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Linking Malawian smallholders to larger-scale agribusiness enterprises for inclusive development

A conceptual critique of the anchor enterprise model

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EXECUTIVE SUMMARY

While smallholder farming has been and remains at the center of agricultural transformation efforts in Malawi, the limited success of smallholder-centered agricultural development strategies has led policymakers to explore alternative approaches. One emerging approach involves larger farms or agribusiness firms partnering with smallholder farming households, in what we will refer to as an anchor enterprise model. Under this model, smallholder farming households contribute land and labor to produce crops or livestock products that serve as inputs for, or are marketed jointly with, the anchor enterprise. In return, the anchor enterprise provides support such as technical assistance, inputs, transport, or storage. This partnership is intended to be commercial and mutually beneficial. While support for such partnerships is growing and the anchor enterprise model is increasingly being used in development programming in Malawi, there is still little clarity on what they involve, what they aim to achieve, and the conditions they need for success. This study seeks to address these questions and assess whether such linkages between larger farms or agrifood processors and smallholder farming households can contribute to sustainable, resilient, and inclusive wealth creation in Malawi. The findings from this study are also summarized in a policy note (Benson, Cockx, and De Weerdt, 2025).

Anchor enterprise partnerships can be valuable development models in specific contexts. In particular, they can help both larger enterprises and smallholders overcome constraints imposed by weaknesses in Malawi's factor, input, and output markets, enabling both land and labor to be used more productively. However, the viability of the model depends heavily on the nature of the product at its center. Anchor enterprise models are generally not suitable for grain or other generic staple crops. For such products, partnerships are costly and carry high risk since farmers can easily find and sell to other buyers than their anchor enterprise partner if market prices rise above the agreed price for the partnership (*side-selling*). Similarly, if market prices drop below the agreed price, enterprises may buy elsewhere (*side-buying*). Rather, these partnerships are most likely to be economically justified for higher value, less widely grown, more specialized, more complex to produce or process, or highly perishable agricultural products. For these products, the risk of default is lower as the reduction in transaction costs provides both parties with strong incentives for maintaining a longer-term commercial relationship.

These incentives are especially important as the legal framework governing commercial partnerships in Malawi's agrifood sector remains underdeveloped. Formal contracts were found to be important but not central to successful anchor enterprise operations. Partnerships that endure are built on a strong economic rationale, clear financial incentives for all parties, and a degree of bilateral dependency.

Anchor enterprise models cannot be profitably and sustainably employed for many types of commercial agricultural production in Malawi. Consequently, only a small portion of farming households can directly participate, and the poorest and most vulnerable are generally less likely to be included. Nonetheless, where such models work well, they can deliver indirect benefits to the broader rural community, including its poorer and more vulnerable members, by stimulating local demand for labor, goods, and services. Complementary interventions aimed at strengthening the capacity of the poorest households to capture these indirect benefits may, however, be necessary for the model to contribute meaningfully to inclusive development.

A model centered around commercial farms or agro-processors requires an enabling environment for such enterprises to operate effectively. This includes macroeconomic stability, an investment climate that facilitates private investment in agribusiness, and trade and exchange rate policies that support formal exports. To be sustainable, anchor enterprise models must be grounded in a strong economic

rationale for partnering. Government and development partners can, however, support such partnerships without eroding their commercial foundations by, for example, investing in new institutions for conflict prevention and resolution, providing enterprises with assistance in managing relationships with smallholder partners, organizing financial and business training for farmers to reduce information asymmetries, or supporting organizations that can act as effective third-party intermediaries.

INTRODUCTION

Over the past decade, a central agricultural development priority of the government of Malawi has been to sustainably transform the production orientation of the country's smallholder farming households from a focus on meeting their subsistence needs to engaging in commercial production for the market. Such a change is expected to increase agricultural production, marketed surpluses, and the incomes of farming households. While smallholder farming has been and remains at the center of agricultural transformation efforts, the limited success of smallholder-centered agricultural development strategies has led policymakers to explore alternative approaches. The 2016 National Agricultural Policy for Malawi, for example, noted that the policy's ambitions will not be achieved without a more heterogeneous perspective on the farming sector. Public investments under the policy are to be designed "to be beneficial for all farmers – for smallholders operating primarily at a subsistence level, medium-scale farmers who are consistently able to produce marketable surpluses, and larger commercial producers (MoAIWD 2016a, 8)." The aim is to enable entrepreneurial farmers operating at any scale to increase the profitability of their production. Promoting pro-poor linkages between commercially oriented large-scale estates and smallholder farmers was noted as a potential avenue to achieve this (MoAIWD 2016a, xi).

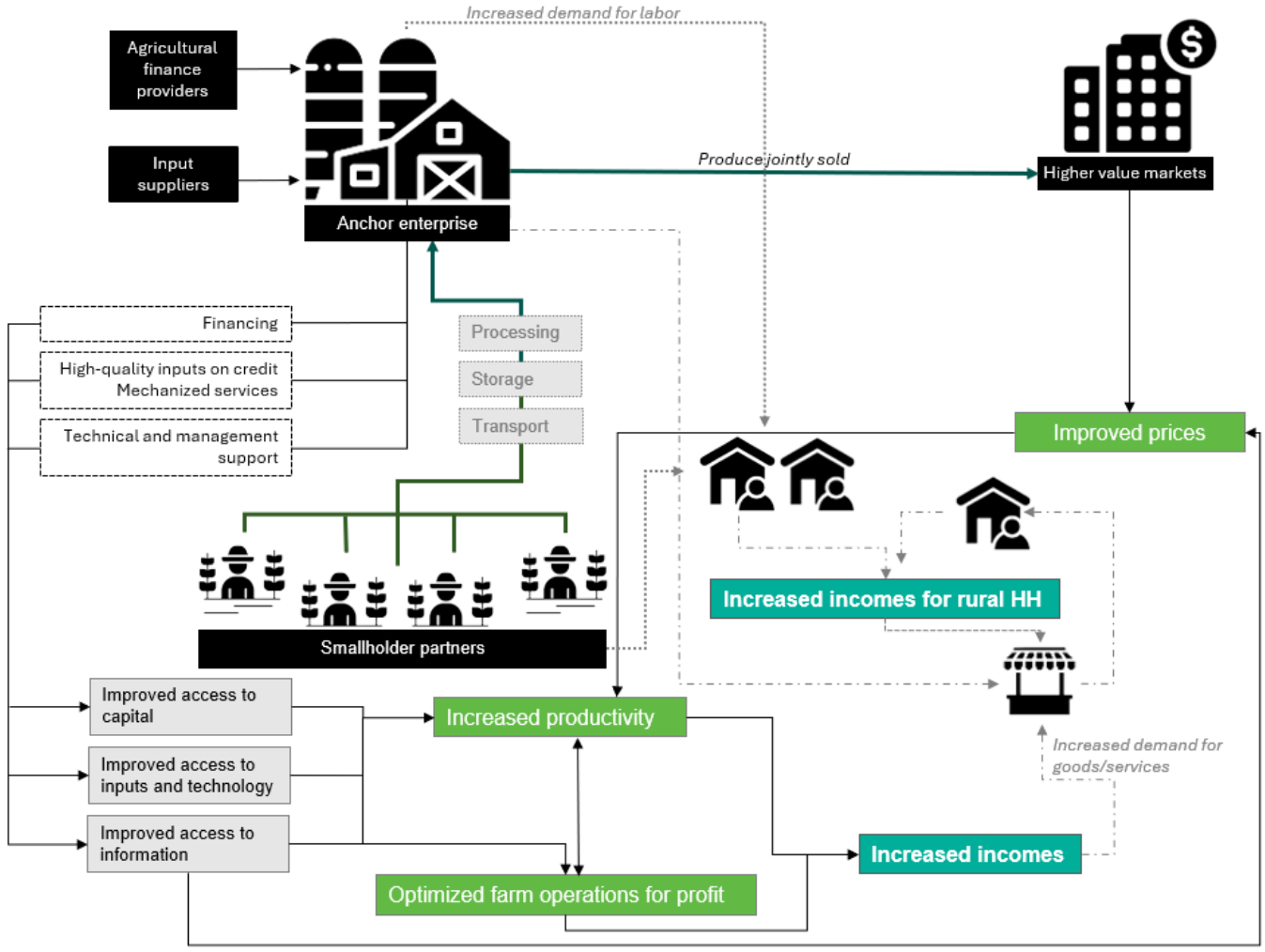
This agricultural development model, centered on larger-scale anchor farms engaging in mutually beneficial economic relationships with smallholders, gained a higher profile through Malawi 2063, the national development vision launched in January 2021 (GoM 2020). As part of the pillar focused on increased agricultural productivity and commercialization, large commercial farms are singled out as a powerful vehicle for modernizing and strengthening the commercialization of Malawian agriculture. The current 2024 National Agricultural Policy echoes this by identifying anchor farms as an important means of expanding agricultural markets and increasing market-oriented and profit-driven activities in the sector (MoA 2024). In parallel, over the past decade, some private enterprises have developed business operations and several of Malawi's development partners have launched pilot programs that link smallholders with larger anchor farms in commercial partnerships.

The development model has also been extended beyond a focus on anchor farms to increasingly involve larger-scale agrifood processors as anchor firms operating in partnerships with smallholder farming households. Consequently, we refer to this agricultural development model built around a larger-scale farm or agro-processor commercially partnering with smallholders as an *anchor enterprise* model.[1]

Under this model, smallholder farming households contribute land and labor to produce crops or livestock products that serve as inputs for, or are marketed jointly with, the anchor enterprise. In return, the anchor enterprise provides support such as technical assistance, inputs (often on credit), transport, or storage (see Figure 1). The type and scope of these supporting activities can vary, but we exclude arrangements where the enterprise only buys crops or livestock products without offering additional support. This partnership is intended to be commercial and mutually beneficial.

[1] Many terms are used interchangeably to refer to arrangements with some elements of the anchor enterprise model as we define it. During our research, we also encountered terms such as *anchor farms, anchor firms, nucleus estates, productive alliances, outgrower schemes, contract farming, hub-and-spoke models, satellite farmers*, and *sharecropping*.

Figure 1. Schematic representation of the anchor enterprise model



Source: Authors
Note: Figure 2 identifies several assumptions underlying this diagram.

The operators of the anchor enterprise are assumed to be more productive, better able to acquire and profitably utilize improved technologies in their farming or other business operations, more creditworthy, and better connected to high-value markets than their smallholder neighbors. Given those advantages, positive spillovers are expected to emerge as the smallholders improve and expand their own use of the elements that contribute to and drive the improved performance of the anchor enterprise. Working with smallholder farmers enables the anchor enterprise to increase production by facilitating access to more land or labor. The resultant larger joint enterprise may achieve economies of scale that cannot be obtained without the partnership. These economies of scale could follow from spreading fixed costs over a large volume of output. Examples of such fixed costs could be investments in agricultural mechanization, large-scale irrigation, or storage and processing facilities. Moreover, input and market access could be improved through coordination to obtain either lower costs for inputs or better output prices. More broadly, through the intensified commercial activity of the anchor enterprise partnership, broader spillovers into the local rural economy will occur. These can be achieved through increased employment, either directly within the anchor enterprise operation or through the greater demand the

increased incomes of the smallholder partners generate for the goods and services that other households in the local economy can provide, increasing their incomes.

However, the validity of assumptions on the strengths and opportunities larger-scale enterprises offer smallholders is not always evident. Large-scale farming in Malawi has historically been characterized as much by failure as by success. Large agrifood processing firms similarly operate in a difficult business environment, exposed to significant production, market, and policy-induced risks. Establishing and sustaining partnerships between smallholder farming households and anchor enterprises can be a challenging task. Even under supportive production, market, and policy conditions, idiosyncratic factors – illness, disputes over land or labor, opportunistic behavior, and the like – may render unworkable a commercial partnership between an individual household and the anchor enterprise. Entering such economic partnerships imposes additional risks to both the business operations of the larger enterprise and the assets of the smallholder, making it unclear whether each will realize any net benefits.

While support for such partnerships between larger-scale enterprises and smallholders is growing and the anchor enterprise model is increasingly being used in development programming in Malawi, there is still little clarity on what they involve, what they aim to achieve, and the conditions they need for success. No robust theories of change have been developed to explain how this partnership model will benefit rural households or be a profitable engagement for the anchor enterprise. This study seeks to address these questions and understand whether such linkages between larger farms or agrifood processors and smallholder farming households can contribute to sustainable, resilient, and inclusive wealth creation in Malawi. Insights from this assessment are intended to assist the government, development partners, and other stakeholders in Malawi's rural economic development in more effectively drawing upon and exploiting the opportunities for agricultural transformation presented by larger-scale agrifood enterprises partnering with smallholders, while also being clear on the limitations of such an approach.

To better understand the potential of anchor enterprise models for agricultural and rural economic development in Malawi and the challenges such models face in implementation, in its organization, this paper moves from context to conceptual issues to analysis and evaluation. We start by summarizing the agricultural development context of Malawi to place anchor enterprises within broader policy and economic trends. Next, we examine several anchor enterprise initiatives in the country, highlighting the particular roles that government agencies, development partners, and private sector actors have taken in shaping these partnerships. We then present a theory of change for the anchor enterprise approach, illustrating how such partnerships are intended to drive agricultural transformation and rural economic development. The next section explores and assesses the significance of a range of potential implementation challenges for anchor enterprise initiatives, focusing first on the economic rationale for these partnerships – including transaction cost reduction, economies of scale, and other efficiency gains – and then on issues of contracting and conflict management. Finally, the paper assesses whether anchor enterprise models are likely to promote inclusive economic development before concluding with a synthesis of key findings and their implications for policy and public investment.

THE AGRICULTURAL DEVELOPMENT CONTEXT FOR ANCHOR ENTERPRISES IN MALAWI

The agricultural sector in Malawi is dominated by smallholder farmers producing rainfed crops primarily for their own subsistence needs. They farm small landholdings to which they have use rights by virtue

of their membership in the local community. Most smallholders have limited access to agricultural inputs and information, as well as insufficient capital to make investments that would increase their productivity levels. When they engage with markets, they find the markets do not reliably provide them with access to buyers offering sufficiently remunerative prices for their produce. Since relying on such markets to guarantee their food security is risky, meeting their own subsistence needs continues to dominate the production decisions of most smallholder farming households (Benson 2021). Over 93 percent of rural workers who are employed work in agriculture, mostly on their own landholdings (IFPRI 2022). Given the large share of Malawians who depend on their farming to meet their basic needs, the smallholder agricultural sector has been the focus of most agriculture development efforts in Malawi since at least World War II, when the country was still the British colony of Nyasaland (Vail 1983), and particularly so from late in the Kamuzu Banda era of independent Malawi and into the current period of multiparty democracy which started in 1994. A central objective of these efforts has been to enable the country to produce sufficient maize, in particular, to ensure food security. A program of annual subsidies on the prices of agricultural inputs for several million smallholder farming households has been the flagship strategy of the Malawian government for agricultural development since the late 1990s.

With the rural population of Malawi growing by 2.9 percent annually, the average smallholder household landholding is shrinking, having fallen to an estimated 0.7 hectares in 2019/20 (Benson and De Weerdt 2023). Many smallholder households now have farms that are too small to provide for the basic needs of their members. There have only been limited improvements in crop productivity levels. In consequence, generating rural economic growth from smallholder agricultural production has proven challenging. Moreover, despite the large share of public expenditure allocated annually to provide subsidies on agricultural inputs for smallholders, many households continue to face food insecurity. On average, one in eight Malawians was judged sufficiently vulnerable to hunger to require humanitarian assistance each year between 2002/03 and 2020/21 (Benson 2021).

Given this evidence of the limited impact of smallholder-centered agricultural development strategies over the past several decades, development planners in Malawi are increasingly exploring alternative ways to accelerate agricultural and rural economic development. Smallholders are not the only agricultural producers in Malawi. Larger-scale estates were first established in the late 1800s by European settlers in the Shire Highlands of southern Malawi, primarily for the production of export crops. Settlers owned most estates in Malawi until independence. However, in the 1970s and 1980s, Kamuzu Banda fostered a significant expansion in estates owned by indigenous Malawians (Kydd and Christiansen 1982). The most recent estimate indicates that approximately 30,000 agricultural estates in Malawi manage 1.35 million hectares (Deininger and Xia 2017), while farming households cultivate around 2.50 million hectares (Benson and De Weerdt 2023).

Although the early estates experimented with several crops, by the 1940s, tobacco had come to dominate estate production, particularly with the expansion of estates into central and northern Malawi (McCracken 1982). Tobacco requires considerable labor to produce, so most estate owners engage smallholder farming households to farm one or two hectares on their estate under sharecropping arrangements. Tobacco leaf has made up over 50 percent of the value of Malawi’s exports for many decades. In both the colonial period and after independence, policies restricted important aspects of tobacco leaf marketing to estate owners alone in order to support the estate sub-sector. However, most of those restrictions were removed in the mid-1990s, allowing smallholders to now dominate tobacco production, producing on their own land. Nonetheless, many estates remain commercially successful.

There is some evidence suggesting that over the past several decades, increasing numbers of Malawians have acquired significant areas of customary land to develop larger farms, ranging in size from 5 to 50 hectares. Many are absentee farmers with significant non-farm income sources who are investing in farming to diversify their economic activities. Others are successful local farmers seeking to expand the scale of their production (Anseeuw, et al. 2016). Consequently, several key stakeholders in agricultural development in Malawi, as well as the current National Agricultural Policy (MoA 2024), view the new medium-scale farms, as well as the longer-established estates, as central to any efforts aimed at establishing a much stronger commercial orientation across the agricultural sector.

SELECTED ANCHOR ENTERPRISE INITIATIVES IN MALAWI'S AGRIFOOD SECTOR

Both the government of Malawi and its development partners have launched in recent years programs and projects that employ components of the anchor enterprise model. In parallel, some private enterprises have developed business operations based on commercial partnerships with smallholder farmers. We provide a summary of several of these activities organized by the government, development partners, and private enterprises, respectively.[2]

Government engagement

As noted above, large commercial farms are identified as a powerful vehicle for the modernization and increased commercialization of agriculture in the Malawi 2063 development vision (GoM 2020). This developmental role is articulated even more strongly in the vision's first implementation plan. Anchor farms – defined as "big aggregate farms and/or cooperatives that best unleash the potential production and productivity of commercial smallholder farmers to generate surplus raw materials for industrialization (GoM 2021, 8)" – are one of the eight priority areas under the 'agricultural productivity and commercialization' pillar. Reflecting this emphasis, the Ministry of Agriculture highlights support for anchor farms in the 2024 National Agricultural Policy as part of efforts to improve access to farm inputs and mechanization services and strengthen agricultural markets (MoA 2024). Beyond agricultural production, anchor firms also feature as a priority under one of the seven enablers of the Malawi 2063 vision, namely private sector dynamism (GoM 2024, 62).

After the launch of Malawi 2063, the Ministry of Agriculture, working with several research partners, developed a strategy centered on the concepts of mega farms and anchor farms, resulting in the launch of the government's Mega Farm Programme before the 2023/24 cropping season (MoA 2022, Gondwe, et al. 2022).[3] Registered mega farms are intended to serve as anchor farms to enhance the commercial performance of neighboring smallholder farming households. These schemes are expected to typically involve smallholders using their own land and labor to produce crops for sale to the mega farm. Ingrower models, where smallholders cultivate land owned or controlled by the mega farm, however, are also possible. The mega farm is expected to negotiate with suppliers to obtain the inputs and services needed for its own operations and, in its role as an anchor farm, those of its smallholder

[2] A review was conducted of programs and projects in Malawi that employ components of the anchor enterprise model. Seventeen interviews were also conducted in March 2025 to obtain additional details on the model from staff members of agencies and enterprises involved in the design or implementation of these programs and projects. Three of these interviews were with larger-scale farmers in Kasungu district.

[3] While the qualifier "mega" is more commonly used in the literature to refer to farms operating on more than 500 or even 1,000 hectares, the government's Mega Farm Programme through the 2024/25 cropping season required participating farmers to operate on a minimum of 20 hectares for field crops and 5 ha for horticultural crops.

partners. It also aggregates the produce of its partners for sale into high-value markets. That way, the mega farm can recover from the sale proceeds the costs of providing its partners with inputs or other services.

The Mega Farm Support Department of the Ministry aims to facilitate access to agricultural credit, advisory services, farm inputs, mechanization and irrigation services, and higher-value output markets for the mega farms and, through them, their smallholder partners. However, the engagement of the Support Department does not extend into the relationship between the mega farm and the smallholders, such as how the mega farm is to share or be reimbursed by the smallholders for any financing, inputs, and services provided. Moreover, there is no guidance on conflict resolution. It is assumed that any disputes arising in such partnerships will be arbitrated by either local traditional authorities or administrative or judicial authorities at the district level.

In the 2023/24 season, over 800 mega farms were registered and over 200 received financing to obtain farm inputs. The program expanded in the 2024/25 season, with 950 out of over 2,500 registered farmers receiving financing for crop production on 46,000 ha (MoA 2025). While in the design of the program, the role of the mega farm as anchor farm was emphasized, the implementation of the program has focused exclusively on supporting the operations of the registered mega farms, very few of which engaged in partnerships with smallholder farmers.

Malawi's Agricultural Commercialization Project (AGCOM 2), which began a second six-year phase in 2024 (World Bank 2023), is another example of a project implemented by the Government of Malawi with elements of an anchor enterprise model. The project, with financing from a World Bank-led multi-donor trust fund grant, aims to facilitate the integration of smallholder farmers into commercial value chains through farmer cooperatives or other producer organizations forming “productive alliances” with agrifood processing firms as off-takers.

AGCOM provides support to improve the agricultural productivity of smallholder farmers and to expand the capacity of their producer organizations to meet the requirements of the buyers (World Bank 2017, GoM 2025). In addition, the project has a matching grant facility for enterprises to enable them to better engage as off-takers. The grants support investments to increase production, improve quality, and enhance value addition in the operations of these enterprises. To be eligible for a grant, the enterprise must provide evidence of the services it provides to the smallholder producer organization. These can include training and extension services, input supply, and supporting and monitoring the quality of the governance of the producer organization. The enterprises supported by AGCOM under these productive alliances can be anchor farms, but are more commonly off-takers, aggregators, or processors of agricultural produce – that is, anchor *firms*.[4]

Development partner engagement

In parallel with the shift in the government’s agricultural development strategies, several of Malawi’s development partners have initiated projects that involve partnerships between households in rural communities, particularly farming households, with larger, commercially oriented anchor farms or agro-processors.

[4] To achieve the Malawi 2063 vision, the government intends to more broadly support relationships between anchor firms and small enterprises (GoM 2024). However, it does not yet have a non-agricultural anchor firm program in place similar to its agriculture-focused Mega Farm Programme or AGCOM.

The Commercializing Agriculture For Industrial Growth (CAFIG) project, launched in 2024 with financial support from the Embassy of Ireland in Malawi, focuses on supporting small and medium-sized enterprises that are expected to act as anchor enterprises. The role of the households that partner with these enterprises is primarily in crop production. However, some anchor enterprises offer wage employment or plan to be a local source of demand for goods and services produced by partner households. The anchor enterprises involved in CAFIG are neither long-established nor large, so project activities to date have primarily focused on ensuring their commercial viability. Support to their partner households is expected to increase over the course of the project's implementation.

In contrast, the Malawi Growth Poles Project, similarly funded by the Embassy of Ireland, works with generally well-established large enterprises to integrate smallholder farmers and other rural households more strongly into agricultural value chains with high growth potential.[5] The project has identified four potential pathways to enable rural households to benefit from partnering with an anchor enterprise – increased smallholder production of high-quality agricultural produce for high-value markets; direct employment in the production or processing operations of the anchor enterprises; expanded markets for local enterprises through local sourcing of goods and services by anchor enterprises; and joint direct investment by the anchor enterprise and community members in community infrastructure or local services. The Growth Poles Project selects successful businesses that already possess many of the facilities and infrastructure, capacity, and resources required to integrate smallholders into various aspects of their business operations. The project then provides both the enterprises and their smallholder partners with support to enable them to better employ their assets and other resources for profitable production and make further investments to expand and strengthen their economic partnership.

Private sector engagement

Perhaps the most significant application of an anchor enterprise model within Malawi's agricultural sector is the Integrated Production Systems (IPS) operated by major international tobacco buyers. Since the early 2000s, the government has increasingly allowed tobacco-buying enterprises to enter into direct production arrangements with smallholder producers, rather than requiring them to purchase all their leaf on the auction floors. Under IPS, the tobacco-buying enterprises agree to purchase a contractually specified amount of tobacco from the farmer, deducting the value of the inputs they provided on credit from the proceeds of the sale. Tobacco-buying firms implementing IPS report repayment rates above 90 percent.

Beyond securing reliable supplies of quality leaf, a key driver of the IPS arrangement was the requirements imposed by their international customers that the tobacco-buying firms document that only appropriate production techniques and lawful labor practices were used in the production of their tobacco leaf in Malawi (Prowse and Grassin 2020, USDL 2024). However, the use of IPS was accelerated following the passage of the Tobacco Industry Act of 2019, which prohibited registered tobacco buyers from also producing tobacco (GoM 2019). This led tobacco-buying enterprises to divest from tobacco farming operations and increase their engagement with smallholder farmers and small estates through IPS. Most tobacco exported from Malawi is now produced under IPS.

[5] The United States Agency for International Development (USAID) initially provided 80 percent of the funding for the Growth Poles Project, scaling up an earlier USAID-funded project, the Agricultural Diversification (AgDiv) activity. However, in early 2025, USAID's financial support was canceled for reasons unrelated to the project.

Pyxus Agriculture Ltd. (Malawi), the national subsidiary of Pyxus International, an international tobacco enterprise with a long presence in Malawi, replicated its IPS model for groundnut production, using many of its tobacco IPS operational components and field staff. Pyxus aims to diversify from tobacco, draw additional value from its tobacco-focused infrastructure, and address some of the international criticisms it receives due to its core tobacco business.[6] However, the margins in groundnut production are much smaller than in tobacco, requiring large volumes of groundnut to be profitable. Participating smallholders, many of whom already receive tobacco IPS packages, are provided with inputs and extension services to produce groundnut. Pyxus purchases unshelled groundnuts and processes them at its factory in Lilongwe, deducting the costs of the inputs supplied the farmers from their sales proceeds.

In the 2024/25 growing season, Pyxus provided groundnut packages to 8,000 farmers with a target of obtaining 8,000 mt of unshelled groundnuts. While loan repayment rates for the groundnut package have been around 80 percent in recent years, they fell significantly after the 2023/24 season due to a disease outbreak (rosette) that reduced harvests, particularly in the Central Region. To retain productive farmers, Pyxus renegotiated repayment terms for many affected producers and rolled unpaid loans into the following season's loan obligations.

Two of the more complex partnership arrangements in Malawi are found in the Lower Shire Valley. Illovo, a large multinational sugar producer, has partnered with the Phata Sugarcane Outgrowers Cooperative (Phata 2018, Landesa 2019). In this model, cooperative members consolidated their land and registered it with the Ministry of Lands, using it as the basis for obtaining membership shares in the cooperative. Members receive annual dividends based on the land they contributed. The cooperative employs professional farm managers and hired workers to produce sugarcane for processing by Illovo. As the land of the cooperative members forms contiguous blocks, agricultural machinery is used in the cultivation of the cane and center pivot systems provide irrigation. The relationship with Phata, which has over 1,100 members, expanded the sugarcane area Illovo exploits by over 600 ha.

A similar partnership has been set up between Press Cane and the Katunga-Maseya Cane Growers (KAMA) Cooperative, which has over 2,100 members. With this arrangement, Press Cane aims to expand ethanol production by distilling it from sugarcane sourced from the cooperative's arable land of over 1,000 ha. Press Cane provided the funds necessary for KAMA to receive a matching grant from the government's AGCOM project. In return, Press Cane received an equity share in the cooperative and sits on the cooperative board. Although the grant was awarded in 2022, the project has experienced significant delays, and apart from a 105-hectare pilot area, sugarcane production had not yet begun by 2025.

Large tea estates were established by European settlers starting before 1900 in agroecologically suited areas in Mulanje and Thyolo districts. Through to the end of the colonial era in 1964, all tea production was done on the estates using wage labor. However, in 1967, the government created the Smallholder Tea Authority to promote smallholder tea production, and, in 1974, established the Malawi Tea Company to buy and process smallholder tea. Both state enterprises failed commercially and closed in 2006 (Cameron and Mkomba 2014). However, smallholder tea production continues with several grower associations selling green leaf to some of the large estates. Smallholder tea productivity is considerably lower than that on estates due to weaker agronomic practices, such as low planting

[6] While Pyxus' groundnut operations are commercial, it is also one of the growth poles with which the donor-funded Growth Poles project collaborates. The project support has centered on strengthening partnerships, as well as groundnut seed production and some co-financing for capital equipment. Support from the Growth Poles project was reported to be less than one-quarter of its operational costs in any year. Pyxus also received additional direct support from USAID. While intended to run from 2023 to 2028, this was terminated in February 2025.

density, limited fertilizer use, poor weeding, and irregular plucking (Pound 2013). Nonetheless, in 2018, about 20,000 smallholders were members of tea grower associations (du Toit, Nankhuni and Kanyamuka 2018).

In addition to these formal partnerships, elements of the anchor enterprise model are also seen within farming communities across Malawi, where larger-scale farming households – typically operators of smaller estates or emerging middle-scale farmers – provide agricultural inputs on loan to their neighbors, often within extended family networks. Several larger-scale farmers interviewed during fieldwork for this study reported having distributed inputs to neighbors in past years. These informal arrangements typically involve repayment after harvest. Although larger farmers may be interested in purchasing, brokering, or otherwise facilitating the sale of the recipients' produce, this marketing element is typically not part of the agreement upon which the inputs are provided. If the social links between the partners are weak, the agreement will often be endorsed and authenticated by the village head as an independent witness. While this type of informal sharing of inputs may provide commercial benefits for the larger farmer by expanding the volumes of produce that they can sell, it also serves to build their social capital within the community.

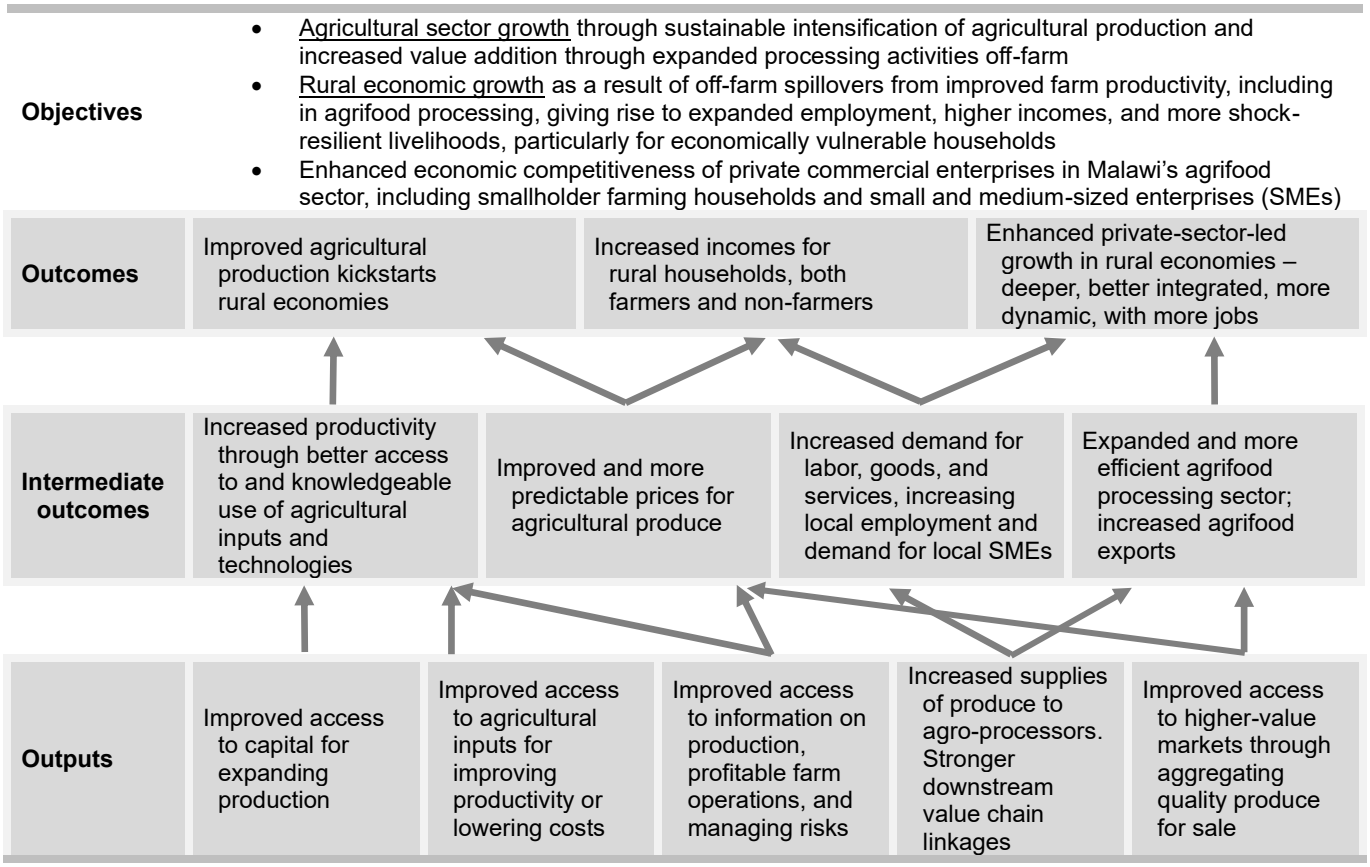
THEORY OF CHANGE FOR THE ANCHOR ENTERPRISE AGRICULTURAL AND RURAL DEVELOPMENT MODEL

Despite the increased support for the use of anchor enterprise models in development programming in Malawi's agrifood sector, there is still little clarity on activities involved in their implementation, what they aim to achieve, and the conditions they require for success.

No theories of change specific to the Malawi context have been developed that are grounded in a basic economic understanding of the organization of private commercial enterprises and the organization of agricultural production, particularly within smallholder-dominated farming systems. While theories of change, often implicit, are found in the documentation on the various anchor enterprise programs now underway in Malawi, the rationale is typically framed in terms of alignment with a framework of government policies, as with the Mega Farms Programme (MoA 2023), or to the broader national or global objectives guiding the work of the development partner involved, as with the Growth Poles Project (Palladium 2025). The rationale for adopting an anchor enterprise model to achieve the program's objectives, rather than an alternative approach, is not provided. Specifically, these theories of change do not provide guidance on what commercial or other advantages might induce a large-scale enterprise to partner with smallholder farming households or on what incentives the farming households might be responding to when entering such a partnership.

Figure 2 describes a broad theory of change for anchor enterprise development models in Malawi. The format used highlights the logic or results chain for the model, running from the bottom of the figure, with the assumptions underlying the model, to the top, where the development objectives in employing the model are specified. This theory of change derives from a review of documents on programs and projects in Malawi that employ components of anchor enterprise models and over a dozen interviews with individuals involved in these activities, as well as academic literature on economic organization. This economics literature offers conceptual insights into what may motivate partnerships between anchor enterprises and smallholders, the challenges that may arise in such relationships, and how those challenges can be addressed so that prospective mutual benefits from the partnership are realized.

Figure 2: Theory of change for anchor enterprise models in Malawi



Source: Author's compilation.

The broad objectives sought in applying the anchor enterprise model to the agricultural sector in the context of Malawi are threefold: improving agricultural productivity and intensifying post-harvest value-addition activities to expand the agricultural sector; fostering growth and increased dynamism in local

rural economies to expand and improve the livelihoods; and generating a much stronger and more successful commercial orientation among all farmers and other participants in Malawi's agrifood value chains. The three outcomes of the theory of change for the anchor enterprise model directly reflect these three broad objectives. At the center of these objectives and outcomes is a vision of improved and more resilient livelihoods for rural households. The commercial partnership between the anchor enterprise and rural households should enable both partners to increase their incomes, resulting in positive economic spillovers for the improved wellbeing of others in their community.

The intermediate outcomes reflect some of the technical and market changes that partnerships between anchor enterprises and rural households are designed to bring about. These include higher agricultural productivity; increased production of consistent, higher quality commodities that attract higher prices; greater and more reliable supplies of agricultural produce to markets, resulting in reduced seasonal price volatility; increased household incomes that stimulate employment opportunities and intensify commercial activities in the local economy; and greater levels of processing, domestic marketing, and exports of Malawi's agrifood products. Achieving these outcomes requires that the anchor enterprise model successfully generate several key outputs. For both the anchor enterprise and the smallholder, these outputs include significantly reducing many of the constraints they now face in making investments to improve productivity on their farms or in their processing facilities. A key output is that adequate amounts of appropriate farm inputs will be supplied to all partners in a timely manner and applied in a way that optimizes the profits obtained from their use. The increased agricultural production that results then contributes to achieving a stronger agro-processing sector in Malawi, with strengthened domestic markets and heightened trade in both primary commodities and, especially, processed agrifood products.

Figure 2 also lists some of the activities involved in implementing the anchor enterprise model. However, these activities are depicted more clearly in the schematic diagram of the model in Figure 1. The principal value of Figure 2 lies in its articulation of the assumptions underpinning the model, which highlight important limitations to its applicability. The first assumption is fundamental: there needs to be a good business case for the partnership based on reliable returns to the investments made by the partners – returns that would not be obtained if the partners were operating independently. The remaining assumptions concern the incentives for initiating and sustaining the partnership, which extend beyond the business case alone, as well as the mechanisms for managing any conflicts that arise between the partners.

The theory of change in Figure 2 provides much of the logic for how commercial partnerships between an anchor enterprise and smallholder farming households are intended to generate various development outcomes. However, it does not provide guidance on when or why such a partnership is the best option that either party could pursue to be commercially successful. In addition, the diagram does not specify where there might be important resource bottlenecks or conflicting objectives that will need to be surmounted if the partnership is to be sustained. It also does not examine the policy elements or oversight mechanisms that should be in place to ensure the partnerships are mutually beneficial and that any conflicts between the partners can be resolved fairly. These issues will be addressed in more detail below.

THE ECONOMIC RATIONALE FOR ANCHOR ENTERPRISE MODELS

In this section, we aim to understand the incentives that motivate an enterprise to partner with smallholder farming households – and, conversely, why smallholders might choose to engage with a larger enterprise. These incentives arise from the characteristics of the good being produced and from the conditions prevailing in the markets for inputs, factors of production, and outputs. We ask why an enterprise would expect the benefits of partnering with smallholders to outweigh the costs of doing so, given all the additional expenses and pressures involved with a partnership. We also seek to understand what net economic benefits smallholders expect from working with an anchor enterprise and how their exposure to various economic risks might change by committing to work with the anchor enterprise.

Reduced transaction costs

Conceptually, two opposing organizational frameworks form the endpoints on a continuum of how an enterprise can obtain (more of) a product: it can buy the product on a competitive market, or it can produce it in-house. Anchor enterprise models are a hybrid between these two extremes, combining elements of market sourcing with features of in-house production. In some cases, this type of commercial partnership with preferred suppliers is the lowest-cost option for securing a reliable supply. Whether this is true depends largely on the nature of the product and on the prevailing market conditions.

When sourcing from a free market, independent suppliers compete to offer the required product to a buyer. The price resulting from dynamic interactions between many buyers and suppliers reflects the levels of supply and demand in the market. However, there will be additional costs to arranging and carrying out an exchange. These transaction costs include costs related to searching for and screening possible suppliers, acquiring information on the quality or other attributes of their product, discovering the appropriate price, negotiating terms, and ensuring they are adhered to. Some of these costs will be tangible (e.g., staff time, transportation, or communication costs), while others are intangible (uncertainty or the risk of being cheated).

To a large degree, transaction costs are linked to two fundamental characteristics of human behavior (Williamson 1981). First, people are given to opportunism. Thus, the discovery of the price that reflects actual supply and demand conditions for a good within a market can be a relatively costly but necessary exercise, particularly when specific product characteristics are important to the buyer. Secondly, while economic agents aim to be rational in their production decisions, there are limits to how well anyone can obtain all relevant information and process it to consistently arrive at an optimally efficient solution – we are constrained by bounded rationality. Mistakes will be made in how the information is assessed, the principal economic objective of the productive activity may be unclear, or economic opportunities may quickly change within dynamic markets.

A well-functioning competitive free market should enable all buyers – including an enterprise seeking a product – to find sufficient suppliers and obtain what they require, so long as they are willing to pay the price that reflects the general levels of supply and demand in the market. Most markets in Malawi do not operate at this expected level of reliability. The dominance of subsistence production among Malawian farming households reflects a vicious circle in which thin markets reduce incentives for the

commercial production of food crops and foster a reliance on their own production by households, as they cannot rely on these markets for food security. This, in turn, reinforces the pattern of weak markets (Benson 2021). For an enterprise sourcing a product in thin markets, the transaction costs associated with identifying a supplier and discovering the appropriate price will be multiplied compared to what would be the case in a context with much stronger markets. Suppliers, meanwhile, can lack information about buyers and face uncertainty about what prices to charge. A challenge that is especially pronounced for smallholder farmers residing far from markets.

For generic, widely produced, nonperishable goods with limited or easily observable differences in quality or other attributes, sourcing from the open market usually remains the lowest-cost option even when markets are thin or weak. For such goods, a supplier can always find another buyer, and a buyer can likely always find another supplier. Consequently, for such products, partnerships are more costly and carry a high risk since farmers can easily find and sell to other buyers than their partner enterprise if market prices rise above the agreed price (*side-selling*). Similarly, if market prices drop below the agreed price, enterprises may buy elsewhere (*side-buying*).

However, when the characteristics of the good are more specialized or difficult to observe and those characteristics are critical to whether or not a transaction proceeds, the somewhat anonymous relationship between buyer and supplier in a free market is unlikely to be the lowest-cost way to organize the transaction. For such specialized goods, their characteristics and who the parties involved in the transaction are matter.

In the academic literature, “asset specificity” describes the degree to which the specific investments made to support a particular transaction “can be redeployed to alternative uses by alternative users without sacrifice of productive value” (Williamson 1985, 95). Asset specificity is thus a characteristic of a transaction, capturing the extent to which it requires tailored investments. Reasons for higher asset specificity range from the specialized skills, knowledge, and experience needed to produce a product, to the requirement for specific physical assets such as processing machinery, to the advantages of spatial proximity between buyer and supplier, and to path dependency in economic processes that entailed important sunk costs in their creation (De Vita, Tekaya and Wang 2011). High asset specificity increases the risk of loss due to opportunism and information asymmetry, raising the costs necessary to safeguard against those risks. For example, tea producers invest in establishing bushes that take years to mature. Tea has limited alternative uses and must be processed within a short time after harvest. This exposes the farmers to opportunistic behavior as the buyer may, for example, try to push prices down upon delivery knowing that farmers cannot easily sell elsewhere.

The degree of asset specificity of transactions is influenced by the type of product involved (see Box 1). Generic agricultural products are less likely to create high asset specificity as they do not necessitate highly specific investments by either party. However, asset specificity can still arise for such products. For example, when a buyer invests in processing equipment that cannot be easily redeployed to alternative uses. In such cases, the supplier is, however, likely to be able to easily find other buyers. This type of asset specificity is one-sided and does not create bilateral dependency that gives both parties strong incentives to maintain the partnership.

By contrast, many agricultural products exhibit characteristics that tend to generate higher asset specificity. Temporal asset specificity is particularly relevant for transactions involving highly perishable products, such as vegetables, fruits, unprocessed roots and tubers, sugarcane, tea, and livestock products (Mugwagwa, Bijman and Trienekens 2020). For such products, suppliers and buyers must coordinate the timing of harvest and delivery, creating mutual dependence and shared exposure to the

risks of relationship breakdown. Similarly, product attributes that are difficult to observe or verify (without specialized testing) such as moisture content, aflatoxin infection, pesticide residues, or adherence to organic production methods, can give rise to asset specificity. Meeting such requirements may require farmers to invest in specific production knowledge and practices that have limited value outside the relationship. The enterprise or buyer, in turn, must invest in identifying and developing suppliers capable of consistently meeting these standards, making it costly to switch to alternative sources.

Where transactions are characterized by high asset specificity, identifying counterparts, assessing the quality or other attributes of the goods, discovering appropriate prices, and negotiating agreements all demand significant time and resources. In such cases, anonymous market transactions are unlikely to be the lowest-cost option. The enterprise faces two alternatives: organize or expand its own in-house production or form partnerships with suppliers.

Box 1: Types of agricultural products

Type	Description	Examples
Generic	Homogenous, widely produced, nonperishable, and easily observable quality or other attributes	Maize, soybean
Specialized	Require specialized skills, knowledge, or inputs	Seed, poultry
	Require specialized processing	Sugarcane, tea
	Have hard-to-observe quality or other attributes	Aflatoxin-free groundnuts, deforestation-free coffee
	Are highly perishable	Horticultural products, dairy

In seeking to start or scale up their own agricultural production or agrifood processing in Malawi, the costs that an enterprise incurs in obtaining sufficient land and labor, in particular, can be significant. Access to land is predominantly organized through customary land tenure mechanisms tied to community membership rather than through markets. Particularly in rural communities where rainfed cropping is the dominant livelihood, intense seasonal demand for labor to conduct crop operations on time may result in periods during which no labor is available for an enterprise to hire, while after the harvest, many workers will be underemployed. In addition, while members of a farming household have strong incentives to work efficiently, hired workers require supervision, which can involve high costs for the enterprise (Binswanger and Rosenzweig 1986). Partnerships with landholding households can offer enterprises more reliable access to these factors of production. While organizing production in-house might offer more control of the production process for the enterprise, it also decreases its flexibility to scale up or down. Commercial partnerships with preferred suppliers, including smallholder farming households, offer such flexibility.

Such partnerships are an intermediate way to organize production between an enterprise sourcing a product from the open market or producing the product itself, and mitigates some of the problems

arising from both opportunistic behavior in economic transactions and the bounded rationality of economic agents in planning (Williamson 1981). Partnerships with smallholder farmers[7] in an anchor enterprise model eliminate transaction costs associated with finding and coordinating with suppliers and avoid inefficiencies associated with weak markets for land and labor, as well as for capital. Even though setting up and managing such partnerships involves substantial costs, the use of the anchor enterprise model can, in some circumstances, result in lower transaction costs than what would be incurred if the enterprise were to rely solely upon either markets or organize production in-house. However, the superiority of the anchor enterprise model for organizing production in a specific context should not be assumed. It would need to be demonstrated with a comparative transaction cost analysis against those incurred in relying on either markets or in-house production.

The fact that agricultural and rural factor markets remain relatively weak in Malawi provides incentives for smallholder farming households to form partnerships with anchor enterprises. Several of these mechanisms are highlighted in both the conceptual diagram (Figure 1) and the theory of change (Figure 2). The anchor enterprise is likely better endowed than the smallholders with productive assets on which the smallholders might also rely, such as agricultural machinery or crop storage facilities. It can also be expected to be better able than smallholders to reliably obtain commercial agricultural inputs of high quality at a relatively low cost, have greater access to capital and information, have greater experience in operating at a larger scale to raise production and profitability levels, and be better able to engage in marketing and trade in higher-value markets.

Bilateral dependency can develop where both parties have strong incentives to maintain the partnership. For a specialized input, the enterprise will often find it more costly to seek out alternative sources of supply within the market. The enterprise can then be expected to make efforts to ensure the partnership with its supplier continues (Williamson 2002). Smallholders producing these more specialized outputs required by the enterprise can also face high transaction costs in seeking to sell in the open market because they lack information on prices and buyers for the specific good and can be located far away from appropriate markets. Returning to the same buyer can reduce these transaction costs. If bilateral dependency develops, conflicts between the partners are more likely to be resolved in a manner that maintains the partnership. In contrast, in commercial relationships with limited bilateral dependency, recurrent conflicts are more likely, and partnerships are more difficult to sustain. Contractual obligations, premium prices, or longer-term considerations such as continued access to inputs can, however, motivate smallholders to continue engaging in their partnership with the enterprise.

Partnerships with smallholder farming households to expand the enterprise's access to land, labor, and specific inputs also provide important benefits for those smallholders by enabling them to commercially benefit from the agricultural production advantages and business acumen of the enterprise. Differences in the ways smallholder households and large farms or other larger-scale enterprises in Malawi access and mobilize factors of agricultural production, particularly the limited role of factor markets, make the anchor enterprise model a potentially profitable way for them to jointly organize their commercial agricultural production and draw upon their respective strengths. In addition, for perishable products, anchor enterprise models can provide the coordination needed to ensure that the smallholders' outputs are marketed in a timely manner, reducing much of the uncertainty that may otherwise cause risk-averse smallholder farmers not to participate in value chains for those products. Nonetheless, among

[7] While this logic also applies to partnerships between enterprises and large farms, in the context of Malawi, where smallholder farmers overwhelmingly dominate agriculture, partnering with smallholders will often be the more readily available option.

the active anchor-enterprise-based initiatives in Malawi's agrifood sector reviewed for this assessment, we found overall quite limited bilateral dependency in the partnerships (Box 2).

Box 2: Asset specificity in anchor-enterprise-based initiatives in Malawi

For most of the anchor enterprise-based programs in Malawi reviewed, the asset specificity of the transactions at the center of the partnership is relatively low. The government's Mega Farm Program has so far focused on increasing maize production. Maize is a generic commodity that is grown by almost all farmers, most of whom will supply the market with any of their production that is surplus to their own subsistence requirements. Buying or selling in the market would likely involve lower transaction costs than using an anchor enterprise model.

For both the IPS programs of the tobacco-buying enterprises and Pyxus' groundnut production, there are elements of asset specificity, but they primarily apply to the enterprises. Specifically, tobacco-buying enterprises must ensure that the leaf is traceable back to its producers. The partnership under IPS enables the buying enterprises to trace the leaf. However, nothing inherent in the farmers' tobacco compels them to sell to the enterprise. Similarly, Pyxus requires a large and reliable supply of groundnuts to use their processing equipment to full capacity. It also seeks to sell into higher-value markets, particularly those requiring the groundnuts to be certified as aflatoxin-free. It purchases unshelled groundnut and processes them centrally in its factory to eliminate any chance of aflatoxin contamination. Yet again, there is nothing in the physical characteristics of the groundnut they produce that compels the smallholder involved in the groundnut program to sell to Pyxus.

Economies of scale

An additional motivation for engaging in an anchor enterprise partnership is that the resultant larger joint enterprise may achieve economies of scale that cannot be obtained without the partnership. By spreading the fixed costs of production of both the anchor enterprise and its partner households over a larger volume of output or by improving input and market access through coordination to obtain either lower costs for inputs or better output prices, the average cost per unit of output produced by the partnership may decline, generating increased commercial returns for all.[8]

The relationship between scale and productivity in agriculture is a subject of debate. Although countries with larger farms tend to have higher agricultural productivity, an inverse relationship between farm or plot size and productivity has been extensively documented in low-income countries. This negative relationship is commonly attributed to labor market imperfections and transaction costs related to hiring and supervising labor. Some recent studies, however, argue that the relationship between farm productivity and scale is U-shaped, with the smallest farms being more productive than somewhat less small farms but with increasing returns to scale among larger farms (Foster and Rosenzweig 2022,

[8] Here we are using a practical definition of economies of scale. See Ellis (1993) for both a practical assessment and a theoretical examination of economies of scale across all factors of production in smallholder-dominated farming systems

Muyanga and Jayne 2019, Omotilewa, et al. 2021). The higher productivity of larger farms is commonly attributed to their use of agricultural mechanization and irrigation and their higher intensity of input use (Ameye, et al. 2025, Foster and Rosenzweig 2022, Muyanga and Jayne 2019).

The potential for economies of scale in crop production in an anchor enterprise partnership is therefore most obvious where partners have adjoining farmland to which agricultural mechanization or large-scale irrigation can be applied. This is, for example, the case for smallholder cooperatives in the Lower Shire Valley producing sugarcane for large-scale neighboring sugar and ethanol enterprises. Economies of scale might also be obtained in the production of field crops suitable for mechanized farming, such as cereals, oilseeds, or grain legumes. However, depending on the geographical spread of the partners and their plot sizes, shared use of the agricultural machinery may not be efficient or feasible.

Economies of scale in anchor enterprise models in Malawi are likely primarily achieved in activities that are supportive of production, rather than directly in production itself (Ma and Sexton 2021). This includes, for example, spreading the costs deriving from investments in transport, storage, or processing equipment, and securing better prices through the coordination of bulk input and services procurement and output sales. A successful anchor enterprise can be expected to have better access to input suppliers and agricultural financial service providers. This will enable the enterprise to obtain inputs at relatively lower prices. Similarly, the enterprise is more likely to have commercial relationships with output buyers who can offer somewhat higher prices than can be obtained in the spot agricultural markets frequented by farming households. However, the smallholder partners are also essential to achieving these economies of scale, as the increased aggregate demand for inputs and supply of outputs will facilitate both lower-cost input and higher-value output market transactions, all coordinated by the anchor enterprise. Through their partnership with the enterprise, the smallholder partners in the anchor enterprise scheme should be able to reduce their average costs per unit of output, increase the average prices they receive for their output, and achieve greater commercial success.

Past attempts in Malawi to achieve such economies of scale from jointly obtaining inputs and selling their agricultural outputs in large aggregate quantities through farmer organizations have had limited success. Farmer cooperatives in Malawi generally have not been able to build sustainable businesses, since doing so requires higher levels of business management capacity than can generally be found in rural farming communities (Davis, et al. 2023, Saitone, Sexton and Malan 2018). To some degree, the current interest in anchor enterprise models in Malawi's agrifood sector reflects a search for a more viable alternative to cooperative models of commercial smallholder agricultural production. The commercial success of some of the established enterprises in Malawi suggests they have the necessary management skills, making the anchor enterprise model centered on these firms a more viable pathway to realize these economies of scale.

Other expected benefits

So far, our examination of the economic rationale for anchor enterprise models has focused on economic efficiency considerations. However, in the context of rural Malawi, the business case for the larger enterprise to form an economic partnership with smallholders can also be based on other expected benefits. Collaborating with smallholder farmers can help anchor enterprises establish and maintain supportive community relations. This can hold economic value for the anchor enterprise by preventing or mediating issues of theft, property damage, and other crime or security incidents on the premises of the anchor enterprise. More broadly, partnering with smallholder farming households can

help enhance the enterprise's image and foster goodwill with both local government agencies and the national government. The national and international public image of the anchor enterprise can be supported through such partnerships. As noted, the establishment of IPSs by the international tobacco-buying enterprises operating in Malawi was in response to both domestic and international factors. One of these was continuing international criticism of the poor and possibly illegal labor practices used in Malawi to produce the leaf that the enterprises sold globally. Partnering with smallholder producers through IPS enabled the tobacco-buying firms to demonstrably reduce the use of those labor practices in the production of the tobacco they obtained in Malawi (USDL 2024), thereby dampening some of those criticisms.

ESTABLISHING CONTRACTUAL EXPECTATIONS AND MANAGING CONFLICT

Any economic partnership will involve expectations regarding the contributions and activities of each partner, as well as how the profits and losses realized will be shared between them. When those expectations are not met, conflict will result. While the interests of the enterprise and its smallholder partners will generally be aligned, situations will arise where they are not, particularly following either production or market shocks that affect the economic performance of their commercial partnership. How will these conflicts be managed to enable the partnership to continue in a manner that continues to provide benefits to both parties? Moreover, the capacity of the larger enterprise to assert its own interests over those of the smallholders in any conflict resolution process is likely significantly greater. With these power differentials, is it possible to sustain their joint operations when the partners are in conflict?

A contract is inherent to any commercial relationship, whether simply a one-off market transaction or, as here, a partnership of a large enterprise with neighboring households involving recurrent transactions. The mutually agreed-upon expectations of the parties in entering into the relationship constitute the contract, even if those expectations may not be explicitly stated or formalized. Each party's expectations are based on their personally defined objectives. At the same time, they will also seek to reduce any opportunistic behavior on the part of the other party that would undermine the advantages they might derive from the commercial relationship.

Breaches of the contract in anchor enterprise arrangements, whether explicit or implicit, can take several forms. Enterprises may break contracts by failing to deliver inputs or other services on time, refusing to purchase the product after harvest, or arbitrarily raising quality requirements. Smallholders, in turn, can default due to production failure, by selling the inputs provided by the enterprise, or side-selling to take advantage of higher or faster payments or to avoid repaying credit. The problem of side-selling is especially common. Incentives for such side selling will be particularly strong since the alternative buyer does not need to factor into the price they offer the smallholder the recovery of the cost of the inputs or other technologies that were provided by the anchor enterprise to the smallholder.

Given the conceptual centrality of contracts to such transactional partnerships in commercial agriculture, Malawi's Ministry of Agriculture has invested considerable effort in developing a Contract Farming Strategy. While pertinent to most contractual relationships in agriculture, the strategy is primarily intended to govern commercial relationships between producers and off-takers that involve a formal contract stating the quantity and quality of the produce to be produced by the farmers and the price to be paid by the off-taker. The first version of the strategy was adopted in 2007 (MoAFS 2007).

However, this was soon revised in part because the rapid development of IPS in the tobacco sector required changes to the strategy. A second version was adopted in 2017 (MoAIWD 2016b), which has since been the subject of several critiques (Prowse and Grassin 2020, ch. 6, Comstock, et al. 2019). Moreover, the institutional architecture proposed by the Contract Farming Strategy for providing oversight of contract farming relationships in Malawi is still not in place at the district and lower administrative levels.

With limited effective official oversight, any commercial partnerships between anchor enterprises and smallholder farmers will have fragile legal foundations, which could then result in considerable conflict emerging between the partners. In the absence of effective legal checks on either partner engaging in opportunistic behavior and with limited mechanisms in place to assist in resolving the resultant conflict, the sustainability of commercial partnerships could be at risk. However, even in the absence of a strong legal framework aligned with the current Contract Farming Strategy, other elements can serve to contribute to the partners acting in good faith with each other, thereby preventing conflicts from arising.

- **Strong economic rationale and clear benefits for the partners.** Agreements can be self-reinforcing when both parties stand to lose by breaking the relationship, and there is a strong economic rationale for both parties beyond the short term. This is most likely when the partnership is grounded in bilateral dependency. As discussed, this dependency in a commercial relationship commonly develops when the product at its center has few alternative suppliers, buyers, or uses. In such cases, the reduction in transaction costs provides strong incentives for the partners to maintain a longer-term commercial relationship. If the partnership dissolves in conflict, it will be costly for the farmers to find a new buyer for the product they offer and for the enterprise to find new suppliers. As an example of this, despite not having formal contracts with outgrowers, Malawi Mangoes has faced few problems with side-selling. The highly perishable nature of mangoes means that farmers cannot easily find alternative buyers on time. For its part, Malawi Mangoes cannot easily source the specific varieties of mangoes they require from other farmers.

  Even when farmers can easily find alternative buyers, continued access to valuable services and technologies can create sufficient incentives for smallholders to uphold agreements. When the expected returns from these technologies are high, or when the technologies are specific to the relationship and the product, farmers are also less likely to divert inputs (Swinnen and Kuijpers 2019). This element is central in IPS tobacco production and the Pyxus groundnut partnership. In the years those operations were launched, repayment rates for the input packages were reported to be less than 50 percent. However, in subsequent years, they quickly climbed to 80 percent or higher. Smallholders who did not repay were excluded. Those who repaid, beyond simply honoring their commitment to the tobacco-buying enterprises or Pyxus, also clearly recognized the value of the inputs and the agricultural advisory services that they received on credit. Those inputs and other services are either of higher quality or were provided at a lower cost than those that smallholders might obtain on their own. While smallholders participating in these programs sign a detailed formal contract, in maintaining the commercial partnerships, several informants judged this formal legal process as secondary to the financial value that participating smallholders ascribe to the inputs provided. The risk of cancellation of that benefit on its own is sufficiently motivating for most participating smallholders to honor their obligations under the partnership.

- **Screening and monitoring.** Accurate screening of partners and close monitoring – supported by sufficient field staff who regularly interact with farmers – further reduces the risk of default and prevents conflict. Identifying good smallholder partners for anchor enterprise operations requires a

personalized approach. This can involve relying on local traditional authorities who will be unlikely to endorse a partnership with an unsuitable smallholder. It is also common for anchor enterprises to partner only with those farmers who comply with some minimum requirements that they deem necessary for successful production. With a national digital identification system now being created for Malawi, a comprehensive credit reporting system could be developed in the coming years. This information would help exclude those who have previously violated the terms of their contract. However, until then, collecting relatively detailed personal information on potential business partners will be required.

Having sufficient field staff also enables relatively high-frequency contact with smallholders participating in the programs. This enables any emerging conflict to be addressed through early interventions by the enterprise to support the farmers in addressing them quickly, thereby resolving the problems while they are still manageable.

- **Transparency and clear communication.** Transparency is key to preventing conflict. Poor understanding of the terms of the partnership agreement can generate distrust and dissatisfaction that results in conflict that may culminate in default or drop-out. Contracts should be written in accessible language and explained clearly to smallholder farmers. If partners have limited information about the terms of loans into which they enter, this raises the risk they face of indebtedness and becoming locked into a relationship that may not be beneficial to them (Ruml and Qaim 2020). Disputes related to the weighing or grading of products are also common. Independent quality verification has been shown to strengthen trust and even increase farmers' investments in production (Saenger, Torero and Qaim 2014).
- **Effective intermediaries.** Intermediaries that help organize farmers, such as cooperatives or other farmer organizations, can also help prevent and mediate conflict. The engagement and oversight of these intermediaries can increase farmers' bargaining power, facilitate communication, and provide a forum for any grievances arising from commercial partnerships. Group-based loan repayment mechanisms can also reduce the risk of default. In Malawi, however, many farmer organizations remain at an infant stage with limited management capacity and weak governance (Davis, et al. 2023), making it difficult for them to fulfill this role in an anchor enterprise model effectively. While the Satemwa tea estate has, for example, partnered with farmer organizations in tea production, it continues to maintain individual farmer contracts to ensure smooth implementation of its outgrower operations.

That formal contracts are important but not central to anchor enterprise operations in Malawi ideally will reflect that such operations are grounded in bilateral dependency between the anchor enterprise and its smallholder partners. This interdependence requires some flexibility in how contractual expectations are interpreted. Formal contracts will always be incomplete. They cannot anticipate every issue that may disrupt the smooth operation of the commercial partnership. Relying on the courts or other formal legal institutions to arbitrate these problems will be costly with likely uncertain outcomes. Instead, conflict resolution is generally more effective when handled directly by the partners themselves, who have both the material incentives stemming from their bilateral dependency and the context-specific knowledge needed to address the underlying issue. On their own, they should generally be more capable of resolving any conflict more effectively than any lawyer, judge, local traditional authority, or other legal arbiter. For example, where a partner made good faith efforts, but the desired production or other contractual expectations still were not achieved, those involved in the partnership would understand that no opportunistic behavior was at play. Judicial authorities would be less likely to

recognize this. That both partners recognize that they each were acting in good faith should result in some forbearance and renegotiation of expectations between the partners to avoid similar problems arising in the future,[9] rather than seeking a punitive remedy, as the formal justice system might impose.

Williamson (2002) suggests that when the nature of the economic relationship moves away from one-off transactions in a competitive market to an economic partnership, as is the case with anchor enterprise relationships, then the contract is better viewed as a framework for resolving disputes. If treated as a framework rather than a more prescriptive document, the contract can guide the resolution of conflict between the partners across a wider range of problems than could be addressed by relying solely on the text of the contract. The contract, when viewed as a somewhat loose framework, provides greater flexibility for guiding the operations of the enterprise under changing economic circumstances and for resolving any problems in the partnership that may arise in consequence. This expansive view of the contract's function is appropriate for partnerships between anchor enterprises and smallholder farmers in Malawi and appears to have been generally adopted in practice.

However, one of the main reasons that these somewhat informal foundations can be adequate to sustain anchor enterprise models is that, in most cases, what is at stake if expectations in the commercial relationship are not met is often relatively small. If a smallholder fails to repay the inputs provided on credit, the partnership between the anchor enterprise and the individual smallholder will end. While this could be damaging for the smallholder in question, the other partnerships in the anchor enterprise operation will continue, since the enterprise can likely absorb the loss of one partner so long as other smallholder partners honor expectations under the partnership. Overall, even if the informal contracting and conflict resolution mechanisms do not work to sustain an individual partnership in such cases, the damage associated with a single commercial relationship ending within an anchor enterprise scheme is relatively limited.

However, where the scale of damage resulting from any breakdown in the commercial anchor enterprise partnership is significantly larger, such informal mechanisms are unlikely to be sufficient. This would be the case for the two partnerships between the sugarcane processors and the farmer cooperatives in the Lower Shire Valley. With the anchor enterprises committing significant resources to bring into their production processes the sugarcane produced on the cropland of the cooperatives, informal mechanisms to handle any conflicts between the partners will not be acceptable. Where the smallholder partners as individuals define the size of the risk, the informal mechanisms may be appropriate. However, where both partners in the anchor enterprise scheme are effectively large enterprises, formal conflict resolution mechanisms that generate legally binding actions will be required to manage potential risks arising from unmet expectations in such partnerships. The damages arising from not meeting expectations in such partnerships are too high.

Finally, the discussion has so far mostly focused on conflict arising from a smallholder partner not meeting the expectations of the anchor enterprise. However, the anchor enterprise may also fail to meet its obligations to its smallholder partners by engaging in opportunistic behavior at their expense. Examples include providing poor-quality inputs or not providing inputs in a timely manner, renegotiating the price upon delivery, or sourcing products from other suppliers rather than their smallholder partners. Another way in which an enterprise might act in bad faith towards smallholder partners would be if the

[9] In managing problems related to contractual non-performance in a partnership despite good-faith efforts, agricultural insurance or other insurance products may also offer a solution to safeguard the enterprise when such problems arise.

partnership is designed and implemented in a way that results in a smallholder being locked into an economic relationship with the enterprise that is found, over time, not to be beneficial to them.

Especially increased access to inputs on credit raises the risk of indebtedness, resulting in smallholder farmers not being able to readily opt out of contracts that are not profitable for them (Ruml and Qaim 2020). The use of tenants for tobacco production in Malawi provides an example of this. While potentially quite beneficial for the tenant and an effective way for the estate owner to mobilize labor, the practice is open to abuse. The tenant is provided with a range of inputs by the estate owner, including consumption items for the use of their household while farming the estate's land. The costs the estate owner incurred in supplying farm inputs and consumption items are then to be recovered from the sales of the tobacco the tenant produced. But, if the production of the tenant was low, the debt is maintained into the following cropping seasons, potentially enabling the estate owner to lock in the tenant's labor. While such outcomes are most commonly a result of bad luck in the farming activities of the tenant, dishonest estate owners in bad faith may seek those outcomes by design.[10]

The locking of smallholders into a partnership with an enterprise can also happen in more benign ways. If the crop at the center of the anchor enterprise arrangement is a tree crop, any smallholder will necessarily be locked into the partnership arrangement for several years while the tree crop matures before they obtain any direct benefits from production (Minot and Sawyer 2016). How the partners will be sustained and, in a sense, recompensed for the shorter-term opportunities they are not able to pursue on their land due to having placed it into tree crops should form a part of the contractual arrangements of partnerships centered on such crops.

Given the importance of these various dimensions of power differentials between the anchor enterprise and the smallholder partners in legal outcomes, the interests of smallholders will be better served in their commercial partnerships with large enterprises if those partnerships are designed in a manner that emphasizes the bilateral dependency of the partners. With such a design, if either partner tries to cheat the other, the pain is felt by both. Without an effective set of institutions in place to balance these power differentials, reliance on contracts and other legal mechanisms alone holds a risk that the more powerful partner can walk away from the anchor enterprise relationship that is in conflict with no consequences for any breach of contract, beyond possibly some reputational tarnish.

ARE ANCHOR ENTERPRISE MODELS SUITED FOR INCLUSIVE ECONOMIC DEVELOPMENT?

There are several challenges to achieving inclusive development using the anchor enterprise model. First, establishing a stand-alone private enterprise engaged in agricultural production, agrifood processing, or marketing in Malawi is inherently difficult (Mwatsika 2021, Engel, et al. 2026). Poor harvests, unreliable factor, input, and output markets, episodes of macroeconomic disorder, uncertainty in international trade, and domestic policy changes all contribute to high rates of failure in new agrifood sector businesses. Private agri-food enterprises that manage to succeed are therefore already exceptional. Moreover, anchor enterprise models are not profitable or sustainable for many types of commercial agricultural production in Malawi. As a result, only a small portion of farming households can realistically be expected to participate in anchor enterprise arrangements.

[10]Given how common the perspective is that abuse is rife in tenant arrangements, the government has taken steps to ban tenant labor in tobacco production (USDL 2024). However, those regulatory efforts have so far had limited effect. The use of tenants remains widespread (ILO 2024).

Second, although commercial partnerships between anchor enterprises and smallholders can work well, the poorest and most vulnerable smallholder farming households are less likely to participate. A partnership with a large enterprise will often carry risks for the smallholder farmer partners that relatively larger or richer farmers are likely better able to manage and cope with. Similarly, partnerships with smallholders introduce additional risks for the enterprise, whether related to production shocks, changing market conditions, policy shifts, or reputational damage. To manage these risks, enterprises can be expected to be selective in choosing partners, favoring farmers who are more motivated, knowledgeable, and productive. The poorest and most vulnerable households generally lack the knowledge, entrepreneurial abilities, and economic resilience that would make them good business partners in an anchor enterprise scheme. They are unlikely to consistently meet the explicit or implicit expectations of an anchor enterprise partnership. These considerations tend to result in the exclusion of the poorest and most vulnerable farming households from such schemes (e.g., Minot and Sawyer (2016)).

For an enterprise, working with fewer, relatively larger smallholder farmers is also less costly. It reduces transaction costs associated with negotiation, as well as the expenses of providing technical assistance, distributing inputs, or collecting the harvest. On the other hand, working with a larger number of smallholders can be part of a risk diversification strategy for an anchor enterprise, since spatially dispersed smallholders will have different levels of exposure to pests, diseases, or even local weather shocks. While the practical challenges of working with a large number of smallholders are significant, these can possibly be mitigated when another organization, such as a farmer cooperative, serves as an intermediary.

Directly achieving more inclusive development outcomes through an anchor enterprise arrangement would require that the anchor enterprise select partners with less attention to their potential for contributing to the profitability of their commercial partnership and more attention to whether a successful partnership will significantly improve the welfare of the smallholder farming household and even bring them out of poverty. From a commercial standpoint, using these criteria is difficult to justify, particularly if it excludes smallholders who are more motivated and entrepreneurial and who may only have a slightly better level of welfare than those such criteria would privilege.

Nonetheless, poorer households may still benefit indirectly from the operations of anchor enterprises in their communities. A central rationale for supporting such private-sector-led approaches is the spillovers that productive and profitable anchor enterprise operations will have on the local economy. When anchor enterprise models are successful, they can generate wider benefits for the local economy. The operations of the anchor enterprise and its partners can, for example, attract more traders and investments in local infrastructure, improving market access for all farmers in the area. Non-participating farming households may also benefit from improved availability of inputs and services, or knowledge and technology spillovers. However, evidence suggests that poorer households are often less able to capture these spillovers than better-resourced households (Chamberlin and Jayne 2020).

Higher labor demand from both the anchor enterprise and its smallholder partners can also expand more local employment opportunities. In addition, rising incomes of participating households can stimulate local economic growth. As their incomes increase, so does their consumption of goods and services – many of which are supplied by non-participating local households. These products tend to be labor-intensive, require limited capital in their production, and typically are not marketed outside of the local community: construction, building repair, and associated services; transport and associated

services; education, health, and other social services; furniture and handicraft-making; and food and beverage processing. As demand for these goods and services rises, local non-farm employment and productivity will also then increase, propelling further growth in the local economy (Mellor 2017, Haggblade, Hazell and Reardon 2007). Through this local economic growth, poorer households in the community should also see welfare improvements indirectly, whether through increased income-generating opportunities or through greater availability of locally produced goods at lower prices.

CONCLUSIONS

Larger-scale farms or agro-processors act as anchor enterprises when engaging in commercial partnerships with smallholder farming households. In specific contexts and for specific products, such partnerships can be mutually beneficial and commercially successful as they help reduce transaction costs, overcome market failures, and realize economies of scale.

Sustainable anchor enterprise partnerships in Malawi emerge from a combination of both context-specific and production-specific factors.

- Markets in rural Malawi for factors of production – land, in particular, but also labor and capital – are quite thin and ineffective in providing enterprises and smallholder farming households with the factors they require for their production processes. Enterprises entering into partnerships with smallholder farming households can gain better access to both land and labor, while smallholder households often can gain improved access to agricultural financing, productive inputs, knowledge and information, and more remunerative output markets through their enterprise partner.
- However, the characteristics of the agricultural product at the center of the anchor enterprise model are important to the sustainability of the partnership. Here, what is important is the degree to which it is specialized for a specific producer or production process and cannot be easily redirected to others without loss of value. Anchor enterprise partnerships are most likely to be economically justified for higher value, less widely grown, more specialized, more complex to produce or process, or highly perishable agricultural products. The model is generally not suitable for grain or other generic staple crops. For such products, partnerships are more costly and carry high risk since farmers can easily find and sell to other buyers than their anchor enterprise partner if market prices rise above the agreed price for the partnership (*side-selling*). Similarly, if market prices drop below the agreed price, enterprises may buy elsewhere (*side-buying*). The low asset specificity of transactions centered around these products means that there are limited incentives for the enterprise and its smallholder partners to resolve any conflicts that might arise between them to maintain their commercial partnership over the long term.
- Anchor enterprise models make the most sense when there are potential economies of scale. Especially in the absence of land consolidation that would allow for large-scale irrigation or mechanized farming, such economies of scale in anchor enterprise models in Malawi are likely primarily achieved in activities that are supportive of agricultural production, rather than directly in production itself. Fixed costs deriving from investments in transport, storage, or processing equipment can be spread over larger volumes of output. The commercial expertise of the enterprise, its coordination of bulk input and services procurement and output sales for both its own account and those of its smallholder partners, and stronger market access can lower input costs and increase returns for all parties in the partnership.

The legal framework governing commercial partnerships in the agrifood sector in Malawi remains underdeveloped. While this limited legal oversight and control could be expected to result in anchor enterprise arrangements in Malawi dissolving when conflicts inevitably arise, formal contracts were found to be important but not central to anchor enterprise operations. Although some anchor enterprise operations examined use formal contracts to specify the performance expectations for both the smallholder farming households and the anchor enterprise, as well as how any conflicts between the partners are to be managed, formal contracts do not appear to have much weight in sustaining the partnerships. Rather, the partnerships that are successful are built on a strong economic rationale, provide significant and clear financial incentives for all partners, and exhibit some degree of bilateral dependency. The functional importance of any contract for the anchor enterprise partnership lies not in the details of its text but more in serving as a framework that can be used flexibly to guide any changes in expectations among the partners or to manage any conflicts that arise without putting the overall partnership at risk.

Many conflicts between partners in an anchor enterprise arrangement can be averted through good screening of prospective partners, transparent and clear communication, and frequent information sharing, and can often be resolved independently without recourse to Malawi's legal and administrative institutions. However, the fact that the conflicts can be managed outside of a legal framework in part reflects the significant asset and power differences between the anchor enterprise and its smallholder partners and implies the latter are likely at a disadvantage. To allow for appeals to a third party if a partner feels that they have been dealt with unfairly in such situations of conflict, a legal framework providing oversight on such partnerships should be established.

Anchor enterprise models cannot be profitably and sustainably employed for many types of commercial agricultural production in Malawi. Consequently, only a small portion of farming households can directly participate, and generally, the poorest and most vulnerable are less likely to be included. Nonetheless, where such models work well, they can deliver indirect benefits to the broader rural community, including its poorer and more vulnerable members, by stimulating local demand for labor, goods, and services.

While likely better suited for commercial agricultural development than inclusive rural development, anchor enterprise models can be valuable for development in Malawi. A model centered around commercial farms or agro-processors, however, requires an enabling environment for such enterprises to operate effectively.

- This includes macroeconomic stability and an investment climate that facilitates private investment in agribusiness sectors.
- Anchor enterprise models are especially suited for export-oriented production. However, the current policy environment in Malawi for trade, including the exchange rate policy, is largely unfavorable for formal exports (Changaya, et al. 2026). When exchange rates better reflect market conditions and other export restrictions are removed, formal exporters can offer more competitive farm-gate prices. This reduces the risk of side-selling to informal traders and improves the viability of anchor enterprise models.
- Strengthening agricultural input supply, processing, domestic marketing, and trade in the agrifood value chains of which anchor enterprises are a part will enhance the business prospects for the anchor enterprise and its partners.

- The viability of partnerships with geographically dispersed smallholder farmers is constrained by poor rural infrastructure. Improved rural roads reduce the cost of distributing inputs, organizing extension services, and collecting harvests.

To be sustainable, anchor enterprise models should be grounded in a strong economic rationale for partnering. Government, development partners, and civil society organizations have several options to support such partnerships without eroding their commercial foundations.

- *Invest in new institutions* to safeguard the individual interests of participants in anchor enterprise schemes and their capacity to operate effectively. The mission of such institutions will center on conflict prevention and resolution. Their activities could include developing model contracts for anchor enterprise partnerships, offering training on how those contracts can be used to make commercial partnerships more sustainable, and convening effective forums in which grievances can be aired and third-party mediation mechanisms brought in to assist in resolving conflicts.
- *Provide assistance in managing relationships with smallholder partners*. Many enterprises are not well-equipped for or experienced in dealing with smallholder farmers. They typically engage in relationships with less marked power imbalances where contracts can be more readily enforced. Managing relationships with smallholders may require different skills and dedicated systems. Assistance could range from the development of contracts to training in relationship management to setting up data systems to track input deliveries, sales, and repayments.
- *Organize financial and business training for smallholder farmers* to reduce some of the information asymmetries that are commonly seen between the generally well-informed anchor enterprise and its potential partners. This type of training could help ensure that farmers understand the terms of the partnership agreement, are able to assess the risks involved, and prevent indebtedness and other forms of lock-in.
- *Support organizations, such as cooperatives or non-governmental organizations, which can act as third-party intermediaries.* These can facilitate effective communication between the smallholder farmers and the anchor enterprise, help coordinate and enforce loan repayment and product delivery, manage grievances, and mediate conflicts. As they reduce the costs for an anchor enterprise scheme of dealing with many smallholders, effective intermediaries can allow for more inclusive anchor enterprise models.
- *Develop effective grades or standards and/or organize third-party certification of quality*. Quality control is often a contentious issue in contract farming. The establishment of grades and standards of agricultural outputs that are easy to implement will facilitate communication and help avoid conflicts and mistrust. Alternatively, organizing a third party to assess and verify the quality independently can help prevent or resolve such disputes.
- *De-risk partnering with smallholder farmers*. Even when the business case is strong, significant levels of risk are inherent to working with smallholder farmers relying on rainfed production. Agricultural insurance or other insurance products may offer a solution to safeguard enterprises when smallholder farmers default because of production failure.

Finally, to ensure that anchor enterprise models contribute meaningfully to inclusive development, government, development partners, and civil society organizations can consider complementary interventions aimed at strengthening the ability of the poorest households, in particular, to capture some of their indirect benefits. Such interventions could focus on easing some of the constraints that

limit their participation in emerging opportunities following from growing local demand for labor and goods and services. This, for example, includes improving their access to productive assets, market information, or finance and addressing skills and knowledge gaps.

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