

Impact of the Millennium Challenge Corporation on Malawi's Foreign Direct Investment (FDI)

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Abstract: This thesis examines the impact of the Millennium Challenge Corporation (MCC) on Foreign Direct Investment (FDI) inflows into Malawi. The MCC is a United States government development agency established in 2004 to assist developing countries in reducing poverty through sustainable economic growth. Malawi has been a beneficiary of two MCC compacts: a USD 350.7 million Energy Compact signed in 2011, and a USD 350 million Transport and Land Compact signed in 2022. Both compacts targeted structural barriers to investment, including energy deficits, infrastructure inadequacies, and governance challenges.

The study employs a mixed-methods approach, combining qualitative data from key informant interviews, focus group discussions, and direct observation with quantitative analysis of FDI trend data drawn from the World Bank, IMF, UNCTAD, and the Reserve Bank of Malawi. The analytical framework applies OECD-DAC evaluation criteria alongside SWOT and PESTEL analyses to assess the compact's relevance, effectiveness, efficiency, and impact on Malawi's investment climate.

The findings reveal a paradox: despite meaningful achievements in energy sector reform, infrastructure development, and institutional strengthening, FDI inflows into Malawi declined over the MCC implementation period. The study attributes this outcome to a convergence of factors that overwhelmed the compact's positive contributions, including recurring political instability, extreme weather events, macroeconomic fragility, COVID-19, geopolitical shocks, and Malawi's weak position in bilateral investment diplomacy.

The thesis concludes that the MCC Compacts targeted the right structural constraints, and the reforms achieved in the energy sector in particular represent genuine and lasting progress. However, their impact on FDI was undermined by external shocks and systemic vulnerabilities that fell outside the programme's scope. The study recommends a coordinated policy response addressing political resilience, human capital development, regional economic integration, infrastructure investment, and Malawi's expanding international investment treaty network.

Keywords: Foreign Direct Investment, Millennium Challenge Corporation, Malawi, energy sector reform, investment climate, sub-Saharan Africa, OECD-DAC evaluation

1. Introduction

1.1 Background to the Study

Foreign Direct Investment (FDI) has long been regarded as a catalyst for economic transformation in developing countries. By channelling capital, technology, managerial expertise, and access to global markets into host economies, FDI can accelerate growth, create employment, and expand the productive base in ways that domestic investment alone cannot achieve. For least developed countries (LDCs) like Malawi, attracting

FDI is not merely an economic ambition but a development imperative, given the country's structural dependence on foreign aid, narrow export base, and persistent fiscal constraints.

Malawi is a landlocked country in sub-Saharan Africa with a population of approximately 20 million people. It consistently ranks among the world's poorest nations, with per capita income well below the regional average and a poverty headcount ratio exceeding 70 percent at the USD 2.15 per day threshold. Agriculture dominates the economy, contributing over 80 percent of export earnings through commodities such as tobacco, tea, and sugar, while the manufacturing and services sectors remain underdeveloped. Chronic energy deficits, deteriorating transport infrastructure, and governance challenges have historically restrained private sector growth and discouraged foreign investors.

Since the transition to multiparty democracy in 1994, successive Malawian governments have pursued FDI as a vehicle for economic diversification and poverty reduction. Various investment promotion frameworks were established, including the Malawi Investment and Trade Centre (MITC) and successive national development plans culminating in the long-term vision document Malawi 2063. Despite these efforts, FDI inflows into Malawi have remained stubbornly low relative to regional peers, constrained by an unfavourable investment environment characterised by energy unreliability, poor road and rail infrastructure, political instability, and limited institutional capacity.

It is within this context that the Millennium Challenge Corporation (MCC) entered Malawi's development landscape. The MCC is a United States government foreign assistance agency created by the Millennium Challenge Act of 2003 and operationalised in 2004. Its founding philosophy distinguishes it from conventional aid: rather than disbursing funds through government budget support, the MCC operates through time-bound performance agreements called compacts, which are co-designed with eligible countries based on demonstrated commitment to good governance, economic freedom, and investment in people. Eligibility is determined through a rigorous scorecard that assesses countries against indicators drawn from internationally recognised sources, including Transparency International, Freedom House, and the World Bank.

Malawi's engagement with the MCC began with a threshold programme focused on reducing public corruption and strengthening fiscal management. Following improvements in its scorecard performance, Malawi qualified for a full compact in 2011, receiving USD 350.7 million to overhaul its power sector. This Energy Compact targeted a core constraint to private investment: the country's inability to generate sufficient, reliable, and affordable electricity. At the time of the compact, Malawi could generate only 284 megawatts against a projected demand of 478 megawatts by 2015, and power outages lasting eight to twelve hours per day were common, costing businesses and households hundreds of millions of dollars in lost productivity.

A second compact, the Malawi Transport and Land Compact (MTLC) worth USD 350 million, was signed in 2022. This agreement addressed complementary investment barriers through three interconnected projects: the Accelerated Growth Corridors Project, which aimed to improve feeder road access for agricultural producers; the American Catalyst Facility for Development, designed to unlock private investment through the United States Development Finance Corporation; and the Land Productivity Project, which sought to improve land markets and tenure security.

Given the scale of the MCC's engagement with Malawi and the explicitly investment-oriented rationale underlying its programme design, this thesis poses a central question: to what extent have the MCC Compacts contributed to an improvement in FDI inflows into Malawi? The study situates this question within a rigorous examination of FDI trends before and after 2011, an assessment of the investment climate changes attributable to the compacts, and an analysis of the structural, political, and macroeconomic factors that moderated the programme's impact.

1.2 Organisation of the Study

The thesis is structured across four chapters. Chapter 1 provides the background, problem statement, research objectives, scope, and theoretical framework. Chapter 2 presents a comprehensive literature review covering FDI theory, the MCC's operating model, and the specific dynamics of FDI in Malawi and sub-Saharan Africa. Chapter 3 describes the research methodology, including data collection instruments and analytical tools. Chapter 4 presents the findings, discussion, and conclusions, followed by policy recommendations drawn from the evidence.

1.3 Significance of the Study

The study contributes to the scholarly and policy debate on the effectiveness of performance-based development assistance in attracting FDI to low-income countries. While a growing body of literature examines the macro-level determinants of FDI in Africa, comparatively few studies apply an impact evaluation lens to the relationship between specific aid interventions and investment outcomes in individual countries over time. This thesis fills that gap in the context of Malawi.

From a policy perspective, the findings are directly relevant to Malawian government planners, MCC programme designers, and development partners engaged in investment promotion. By identifying which compact components contributed most meaningfully to improvements in the investment climate, and which external factors undermined those gains, the study offers actionable insights for future programme design. More broadly, the Malawi case provides lessons applicable to other LDCs contemplating engagement with performance-based aid mechanisms.

1.4 Problem Statement

Despite two successive MCC compacts totalling approximately USD 700 million and a series of significant governance, energy, and infrastructure reforms, Malawi has not experienced a commensurate increase in FDI inflows. Between 2011 and 2022, FDI as a share of GDP declined, and the country continued to attract substantially less foreign investment than comparable neighbours such as Mozambique and Tanzania. This disconnect between reform effort and investment outcome raises a fundamental empirical question: why has Malawi's ambitious development partnership with the MCC not translated into a sustained improvement in FDI performance?

1.5 Aim of the Study

The overarching aim of this thesis is to assess the impact of the MCC Compacts on FDI inflows into Malawi, with a view to understanding both the direct contributions of the programme and the broader structural and contextual factors that shaped the investment environment during the implementation period.

1.6 Objectives of the Study

The study pursues four specific objectives:

- To assess the extent to which the MCC Compacts improved Malawi's investment reputation and ranking.
- To analyse FDI inflow trends in Malawi before and after the inception of the MCC, with reference to GDP performance.
- To identify and evaluate the structural, political, and economic factors that influenced FDI outcomes during the MCC implementation period.
- To formulate evidence-based recommendations for future investment promotion programming in Malawi.

1.7 Scope of the Study

The study covers the period from the late 1990s to 2022, providing a historical baseline of FDI performance before the MCC and a post-compact assessment window. The primary focus is on the 2011 Energy Compact, with supplementary consideration of the 2022 Transport and Land Compact. The analysis draws on data from Malawi and selected regional comparators, including Mozambique, Tanzania, and Zambia, to contextualise performance trends. The study focuses on macro-level FDI flows rather than firm-level investment decisions, and on structural and institutional determinants rather than sector-specific investment strategies.

Table 1.1: Study Timelines

Phase	Focus	Period
Pre-MCC baseline	FDI trends and investment climate prior to MCC engagement	1996-2010
MCC threshold programme	Governance reforms and fiscal management improvements	2006-2011
Energy Compact	Power sector reform, infrastructure investment, institutional changes	2011-2018
Post-compact assessment	FDI trends, sustained impact, and identification of mitigating factors	2018-2022
Transport and Land Compact	Road infrastructure, land markets, private investment facilitation	2022-present

1.8 Research Strategy

This study adopts a mixed-methods research strategy that combines quantitative trend analysis with qualitative inquiry. This approach is appropriate given the complexity of the research problem, which requires both statistical examination of FDI flows and contextual interpretation of institutional, political, and economic dynamics. The study is designed as an impact evaluation, assessing causality between the MCC programme inputs and observed FDI outcomes while accounting for confounding variables.

1.9 Research Questions

The study is guided by three principal research questions:

- To what extent have the components of the MCC Compacts improved Malawi's investment reputation and ranking since their inception in 2011?
- What has been the trend of FDI inflows relative to GDP in Malawi since the inception of the MCC, and how does Malawi's performance compare to regional peers?
- What structural, political, and macroeconomic factors explain the gap between the reforms achieved through the MCC and the FDI outcomes observed in Malawi?

1.10 Theoretical Framework

The study is anchored in two complementary theoretical traditions.

The first is John Dunning's Ownership-Location-Internalisation (OLI) eclectic paradigm, which holds that FDI occurs when three sets of advantages converge: ownership advantages specific to the investing firm, location advantages inherent to the host country, and internalisation advantages that make it more profitable to exploit those advantages within the firm than through licensing or export. Within this framework, the MCC's contributions to Malawi's energy infrastructure, transport network, and governance quality are understood as interventions designed to strengthen location advantages, thereby making Malawi a more attractive destination for foreign capital.

The second theoretical lens is Simon Anholt's National Branding Hexagon, which conceptualises a country's international reputation across six dimensions: exports, governance, culture and heritage, people, investment and immigration, and tourism. Anholt's model is relevant because investor confidence is shaped not merely by objective economic indicators but by perceptions of a country's stability, competitiveness, and openness. Malawi's ability to attract FDI depends on how potential investors perceive the country across these dimensions, and the MCC's visible reforms in governance and infrastructure can be understood as contributing to an improved national investment image. Figure 1.1 illustrates the Anholt Hexagon model as applied in this study.

2. Literature Review

2.1 Geographical Description of the Study Area

Malawi is a small, landlocked country in south-eastern Africa, bordered by Zambia to the northwest, Tanzania to the northeast, and Mozambique to the east, south, and west. The country covers approximately 118,484 square kilometres, of which Lake Malawi accounts for roughly one-fifth. Despite this substantial water body, Malawi has struggled to harness its natural endowments for economic development, and the lake's hydropower potential remains only partially developed.

The country's population of approximately 20 million is predominantly rural and agriculturally dependent. Malawi's economy is heavily reliant on rain-fed smallholder agriculture, particularly tobacco, which historically contributed over 60 percent of export earnings. This structural dependence exposes the economy to significant climatic and commodity price volatility, making macroeconomic stability difficult to sustain. The country ranks among the lowest globally on the Human Development Index and has consistently struggled to meet fiscal obligations without substantial donor support, which funds approximately 40 percent of the national budget.

Geographically, Malawi's landlocked position imposes significant logistical costs on both importers and exporters. Unlike Zambia, which has pursued multimodal transport solutions through the Tanzania-Zambia Railway (TAZARA), Malawi relies predominantly on road haulage to reach the ports of Dar es Salaam in Tanzania and Nacala and Beira in Mozambique. The Nacala Corridor, though partially rehabilitated with external assistance, remains underutilised, and the domestic railway system that once connected Malawi's economic heartland to the coast has largely ceased to function. These logistical constraints translate directly into elevated landing costs for capital goods, raw materials, and fuel, which raise the cost of doing business and weaken Malawi's competitiveness as an investment destination.

Administratively, Malawi is divided into three regions: the Northern, Central, and Southern regions, which together contain 28 districts. Economic activity is concentrated in the Central Region, particularly around the capital Lilongwe, and in the Southern Region around the commercial city of Blantyre. Malawi is a member of multiple regional economic bodies, including the Southern African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA), which in principle offer preferential access to larger regional markets. However, the practical benefits of this membership have been constrained by the country's limited productive capacity and logistical challenges.

Table 2.1: Malawi's Ranking on Selected International Indicators

Indicator	Malawi Score/Rank	Source
Poverty headcount ratio (USD 2.15/day, 2022)	70.1%	World Bank
GDP per capita (2022)	USD 672	World Bank
Human Development Index (2022)	Low – 174th of 191	UNDP
Corruption Perception Index (2022)	34/100	Transparency International
FDI inflows (2022)	USD 46.4 million	World Bank
Electricity access (pre-MCC)	Approx. 9%	MCC/World Bank

2.2 Foreign Direct Investment

2.2.1 The Growing Role of FDI in Development

The theoretical case for FDI as a driver of development in low-income countries rests on several well-established propositions. FDI brings capital resources that supplement constrained domestic savings and foreign currency reserves. It transfers technology and managerial expertise that can raise total factor productivity in host economies. It integrates host firms into global production networks, expanding market access and embedding technological learning. And it creates employment at wages that are often above the domestic mean, contributing to income growth and consumer market development.

These propositions are supported by a substantial body of empirical literature. Alfaro (2003) finds that FDI contributes differentially to growth depending on the sector, with manufacturing and services generating stronger spillovers than primary sector investments. Asiedu (2006) demonstrates that institutional quality, market size, natural resource endowments, and infrastructure availability are the principal determinants of FDI in Africa, with governance quality playing a particularly significant role. Anyanwu (2011) confirms these findings using a panel dataset spanning 1980 to 2007, and additionally identifies trade openness and regional economic integration as significant positive determinants of FDI flows to African economies.

Dunning's OLI paradigm remains the most comprehensive theoretical framework for understanding the conditions under which multinational enterprises choose to invest abroad rather than export or license. The ownership advantages of the investing firm, the location advantages of the host country, and the internalisation incentives that make direct investment preferable to market-based alternatives collectively determine the FDI decision. For host country policy, the most actionable dimension of this framework is the location advantage: governments can improve their investment attractiveness by strengthening institutional quality, reducing policy uncertainty, investing in infrastructure, and creating a regulatory environment conducive to business.

2.2.2 Determinants of FDI Inflows

The empirical literature consistently identifies several categories of FDI determinants that are particularly relevant to the Malawian context. These can be grouped into institutional, macroeconomic, infrastructural, and diplomatic dimensions.

Institutional quality is among the most robust predictors of FDI. Countries that rank highly on governance indicators, including control of corruption, rule of law, regulatory quality, and political stability, consistently attract greater volumes of foreign investment. Corruption imposes direct costs on investors through bribery, and indirect costs through institutional uncertainty, contract enforcement failures, and the misallocation of productive resources. Transparency International's Corruption Perception Index and the World Bank's Governance Indicators are frequently used to operationalise this dimension in empirical studies.

Macroeconomic stability is equally important. Investors require predictable inflation, stable exchange rates, adequate import cover, and sustainable public finances before committing long-term capital. Countries experiencing acute foreign currency shortages find that even willing investors are unable to import capital goods or repatriate profits, making investment effectively impossible regardless of the formal regulatory framework. Malawi's recurring balance of payments crises, episodes of high inflation, and exchange rate volatility have repeatedly created precisely these conditions.

Infrastructure, particularly energy reliability and transport connectivity, is a third critical determinant. Manufacturing and export-oriented investors require uninterrupted power supply and access to ports at competitive logistical costs. Malawi's chronic power shortages, which historically caused outages of eight to twelve hours per day, imposed enormous costs on existing businesses and served as a powerful deterrent to new investors. Similarly, the absence of a functional railway connection to regional ports and the high cost of road-based freight significantly eroded Malawi's competitiveness relative to coastal or better-connected neighbours.

Finally, market size and human capital quality are important determinants, particularly for market-seeking and efficiency-seeking FDI. Malawi's small population, high poverty incidence, and limited skilled

workforce constrain the domestic market opportunity and reduce the attractiveness of efficiency-seeking investments in sectors such as business process outsourcing and light manufacturing.

Table 2.3: FDI Inflows, GDP and Population in Selected African Countries (Selected Years)

Country	FDI Inflows (USD Bn)	GDP (USD Bn)	Population (m)	Year
Malawi	0.046	14.08	20	2022
Mozambique	1.97	20.62	33	2022
Tanzania	1.10	79.16	63	2022
Zambia	0.12	28.10	19	2022
Zimbabwe	0.34	26.50	16	2022

The table above illustrates Malawi's comparatively weak FDI performance relative to regional peers, despite sharing many structural characteristics with countries such as Zambia and Zimbabwe. This underperformance is central to the research problem this thesis investigates.

2.2.3 Global FDI Trends

Global FDI flows have exhibited considerable volatility over the past three decades, shaped by global financial cycles, geopolitical events, commodity price movements, and the shifting strategies of multinational corporations. Following a period of rapid growth in the 1990s driven by cross-border mergers and acquisitions, global FDI peaked in 2000 before declining sharply in the aftermath of the technology sector collapse. Flows recovered through the mid-2000s, reaching a new peak in 2007, before collapsing again during the 2008-2009 global financial crisis.

The post-crisis recovery was uneven, with emerging markets and developing economies absorbing a growing share of global FDI as investors sought higher returns in less saturated markets. Africa's share of global FDI remained persistently low despite its relatively strong economic growth performance in the 2000s and 2010s, constrained by infrastructure gaps, governance challenges, and the commodity-dependent nature of much of the continent's investment profile. UNCTAD's World Investment Reports document that Africa attracted between two and four percent of global FDI flows through most of the 2010s, with significant concentration in natural resource-rich economies such as South Africa, Mozambique, and the Democratic Republic of Congo.

The COVID-19 pandemic triggered the largest single-year decline in global FDI since the Second World War, with flows falling by nearly 35 percent in 2020. Recovery was partial and uneven in 2021, followed by renewed uncertainty in 2022 as Russia's invasion of Ukraine disrupted global supply chains, drove commodity price inflation, and tightened global financing conditions. These global shocks intersected with Malawi's domestic vulnerabilities in ways that significantly complicated the attribution of FDI trends to specific policy interventions.

2.2.4 Foreign Direct Investment in Malawi

Malawi's FDI history reflects the broader structural challenges that constrain investment in sub-Saharan Africa's least developed economies. Prior to the transition to multiparty democracy in 1994, the investment environment was characterised by pervasive state ownership, limited economic liberalisation, and a highly controlled regulatory framework that discouraged private sector entry. The democratic transition opened the door to economic reform, and the subsequent adoption of the Malawi Poverty Reduction Strategy Paper in 2002 established a framework for macroeconomic stabilisation, privatisation, and market liberalisation.

The post-transition period saw a modest increase in FDI, particularly in the telecommunications sector. The entry of Celtel as a horizontal FDI in mobile telecommunications reflected the opening of previously state-dominated sectors and the improved regulatory environment that accompanied the privatisation programme. The mining sector also attracted greenfield investment, most notably from Paladin Energy's Kayerekera Uranium Mine, which began operations in the late 2000s and represented one of Malawi's most significant FDI inflows during that period.

However, these gains were fragile and episodic. FDI inflows as a share of GDP fluctuated sharply, responding as much to political events and commodity price cycles as to structural improvements in the investment climate. Years of civil unrest in 1992, 2006, 2012, and 2019 corresponded with noticeable declines in FDI, while periods of political stability and donor engagement saw modest recoveries. Malawi has consistently attracted FDI at levels well below what its reform trajectory might have suggested, pointing to the persistence of deeper structural barriers that policy interventions have not yet fully addressed.

2.3 The Millennium Challenge Corporation (MCC)

2.3.1 The MCC Concept

The Millennium Challenge Corporation was established by the United States Congress through the Millennium Challenge Act of 2003, with the explicit mandate to reduce poverty in developing countries through economic growth. What distinguishes the MCC from traditional bilateral aid agencies is its selective, performance-based operating model. Rather than allocating assistance on the basis of strategic alliances or diplomatic considerations, the MCC selects eligible countries through a rigorous annual scorecard that assesses performance across three domains: ruling justly, investing in people, and encouraging economic freedom.

The scorecard draws on data from independent sources, including Freedom House, Transparency International, the World Health Organization, the World Bank, and the International Monetary Fund. Countries must pass more than half of the indicators in each domain to be considered eligible, and the process is explicitly designed to create incentives for governance reform prior to selection. This ex ante conditionality distinguishes the MCC from many multilateral aid instruments, which attach conditions retrospectively to disbursements. The MCC's founding rationale holds that aid is most effective when directed at countries that have already demonstrated a genuine commitment to good governance, economic reform, and investment in human capital.

Once selected, eligible countries develop compact programmes in close collaboration with MCC staff through a co-creation process that draws on comprehensive constraints-to-growth analyses. Compacts are time-bound agreements, typically lasting five years, and include binding performance benchmarks, independent evaluation requirements, and Environmental and Social Impact Assessments. The MCC's Economic Rate of Return (ERR) methodology provides a quantitative basis for prioritising investments based on their expected economic returns, with a minimum threshold of ten percent required for compact inclusion.

Table 2.4: Malawi MCC Scorecard Indicators for the 2011 USD 350.7 Million Compact

Indicator	Malawi Score	Passed?
Rule of Law	Above median	Yes
Control of Corruption	Above median	Yes
Government Effectiveness	Above median	Yes
Political Rights and Civil Liberties	Above median	Yes
Land Rights and Access	Above median	Yes
Natural Resource Management	Above median	Yes
Girls' Primary Education Completion	Above median	Yes
Health Expenditure	Above median	Yes
Immunisation Rates	Above median	Yes
Inflation	Below threshold	Yes
Regulatory Quality	Above median	Yes
Trade Policy	Above median	Yes

Source: MCC Scorecard, Fiscal Year 2018 – Malawi

2.3.2 The MCC Funding Model

The MCC's approach to investment planning relies centrally on the Economic Rate of Return analysis, which estimates the net present value of expected economic benefits relative to programme costs over a defined time horizon. This methodology ensures that compact investments are prioritised according to their expected development impact rather than political convenience or donor preferences. Projects that do not meet the ten percent ERR threshold are excluded from compact funding, regardless of their political salience.

Compact implementation is overseen by a country-level Millennium Challenge Account (MCA) entity, which operates with considerable institutional independence from the host government. This design is intended to insulate programme management from political interference and to maintain transparent procurement and financial management standards aligned with the MCC's fiduciary requirements. The MCA entity is responsible for procurement, implementation oversight, environmental compliance, and reporting against programme benchmarks.

The MCC also operates a threshold programme instrument for countries that do not yet qualify for a full compact but demonstrate potential for improvement. Threshold programmes are smaller grants, typically in the range of USD 10 to 30 million, targeted at specific governance or institutional constraints that are preventing scorecard eligibility. Malawi received a threshold programme focused on fiscal transparency and anti-corruption measures before qualifying for its first full compact.

Table 2.5: Summary of MCC Engagements with Malawi

Programme	Year	Value	Key Focus Areas
Threshold Programme	2006-2010	~USD 20m	Anti-corruption, fiscal management, IFMIS, Parliament, National Audit
Energy Compact	2011-2018	USD 350.7m	Power generation, transmission grid, sector unbundling, regulatory reform
Transport and Land Compact (MTLC)	2022-present	USD 350m	Feeder roads, land markets, DFC-catalysed private investment

2.4 The Nexus between the MCC and FDI in Malawi

The theoretical connection between MCC programming and FDI outcomes rests on the assumption that the compact's target areas, namely governance, infrastructure, and institutional reform, correspond directly to the location advantages identified by Dunning's OLI framework as determinants of investor decision-making. If the MCC successfully improves governance quality, reduces energy costs, and strengthens infrastructure, it should, in principle, enhance the attractiveness of the host country to foreign investors.

The MCC itself articulates this logic explicitly. Democratic institutions and well-functioning governance systems, the MCC argues, reduce economic volatility, curtail corruption, and improve the reliability of contract enforcement, all of which raise investor confidence. By conditioning compact eligibility on governance performance, the MCC creates pre-selection incentives for reform, and by embedding governance improvement targets within compact programmes, it seeks to lock in those improvements over the medium term.

In Malawi's case, the Energy Compact was designed with a clear causal chain: addressing energy deficits would lower production costs for existing businesses, attract new private sector investment in the power sector, and create enabling conditions for productivity growth in agriculture, manufacturing, and services. The unbundling of the state electricity utility ESCOM into separate generation (EGENCO) and transmission entities, the rehabilitation of hydropower stations, the extension of the transmission grid, and the connection of Malawi to the regional Southern African Power Pool were all intended to transform energy from a binding constraint on investment into a comparative advantage.

The 2022 Transport and Land Compact deepened this logic by addressing complementary constraints. Improved feeder road access was designed to reduce the logistical costs that made agricultural investment economically marginal in remote areas. The Land Productivity Project aimed to resolve tenure insecurities that had deterred private investment in land-intensive sectors. And the American Catalyst Facility for Development explicitly sought to leverage public compact resources to crowd in larger volumes of private investment through the US Development Finance Corporation.

Whether this causal chain translated into the expected FDI outcomes is the central empirical question this thesis investigates.

3. Methodology

3.0 Overview

This study employs a mixed-methods research design that integrates qualitative inquiry with quantitative trend analysis. The choice of methodology is grounded in the nature of the research problem: evaluating the impact of a complex, multi-year development programme on a multifaceted outcome such as FDI requires both the analytical rigour of statistical data and the contextual depth that qualitative methods provide. The research is designed as an impact evaluation, examining the extent to which observed changes in Malawi's investment climate and FDI inflows can be attributed to the MCC Compacts, while accounting for confounding variables.

3.1 Data Collection

3.1.1 Primary Data

Key Informant Interviews

In-depth interviews were conducted with a purposefully selected group of twenty key informants who possessed direct and substantive knowledge of both the MCC programme and FDI dynamics in Malawi. Respondents included technical experts in foreign investment, current and former investors, MCC country office staff, officials from the Reserve Bank of Malawi and the Malawi Investment and Trade Centre, representatives of the US Embassy in Malawi, government officials in trade and investment roles, and researchers from think-tank institutions. Eighteen of the twenty targeted respondents participated in the study.

Given logistical constraints encountered during fieldwork, most interviews were conducted remotely via structured questionnaires delivered by email, while a smaller number of respondents were interviewed in person. The questionnaire design was differentiated by respondent category to ensure that questions were appropriately

calibrated to each participant's expertise and role. Data collected through the interviews covered FDI volume trends, investor perception of Malawi's investment climate, changes in the macroeconomic environment, and respondents' assessment of the MCC's direct and indirect contribution to these changes.

Semi-Structured Investor Survey

To gauge investor confidence and understand perceptions of Malawi as an investment destination, a semi-structured opinion survey was administered to a sample of potential and active investors drawn from five sub-regions: Southern Africa, Europe, North America, Asia, and the Middle East. The survey was designed around the key determinants of FDI identified in the literature, guided by the study's theoretical framework and research questions. Respondents were randomly selected within each regional sub-sample and all interviews were conducted virtually.

Focus Group Discussions

The study targeted ten focus group discussions, of which seven were conducted virtually with beneficiaries and stakeholders of the MCC Energy Compact. The discussions were structured around the OECD-DAC evaluation criteria of relevance, coherence, effectiveness, efficiency, and impact, enabling a structured assessment of the compact from the perspective of those most directly affected by its implementation. The discussions also sought to capture success stories, lessons learned, and recommendations for future programming.

Direct Observation

The researcher conducted direct observation of changes in the areas targeted by the MCC compact, drawing on first-hand experience of conditions both before and after programme implementation. Observations focused on visible changes in infrastructure, including power generation facilities, the transmission grid, and road networks, as well as new investment activity in areas targeted by the compact.

3.1.2 Secondary Data

An extensive body of secondary data informed both the literature review and the empirical analysis. Key sources included MCC programme documentation and the Malawi Star Report (2020), IMF country reports and Article IV consultations, World Bank FDI and macroeconomic databases, UNCTAD World Investment Reports and investment trend monitors, Reserve Bank of Malawi annual reports and financial stability reports, reports from the African Development Bank, OECD African Economic Outlook publications, the Malawi Ministry of Finance Annual Economic Reports, and data from MITC and the Malawi Stock Exchange. Country newspaper archives and peer-reviewed academic literature on FDI determinants in sub-Saharan Africa supplemented these institutional data sources.

3.2 Data Analysis

3.2.1 OECD-DAC Assessment Criteria

The OECD-DAC evaluation framework was applied as the primary tool for assessing the MCC compact's performance. This framework evaluates development interventions across five criteria: relevance (the extent to which the intervention addressed the country's genuine development needs), coherence (the degree to which the intervention aligned with national and international policies and frameworks), effectiveness (whether the programme achieved its stated objectives), efficiency (whether outcomes were achieved at reasonable cost and within the planned timeframe), and impact (the lasting changes, both intended and unintended, attributable to the intervention). The OECD-DAC framework is widely recognised as a rigorous and practically applicable tool for holistic programme evaluation.

3.2.2 SWOT Analysis

A SWOT analysis was applied to assess Malawi's position as an investment destination before and after the MCC engagement. Using data generated from both primary and secondary sources, the study examined the country's internal investment strengths and weaknesses alongside external threats and opportunities. The SWOT assessment provided a structured basis for the recommendations offered in Chapter 4.

3.2.3 PESTEL Analysis

PESTEL analysis was used to systematically assess changes in the political, economic, social, technological, environmental, and legal dimensions of Malawi's investment environment over the study period. This tool was particularly useful for identifying the range of external factors that affected FDI outcomes during

and after compact implementation, and for distinguishing between changes attributable to the MCC programme and those driven by exogenous forces.

3.2.4 Quantitative Data Analysis

Microsoft Excel was used to compile, clean, and analyse quantitative FDI and macroeconomic data from primary and secondary sources. Trend charts, pivot tables, and comparative matrices were generated to illustrate FDI inflow patterns before and after the inception of the MCC, and to contextualise Malawi's performance against regional benchmarks. These visual presentations form the empirical backbone of the findings presented in Chapter 4.

4. Findings and Discussion

4.0 Introduction

The findings are presented in response to the three principal research questions identified in Chapter 1. Given the mixed-methods design, results are presented in a combination of narrative, graphical, and tabular form. The analysis draws on both quantitative FDI trend data and qualitative responses from key informant interviews, focus group discussions, and the investor perception survey. The structure of this chapter moves from an assessment of changes in Malawi's investment climate attributable to the MCC, through an analysis of FDI trends before and after compact inception, to an examination of the structural and contextual factors that shaped those trends.

4.1 Research Question One: The Impact of the MCC Compacts on Malawi's Investment Reputation

4.1.1 Investment Policy and Legal Framework Before and After 2011

The primary data generated through the investor perception survey and key informant interviews reveals a broadly positive, if cautiously qualified, assessment of improvements in Malawi's investment climate following the MCC engagement. Approximately 55 percent of respondents characterised Malawi's investment climate before 2012 as poor, 25 percent saw no significant change over the study period, while 20 percent rated it as good or very good. Among those who perceived improvement, 52.9 percent attributed the change, at least in part, to the MCC Compacts, particularly in the areas of policy and legal reform and infrastructure development. A smaller but noteworthy minority, 11.7 percent, viewed the MCC as an instrument of a capitalist agenda that had worsened, rather than improved, the investment environment.

The most consistently cited sources of improvement related to the energy sector. The commissioning of the Kapichira and Tedzani hydropower stations, the rehabilitation of the Nkula hydropower facility, and the completion of the regional power interconnector with Mozambique were identified by respondents as tangible indicators of progress that had raised investor confidence. These infrastructure improvements reduced the duration and frequency of power outages, lowered the costs associated with diesel-powered backup generation, and, through the Southern African Power Pool connection, provided Malawi with access to regional electricity markets for the first time.

Governance reforms also received significant attention. The unbundling of ESCOM into separate generation and transmission entities, the establishment of the Malawi Energy Regulatory Authority, and the opening of the power sector to private independent power producers were identified as structural changes that reduced monopolistic inefficiency and signalled a meaningful shift in the government's approach to investment facilitation. Before the compact, ESCOM combined the roles of generator, transmitter, and sole buyer of electricity, an arrangement that simultaneously stifled competition, cross-subsidised inefficiency, and deterred private investment. The institutional separation of these functions created a more transparent and contestable market structure.

The threshold programme's contribution to governance more broadly was also acknowledged. The establishment of the Integrated Financial Management Information System (IFMIS), support to the National Audit Office and Malawi Anti-Corruption Bureau, and Parliamentary capacity-building activities were cited as having contributed to modest but measurable improvements in fiscal transparency and accountability. These improvements were reflected in Malawi's upward movement in the Corruption Perception Index during the implementation period.

Perhaps the most significant testimony to the compact's governance impact came from a single investor case study cited by multiple respondents: a uranium mining company that had suspended operations in Malawi due to severe and persistent power outages returned to the country following the completion of the Energy Compact, citing the improved reliability and cost of electricity supply as decisive factors in its decision to resume investment. This case, while anecdotal, illustrates the concrete mechanism through which energy sector reform translates into investor behaviour.

The investor perception data also revealed a nuanced picture of Malawi's competitive position relative to regional peers. Analysis drawing on Lloyd's Bank and World Bank data indicates that, in certain dimensions of investor protection, including transparency in transactions and shareholder rights to legal recourse, Malawi performs comparably to Zambia and favourably relative to some indicators for South Africa. This finding challenges the assumption that Malawi's investment climate is uniformly poor and suggests that selective strengths in legal and regulatory frameworks have not been adequately communicated to the international investor community.

However, 68 percent of respondents identified significant areas of remaining concern, including restrictions on foreign equity stakes during initial public offerings, the limited reach of Malawi's bilateral investment treaty network, and continued weaknesses in contract enforcement and dispute resolution. These structural gaps represent persistent deterrents that partly explain why improvements in investor perception have not translated into commensurate FDI volumes.

4.1.2 The Energy Sector: A Detailed Assessment

The scale of the energy sector transformation achieved under the MCC Energy Compact merits detailed examination. Prior to the compact, Malawi's installed power generation capacity stood at approximately 284 megawatts against a demand that was projected to reach 478 megawatts by 2015 and 757 megawatts by 2020. This structural deficit meant that power outages of eight to twelve hours per day were routine, imposing enormous productivity losses on businesses and households. The World Bank estimated these losses in the hundreds of millions of dollars annually.

The Energy Compact addressed this constraint through multiple interventions. The rehabilitation of the Nkula hydropower station added generation capacity that had been lost to years of deferred maintenance. The construction of a 400 kilovolt overhead transmission line stretching 173 kilometres from Phombeya to Nkhoma fundamentally transformed the grid's carrying capacity, replacing a 132 kilovolt network with a system capable of transmitting bulk power at lower losses and at greater speed. The interconnection substations built at Phombeya and Nkhoma integrated Malawi into the Mozambican and Zambian grid networks, opening the country to the Southern African Power Pool and providing both import access during domestic shortfalls and potential export capacity in surplus periods.

The institutional reforms accompanying these infrastructure investments were equally consequential. The unbundling of ESCOM into EGENCO and a transmission-focused ESCOM created the structural conditions for private sector participation in power generation. Following this reform, Malawi registered two greenfield investments in renewable energy, adding further capacity to the grid. The liberalisation of the sector also attracted interest from major international players, including Siemens, signalling a shift in the perception of Malawi's energy market from a state-controlled monopoly to an emerging competitive investment opportunity.

From the perspective of investor location advantage, the energy compact's achievements were significant. While Malawi continues to face electricity access challenges, the systemic nature of the pre-compact crisis has been substantially mitigated, and the institutional framework for future private sector participation has been established.

4.1.3 Country Comparison for Investor Protection

Lloyd's Bank comparative data (2024) highlights several institutional strengths in Malawi's investment environment that are frequently overlooked in general assessments of the country's investment climate. The Malawi Investment and Trade Centre operates with relatively few restrictions on the size of investment or the sectoral composition of foreign capital, and there are no requirements that products be destined for export or the domestic market. These features compare favourably with the more restrictive frameworks of some regional peers.

However, the restriction limiting foreign equity stakes to a maximum of 49 percent during initial public offerings on the Malawi Stock Exchange, and the cap on foreign participation at 10 percent, represent regulatory features that may discourage certain categories of portfolio and strategic investors. The banking and financial services sector retains similar foreign participation limits, which, while designed to protect domestic financial stability, may deter institutional investors seeking majority ownership positions.

4.2 Research Question Two: FDI Inflow Trends Before and After the MCC

4.2.1 FDI Performance Before 2012

Malawi's pre-MCC FDI trajectory was characterised by considerable volatility, shaped by the intersection of structural reform efforts, political events, and external economic conditions. The transition from single-party rule in 1994 initiated a period of economic liberalisation that included the privatisation of state enterprises, tariff reductions, and bilateral trade agreement negotiations. These reforms produced a modest

increase in FDI inflows in the early 2000s, as sectors previously closed to foreign participation were opened and macroeconomic policy frameworks improved.

The adoption of the Malawi Poverty Reduction Strategy Paper in 2002 provided a coherent framework for economic reform that aligned with donor expectations and facilitated significant debt relief. The cancellation of Malawi's debt under the Heavily Indebted Poor Countries Initiative following the successful implementation of the Poverty Reduction and Growth Facility in 2005-2006 restored foreign reserve levels, improved the balance of payments, and raised investor confidence sufficiently to drive FDI inflows to approximately 1.9 percent and 2.5 percent of GDP in 2007 and 2008, respectively. This period coincided with the economy growing at an average of approximately seven percent per annum.

Paradoxically, Malawi was relatively insulated from the 2008-2009 global financial crisis, precisely because its financial sector was not significantly integrated into global capital markets. This isolation, while limiting in normal times, provided a buffer against the most severe external shocks of the crisis period. During the same period, greenfield investments in the mining sector, particularly Paladin Energy's Kayerekera Uranium Mine, contributed a disproportionate share of FDI inflows and created expectations of a broader mining sector expansion that did not materialise.

However, years of civil unrest and political instability consistently corresponded with FDI declines. The industrial strikes and urban protests of 1992, the political confrontation between the executive and legislature in 2006 that paralysed the national budget, and the nationwide protests of 2011-2012 that preceded the MCC suspension all produced sharp downturns in investment confidence. These episodes illustrate the inherent fragility of Malawi's investment climate and the extent to which political volatility can rapidly offset institutional reform gains.

4.2.2 FDI Performance After the MCC Inception

The MCC Energy Compact period witnessed a paradoxical pattern in FDI performance. The year 2011, when the compact was signed, saw FDI inflows reach approximately seven percent of GDP, the highest level recorded during the study period. This surge reflected a combination of compact-related financial inflows, renewed investor confidence associated with the signing of the agreement, and continued momentum from the mining and agricultural sectors.

However, the years immediately following were marked by a sharp reversal. Political unrest in 2011 and 2012, culminating in the death of twenty-one protesters in July 2011, triggered the suspension of MCC support and the simultaneous withdrawal of budgetary assistance by the major donors operating under the Common Approach for Budgetary Support (CABS) framework. The resulting collapse in foreign reserve levels, coupled with acute shortages of fuel, fertiliser, and basic commodities, created conditions that were fundamentally hostile to new investment. FDI inflows declined sharply in 2012 and remained subdued through much of the Energy Compact implementation period.

The period 2016 to 2022 saw continued low FDI inflows, despite the near-completion of the Energy Compact's major infrastructure works. The primary explanation lies in the convergence of multiple adverse shocks: cyclones in 2016, 2018, and 2021 that damaged power infrastructure, most severely at the Kapichira Power Station where Cyclone Ana destroyed 129.6 megawatts, approximately 23 percent of national capacity; the 2019 electoral crisis and its prolonged political resolution; and the triple impact of COVID-19, the Russia-Ukraine conflict, and extreme weather events from 2020 to 2022.

By the end of 2022, Malawi's gross official reserves had fallen to USD 292 million, representing only 1.2 months of import cover, compared to 1.6 months at the end of 2021. Inflation reached 28 percent at year-end, driven by global commodity price shocks and supply chain disruptions. The Reserve Bank responded by raising the policy rate to 24 percent in 2023, further increasing the cost of domestic borrowing and crowding out private investment. In November 2023, a 44 percent devaluation of the Malawi Kwacha was implemented to align the official rate with the parallel market, sharply increasing import costs and reducing real household incomes.

These conditions explain why, despite the genuine reform achievements of the Energy Compact, FDI inflows failed to exhibit a sustained upward trend during the implementation period. The external shock environment was simply too severe and too persistent to be overcome by infrastructure and governance improvements that, under more stable conditions, might have produced significantly different outcomes.

4.2.3 Malawi's International FDI Position

In comparative terms, Malawi's FDI performance places it among the weakest recipients in sub-Saharan Africa. With inflows of approximately USD 46 million in 2022, Malawi ranked far behind regional peers including Mozambique (USD 1.97 billion), Tanzania (USD 1.10 billion), and South Africa (USD 13 billion). Even countries with broadly similar structural profiles, such as Zambia, attracted significantly larger FDI volumes despite facing comparable governance and infrastructure challenges.

This comparative underperformance persists despite the significant reforms undertaken with MCC support and is not fully explained by macroeconomic or governance differentials alone. Key distinguishing factors include Mozambique's substantial natural gas discoveries, which attracted large-scale resource-seeking FDI that is categorically different from the market-seeking and efficiency-seeking investments that Malawi has sought; Tanzania's considerably larger domestic market and more extensive road and railway infrastructure; and Zambia's longer history of mining sector development, which has created institutional relationships and investor familiarity that Malawi has not yet established.

At the global level, Africa's share of total FDI remained low throughout the study period, constrained by perceptions of political and regulatory risk, infrastructure gaps, and market size limitations that affect the continent as a whole. Within this challenging global context, Malawi's investment promotion efforts have been further handicapped by a limited diplomatic network and a relatively sparse bilateral investment treaty portfolio, issues that are discussed in detail below.

4.3 Research Question Three: Factors Explaining Malawi's FDI Underperformance

4.3.1 Overall Assessment of the MCC Compact's Impact

The weight of evidence from both primary and secondary data sources leads to a nuanced conclusion. The MCC Malawi Compact was one of the most ambitious and comprehensively designed reform programmes in sub-Saharan Africa during the study period. It targeted genuine structural constraints to investment with technically sound interventions and achieved measurable results in energy generation, grid capacity, institutional reform, and governance quality. These achievements were real and, in several cases, significant.

However, the programme's impact on FDI inflows was substantially moderated by a set of structural factors and external shocks that the compact design did not, and arguably could not, anticipate. The following sections examine the principal explanatory factors.

4.3.2 Political Instability

Political instability has been the single most consistently significant moderator of FDI inflows in Malawi throughout the study period. The correspondence between episodes of civil unrest and FDI declines is striking: the protests of 1992, 2006, 2012, and 2019 each produced measurable downturns in investment confidence, regardless of the state of underlying institutional reforms.

The 2019 electoral crisis is particularly instructive. Following general elections marred by widespread irregularities, Malawi's courts nullified the results, triggering an extended period of political uncertainty that lasted until fresh elections were held in 2020. The associated protests represented the largest and most sustained wave of civil unrest in the post-independence era. For foreign investors, particularly those operating in risk-sensitive sectors such as manufacturing, services, and financial products, this sustained political volatility was sufficient to defer or cancel planned investments, regardless of the positive signals provided by energy sector improvements and legal reforms.

Beyond episodic instability, Malawi also faces structural political risks associated with the fragility of its democratic institutions, the limited capacity of oversight bodies, and the periodic friction between executive and legislative branches that has at times paralysed budget approval processes and created acute fiscal uncertainties. These systemic risks compound the deterrent effect of individual political crises.

Human development indicators represent a related dimension of the investment deterrent. Malawi's poverty headcount ratio of 70.1 percent, its GDP per capita of USD 672, and its high rates of illiteracy and low levels of secondary and tertiary education completion collectively limit the attractiveness of the market for consumer-oriented investments and constrain the availability of skilled labour for more sophisticated manufacturing or service operations. By comparison, Tanzania's poverty headcount ratio of 44 percent and its considerably larger educated workforce make it a substantially more attractive destination for market-seeking and efficiency-seeking FDI.

4.3.3 Limited Resilience to External Shocks

Malawi's vulnerability to external shocks, whether economic, geopolitical, or climatic in origin, has severely and repeatedly undermined the investment gains achieved through the MCC compact. The country's narrow economic base, heavy dependence on rain-fed agriculture, and limited fiscal space have combined to make each shock disproportionately destructive.

The cyclones of 2016, 2018, and 2021 illustrate this vulnerability with particular clarity. Cyclone Ana in January 2022 caused particularly severe damage to the Kapichira Power Station, removing 129.6 megawatts, approximately 23 percent of national capacity, from the grid and triggering power outages exceeding twelve hours per day. The station had been one of the key infrastructure assets improved under the MCC Energy Compact, and its sudden loss demonstrated the fragility of gains made in a country exposed to increasing

climate volatility. The cost of emergency diesel generation to compensate for the lost capacity fell disproportionately on businesses and the government, creating precisely the conditions that the compact had been designed to eliminate.

The COVID-19 pandemic similarly exposed the depth of Malawi's economic fragility. GDP growth fell to approximately 0.8 percent in 2020 before recovering partially to 4.6 percent in 2021, only to drop again to 1.1 percent in 2022 as geopolitical conflict and extreme weather compounded the pandemic's legacy effects. Gross official reserves declined from USD 411 million (1.6 months import cover) at end-2021 to USD 292 million (1.2 months import cover) at end-2022, further straining the government's capacity to finance essential imports and maintain macroeconomic stability.

Malawi's landlocked status amplifies the impact of these shocks. Unlike coastal peers, Malawi cannot benefit from short-sea shipping options and relies entirely on overland routes to reach regional ports. The combination of global supply chain disruptions with high domestic logistics costs, already among the most elevated in the region, created conditions of extreme economic stress during the 2020-2022 period that were deeply inhospitable to new investment.

4.3.4 Economic Factors

Malawi's macroeconomic profile presents persistent challenges to investment attractiveness that extend beyond the reach of any single development programme. The country has maintained a structural current account deficit throughout the study period, driven by a narrow export base and chronic import dependence. The ratio of total debt to GDP rose from 30 percent in 2021 to 42 percent in 2023, reflecting the combined impact of pandemic-related fiscal expansion, infrastructure financing, and the ongoing cost of servicing an increasing domestic debt burden.

Table 4.1: Energy Costs in Southern Africa

Country	Petrol	Diesel	Electricity	GDP (Bn USD)	FDI (Bn USD)
Zimbabwe	2,652.00	2,958.00	8.10	26.5	0.34
Malawi	2,530.00	2,734.00	10.22	14.08	0.18
Mozambique	2,295.00	2,431.00	13.08	20.62	1.97
South Africa	2,228.00	2,274.00	9.56	377.78	13.0
Tanzania	2,227.00	2,295.00	10.22	79.16	1.10
Zambia	2,182.00	2,181.00	7.00	28.1	0.12
Botswana	2,084.00	2,223.00	10.43	19.4	0.216

Source: Malawi Energy Regulatory Authority (November 2023); UNCTAD World Investment Report (2023)

The table above reveals an important dimension of Malawi's investment cost environment. Despite energy sector improvements, Malawi's petrol and electricity prices remain among the highest in the region, exceeded only by Zimbabwe. This cost burden reflects both the structural inefficiencies that persist in the energy sector post-compact and the high logistical costs of importing fuel. The data illustrate a clear negative correlation between energy costs and both GDP size and FDI inflows: countries with lower energy costs, such as Zambia and South Africa, attract substantially greater investment volumes. For Malawi to significantly improve its FDI performance, reducing the landed cost of energy remains a critical priority.

The 44 percent devaluation of the Malawi Kwacha in November 2023, while endorsed by the IMF as a necessary step towards external balance, had immediate and severe consequences for import-dependent businesses. The cost of capital goods, raw materials, and intermediate inputs denominated in foreign currency increased proportionally, eroding operating margins and reducing the real purchasing power of domestic consumers. The simultaneous rise in inflation to 43.5 percent for food items in December 2023 further suppressed household demand, weakening the consumer market signals that might otherwise attract market-seeking investors.

Fiscal consolidation pressures also constrained the government's capacity to provide investment incentives and maintain the public infrastructure expenditure necessary to sustain the gains made under the MCC compact. Increasing domestic debt, at an average lending rate that reached 24 percent following the policy rate adjustment, crowded out private sector credit and raised the cost of business financing to levels that were uncompetitive relative to the regional norm.

4.3.5 Foreign Policy and Bilateral Investment Relations

Malawi's international investment treaty network represents one of the most significant and least discussed structural barriers to FDI. The country has signed fewer bilateral investment treaties and trade

agreements than most of its regional peers, and a substantial proportion of those agreements remain unratified and therefore legally inoperative. In the modern era of economic diplomacy, bilateral investment treaties serve as important risk-management instruments for investors, providing legally enforceable guarantees of investment protection, dispute resolution mechanisms, and in some cases profit repatriation rights.

The comparative data indicate that Tanzania, Mozambique, and Zimbabwe have all concluded significantly more active bilateral investment agreements than Malawi, and this differential partly explains the gap in FDI inflows. Investors, particularly those from jurisdictions with robust outward investment frameworks, are more comfortable deploying capital in countries with which their home government has concluded a bilateral investment treaty that offers protection through international arbitration.

Malawi's limited diplomatic footprint compounds this problem. With fewer embassies than most regional peers, Malawi is less effectively represented in the investment promotion networks of major capital-exporting countries. Investment deals are frequently facilitated through diplomatic relationships, and countries with limited representation in key markets are structurally disadvantaged in the competition for globally mobile capital.

4.3.6 Investment Policy and Governance

Despite the reforms achieved through the MCC compact, Malawi's investment policy framework retains several features that constrain its competitive position. The equity stake limitations on foreign participation in listed companies, the absence of a comprehensive investment facilitation service offering streamlined approvals across regulatory agencies, and the inconsistent application of tax and customs rules have each been cited by investors as deterrents to entry. Fighting corruption, while identified as a priority in the MCC compact design, remains an ongoing challenge: Malawi's Corruption Perception Index score of 34 out of 100 in 2022 places it in the lower quartile of African countries, and investor surveys consistently identify corruption as a significant risk factor.

The overall investment policy environment improved materially under the MCC compact, and the reforms achieved in the energy sector in particular represent lasting institutional gains. However, the policy and legal framework operates within a broader governance context in which institutional capacity, rule of law, and contract enforcement remain works in progress. Sustaining and deepening the compact's institutional legacy will require continued commitment from successive Malawian governments beyond the MCC programme period.

Recommendations

The findings of this study point to a set of concrete and interconnected policy recommendations for the Government of Malawi, development partners, and future programme designers. These recommendations are grounded in the evidence generated by the study and are intended to be practically actionable within realistic institutional and fiscal constraints.

Export Expansion and Fiscal Consolidation

Malawi must pursue a decisive shift from import dependence towards export competitiveness. This requires targeted investment in the productive sectors with demonstrated comparative advantage, including high-value agricultural products, agro-processing, and minerals. Reducing the current account deficit will improve foreign reserve adequacy, stabilise the exchange rate, and reduce the macroeconomic uncertainty that continues to deter long-term foreign investors. Fiscal consolidation, including the rationalisation of recurrent expenditure and improved domestic revenue mobilisation, is essential to reduce reliance on costly domestic borrowing and create fiscal space for investment-enabling public expenditure.

Political Stability and Institutional Resilience

The study demonstrates unequivocally that political instability imposes severe costs on Malawi's investment performance. The Government of Malawi must draw lessons from the civil unrest episodes of 1992, 2012, and 2019 and invest in the institutional mechanisms, electoral integrity, parliamentary process, and independent judicial capacity that prevent political disputes from escalating into investment-detering crises. State organs must function in ways that reinforce, rather than undermine, investor confidence.

Human Capital Development

Government and development partners must significantly increase investment in education and skills development at secondary and tertiary levels. A well-educated and technically skilled workforce is both an FDI determinant in its own right and a prerequisite for absorbing the technology and management expertise that FDI can transfer. Investment in health systems, which reduces workforce absenteeism and improves labour productivity, represents an equally important dimension of human capital development.

Middle Income Transition Strategy

Malawi must pursue policies designed to expand the middle-income population and deepen domestic consumer markets. Service sector FDI in hospitality, retail, financial services, and information technology is primarily attracted to countries with growing middle-income populations that provide an adequate consumer base. A combination of agricultural productivity improvement, labour market formalisation, and targeted social protection can accelerate income growth in the lowest income quintiles and expand the domestic market opportunity for foreign investors.

Regional Economic Integration

Malawi and its SADC partners must accelerate the deepening of regional economic integration, including the full implementation of the SADC Free Trade Area and the harmonisation of non-tariff regulatory requirements. The individual markets of most Southern African economies, including Malawi, are too small to attract large-scale manufacturing or processing FDI on the basis of domestic market size alone. An integrated regional market of over 400 million consumers would fundamentally transform the investment calculus for efficiency-seeking and market-seeking investors across the region.

Resilience to External Shocks

Malawi must invest substantially in climate adaptation infrastructure to protect the economic assets and energy systems that underpin investor confidence. The recurring destruction of the Kapichira Power Station and surrounding infrastructure by successive cyclones demonstrates the catastrophic cost of inadequate resilience investment. Climate-proofing of critical infrastructure, diversification of generation sources to reduce reliance on a small number of hydro assets, and the development of early warning and disaster response systems are essential components of a credible resilience strategy.

Infrastructure Development

Beyond the energy sector, Malawi must prioritise the rehabilitation and extension of its transport infrastructure, particularly the railway connections to regional ports. The reactivation of the Nacala Corridor rail link to Mozambique and the development of multimodal logistics infrastructure would substantially reduce the landing costs that currently make Malawi one of the most expensive investment destinations in the region despite its relatively liberal regulatory framework.

International Investment Diplomacy

Malawi must accelerate the negotiation, ratification, and activation of bilateral investment treaties with major capital-exporting countries, including those in Europe, North America, the Gulf Cooperation Council, and East Asia. This requires both a diplomatic investment, including expanding the country's embassy network in key investor markets, and a domestic institutional strengthening effort to equip Malawian negotiators with the technical capacity to conclude agreements that adequately protect both investor interests and Malawi's developmental policy space.

Conclusion

This thesis has examined the impact of the Millennium Challenge Corporation Compacts on foreign direct investment inflows into Malawi, covering the period from the late 1990s to 2022. The study was motivated by a striking empirical paradox: despite two successive MCC compacts totalling approximately USD 700 million, a series of significant institutional and infrastructure reforms, and a demonstrable improvement in the country's energy sector and governance framework, Malawi's FDI inflows declined over the compact implementation period and remained well below those of regional peers.

The findings confirm that the MCC Energy Compact targeted the right structural constraints and achieved genuine progress across several dimensions. The rehabilitation and expansion of hydropower capacity, the construction of the 400 kilovolt transmission line, the connection of Malawi to the Southern African Power Pool, the unbundling of the electricity utility, and the opening of the energy sector to private investors were all substantive achievements that improved the enabling environment for foreign investment. The governance reforms supported by the threshold programme and embedded in the compact, including improvements in fiscal transparency, anti-corruption institutions, and regulatory frameworks, also produced measurable improvements in Malawi's investor confidence ratings.

However, these achievements were overwhelmed by a convergence of external shocks and structural vulnerabilities that fell substantially outside the compact's scope of intervention. Recurring political instability, including the electoral crisis of 2019 and the associated civil unrest, repeatedly deterred investors during periods when reform momentum was building. Cyclone damage to energy infrastructure, most severely at Kapichira in

2022, reversed gains made at considerable cost and effort. The COVID-19 pandemic, global supply chain disruptions, and the inflationary consequences of the Russia-Ukraine conflict combined to create macroeconomic conditions that were inhospitable to new investment. And Malawi's structural vulnerabilities, including its narrow export base, poor bilateral investment treaty coverage, limited diplomatic presence, and human development deficits, meant that even an optimally performing compact could not have delivered transformative FDI outcomes in isolation.

The study therefore concludes that the MCC Compacts were well-designed and broadly effective within their scope, but their impact on FDI was inherently limited by factors beyond the programme's reach. The Malawi case offers a cautionary lesson for development programme designers: institutional and infrastructure reforms, however well-executed, cannot fully compensate for macroeconomic instability, political fragility, and structural competitiveness deficits when these converge simultaneously.

Looking forward, the 2022 Transport and Land Compact offers a renewed opportunity to deepen the investment-enabling gains of its predecessor. The success of this compact, and Malawi's longer-term FDI performance, will depend on the government's capacity to sustain political stability, build macroeconomic resilience, deepen regional integration, and expand its international investment diplomacy, alongside the continued support of development partners willing to engage with the long-term structural reforms that Malawi's investment transition genuinely requires.

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