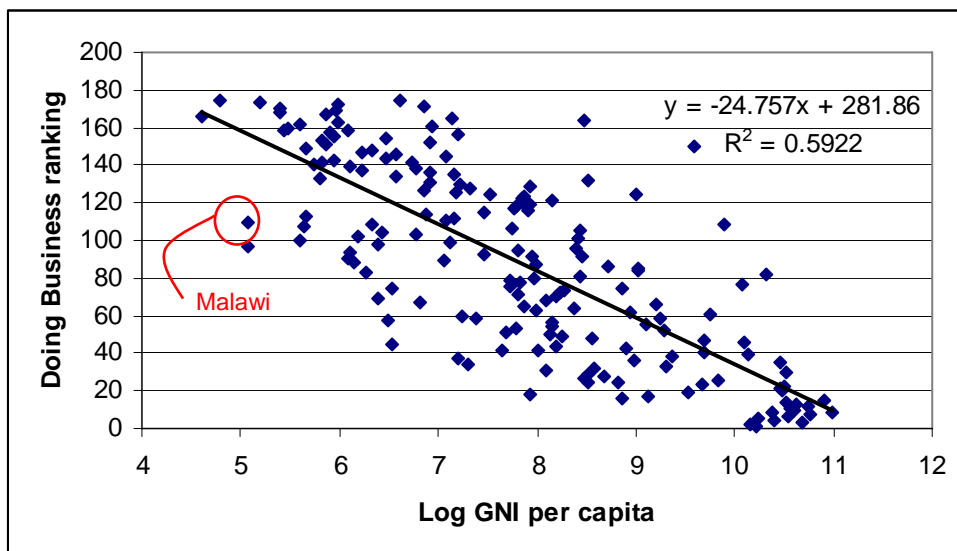
Figure 1: Plot of Doing Business ranking against GNI per capita, 176 countries, 2006



Regression analysis suggests an exponential relationship. A strong econometric relationship between Doing Business rankings and gross national income per capita is found. An R^2 of 0.59 implies that 59 percent of a country's Doing Business ranking is “explained” by relative income differentials.

Figure 2 shows a plot where GNI per capita on the x axis has been replaced by Log GNI per capita. This makes interpretation easier by distributing the values more evenly along the x axis and transforms the curved exponential curve into a straight line.

Figure 2: Plot of Doing Business ranking against log of GNI per capita, 176 countries, 2006



As indicated, Malawi is an outlier. According to the trend for GNI per capita, Malawi should be ranked much lower than the current position of 110. Countries below the trend line have a better than average business environment, compared to their peers at any given income level. Countries above the trend line have a worse than average business environment, compared to peers at any given income level.

This suggests that, given Malawi's per capita income level, the country already has a better business environment that would be expected. However, the recent changes in the way that Malawi's national accounts are calculated (which resulted in an increase in nominal GDP by 37.5 percent once the informal sector is included) suggests that Malawi may be actually be closer to the trend.

The key question is one of causality: does a better business environment result in higher income levels; or do higher income levels result in a better business environment?

The missing step, of course, is the need for investment. Malawi's efforts to improve the business environment are a necessary first step in order to facilitate the increased investment needed to push income levels higher.