

WORKSHOP CONCEPT NOTE

IMPROVING THE FUNCTIONING OF COMMODITY MARKETS IN EASTERN AND SOUTHERN AFRICA THROUGH WAREHOUSE RECEIPT SYSTEMS AND MARKET-BASED INTERVENTIONS

Jointly organized by:
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ALL ACP Agricultural Commodities Programme



1. Background: The Eastern and Southern African context

Improving the performance of the agricultural sector is seen as critical in achieving accelerated economic growth and poverty reduction in Eastern and Southern Africa. The sector contributes 32% of GDP and provides 65% of the raw materials used by industry in the COMESA region. It also accounts for 80 % of employment in the region, where 90% of the rural population are dependent on the farm sector for their livelihoods. Growth in the agricultural sector can generate significant inter-sector multiplier effects as well as contribute directly to reducing poverty, especially in the rural areas. Thirtle et al. (2005) reported that each percentage point growth in agricultural yields reduces the number of people living on less than US \$1 per day by between 0.6 and 1.2 per cent¹. Increased food supply capacity in the region as well as enhanced intra-regional trade in agricultural goods are also critical in enhancing household food security for the 200 million people out of 400 million who suffer from chronic malnourishment.

Various agricultural development initiatives have been launched in response to the pressing need to raise agricultural productivity and output in Africa. Among these is the *Comprehensive Africa Agriculture Development Programme (CAADP)*, a regional initiative which was launched by the New Partnership for Africa's Development (NEPAD) with the explicit target of achieving 6% growth in agriculture. One critical condition for achieving this goal is the enhancement of the functioning of agricultural markets – for both food crops² and agricultural export commodities. The second and third “Pillars” of CAADP specifically focus on “trade-related capacities for market access” and to “increasing food supply, reducing hunger and improving responses to food emergency crises”. Among these is also the creation of the Alliance for Commodity Trade in Eastern and Southern Africa (ACTESA), which was endorsed by the COMESA Authority as a Specialized Agency of COMESA to promote the competitiveness and integration of small farmers into national, regional and international markets³

COMESA is implementing a number of programmes which are synergic with CAADP, ACTESA and the planned UNCTAD/COMESA/EAGC collaboration. These programmes include the Agricultural Marketing Promotion and Regional Integration Project (AMPRIP), the African Agricultural Markets Programme (AAMP), and the Programme for Building African Capacity for Trade (PACT) - see Annex 2. COMESA is also in the process of developing a regional strategy for its agro-industry sector with AAACP/ITC support. The strategy is based on a comprehensive view of agro-industries encompassing agricultural production and trade. It stems from COMESA's initiatives enunciated by the UNIDO supported 17th Conference of African Manufacturing Industries (CAMI) held in Cairo in June 2006 and is also consistent with the initiative by the Economic Commission for Africa (ECA) to foster the development of regional agricultural values, in particular along the regional development corridors.

¹ Thirtle C, Piesse J, Irz X. (2005). ‘Governance, Agricultural Productivity and Poverty Reduction in Africa, Asia and Latin America’ In Mosley and Gray (eds.) *Cotton, Natural Resources and Society in Sub-Saharan Africa*. Oxford University Press: Oxford.

² Every year a number of countries experience severe food deficits while the region as a whole generates staple food surpluses that can range from 500,000 to 1,500,000 MT – which is an indicator among many others of the important potential that exists for the enhancement of intra-regional trade.

³ 13th Summit of the COMESA Authority of Heads of State and Government in Zimbabwe (June 2009).

These initiatives, as well as others such as USAID/COMPETE and USAID/PROFIT, the implementation of some of which involves COMESA and EAGC, are briefly described in Annex 2. It is important to strengthen synergies between these initiatives and efforts to promote market-based institutions and instruments such as *warehouse receipts systems* and *commodity exchanges*, which can improve supply chain finance as well as enhance efficiency in agricultural trade to the benefit of producers, traders, processors and other stakeholders.

2. Warehouse receipt systems and commodity exchanges

Liberalisation of agricultural marketing systems brought to the fore the need to develop market institutions such as warehouse receipt systems (WRS) and commodity exchanges as they offer a significant potential for the enhancement of the functioning of commodity markets. African Ministers of Trade, at a summit in Arusha in November 2005, resolved that national governments should support the development of these institutions.⁴

Warehouse receipt system and inventory credit

The development of warehousing has positive knock-on effects up and down the supply chain. For farmers, the WRS can help them store more food for their local consumption requirements, avoid post-harvest distress sales and provide a market window to secure the best possible deal for surplus produce. The WRS provides a platform for the introduction of other institutional innovations, notably grading, contracting and exchange trading. It facilitates public procurement as national and international agencies can simplify their activities by dealing in paper such as warehouse receipts, rather than trade directly in physical commodities. WRS is also a valuable instrument for financing agricultural commodity chains, especially in countries where the shortage of alternative forms of collateral constitutes one of the most important obstacles in access to finance.

The use of warehouse receipts within the supply chain has been pioneered in Eastern and Southern Africa with a focus on the key staple foods although some cash crops such as coffee, cashew nuts and cotton have also been targeted in recent initiatives. The Republic of South Africa has by far the strongest WRS in the Region, but it works almost entirely with large-scale commercial farmers and has emerged without active involvement of the State or international agencies. However, other countries in the region have had to rely upon (or will need) such support to get started. In recent years, several warehouse receipts and inventory credit initiatives have been developed in countries such as Ethiopia, Kenya, Tanzania, Uganda, Zimbabwe, Zambia, Madagascar and Malawi. These initiatives are at varying stages of implementation and have adopted different approaches, in particular with regard to targeting, legislation, regulatory oversight, crops, WRS documentation and interaction with public procurement. A close examination of these recent initiatives will reveal their differences and similarities. It will also identify the prerequisites for a successful WRS and inventory credit project such as legal and related policy issues, including the pros and cons of different regulatory approaches, sustainability of warehouse receipt and inventory credit systems, and the strengths and weaknesses of paper-based and electronic systems.

⁴ AU (2005b), *Arusha Declaration and Plan of Action on African Commodities*, AU Conference of Ministers of Trade on Commodities, 21-23 November, 2005, Arusha, Tanzania.

Under the EU funded All ACP Agricultural Commodities Programme (AAACP), the Eastern and Southern Africa Consultative Kick-Off Workshop which was held in June 2008 in Dar es Salaam prioritised WRS & inventory credit as means to enhancing access to agriculture supply chain finance in the region. The participants of the Workshop expressed their strong demand to share experience and learn best practice from the ongoing WRS and inventory credit initiatives in the region.

As a follow-up activity of this regional workshop and to accelerate the learning process, both within the region and in other AAACP regions, UNCTAD, as one of the five international organizations implementing the AAACP,⁵ commissioned a study to review warehouse receipts and inventory credit initiatives in Eastern and Southern Africa. From March to May 2009 the consultant undertook field missions with the objective of reviewing the performance of existing WRS and inventory credit in six ESA countries, namely Kenya, Tanzania, Uganda, Zambia, Madagascar and Malawi. The preliminary report of the study will be presented to the Workshop by the consultant.

This preliminary report analyzed in detail the development of WRS and inventory credit in the targeted countries, identified lessons from the different projects and provided recommendations. In particular, the report highlighted some key issues for the development of WRS in the region such as public policy, warehouse licensing and regulating, market off-take, electronic warehouse receipt system and warehouse-based financing (including storage credit by microfinance institutions). It also identified different approaches to promoting WRS in the African context.

Commodity exchanges

The introduction of the warehouse receipt system has for the most part gone hand in hand with the development of commodity exchanges, though there are some exceptions where exchanges have not been in place. There is a high level of interdependence between these two innovations, with the warehouse receipts providing a mechanism for delivery against exchange contracts, and the exchange providing additional liquidity, plus a means of valuing the warehouse receipt and liquidating the underlying commodity.

The development and use of agricultural commodity exchanges within Africa has been pioneered in the Southern Africa and Eastern Africa sub-regions, where it focuses on maize and export crops. The agricultural commodity exchanges projects in these sub-regions are the following:

- Botswana: MCX launched the creation of a Pan African Exchange - Bourse Africa
- Ethiopia: Ethiopia Commodity Exchange (ECX - spot and forwards)
- Kenya: i) Kenya Agricultural Commodity Exchange (KACE / operational - information dissemination); ii) Africanlion.com (a planned internet trading platform that didn't become operational)
- Malawi: i) Agricultural Commodity Exchange for Africa (ACE / operational - regional listings & auctions); ii) Malawi Agricultural Commodity Exchange (MACE, operational - information dissemination)
- South Africa: JSE/SAFEX (operational - futures and options)

⁵ The other four international organizations are FAO, International Trade Centre (ITC), World Bank and Common Fund for Commodities (CFC).

- Uganda: Uganda Commodity Exchange (UCE operational - mostly information dissemination but did not yet generate much business; supported by Natural Resources Institute)
- Zambia: Zambia Agricultural Commodity Exchange (ZAMACE)

Both the UCE and ZAMACE have been active in developing a system of electronic warehouse receipts.

The continued and reinforced development of agricultural commodity exchanges will entail benefits such as the provision of financial services to the supply chain stakeholders; the wide development of warehouse receipt systems; price discovery, price transparency, wider market information and marketing choices; grades use and grading development; premiums for quality production; quality assurance/upgrade; as well as transaction risk management development and regional integration.

Nevertheless, it appears that with a few exceptions, commodity exchanges in the region have to date not realized their full potential. As noted by UNCTAD (2007)⁶, most of the exchanges promoted in Africa have been unable to sustain spot trade and much less trade in futures and other derivatives. The major exceptions in Africa are SAFEX in South Africa and the Zimbabwe Agricultural Commodities Exchange (ZIMACE), which successfully traded in grains between 1994 and 2001 when it was suspended.

Among the many conditions that have to be met before commodity exchanges can significantly impact on markets, one is the existence of a critical mass of physical and actually tradable stocks – an area in which reliable warehouse receipts systems (and their electronic linkages) do play an essential role.

3. Workshop's objectives and methodology

From the foregoing, it is clear that WRS and Commodity Exchanges are interdependent and complimentary market-based instruments. The institutional requirements for the two sets of interventions, in particular the legal and regulatory framework, greatly overlap. In addition, WRS encourages not only the use of Commodity Exchanges, but also enhances their efficiency. Similarly, the latter could also facilitate the development of WRS and promote its widespread acceptance and use by clients. This Workshop is thus driven by the need to tap the complementarity between these two instruments in the ESA region in order to promote their symbiotic development.

It is within this context that UNCTAD commissioned the study on the review of warehouse receipts and inventory credit initiatives in Eastern and Southern Africa. It is expected that this Regional Workshop will to enhance the linkages between WRS and commodity exchanges in Eastern and Southern Africa, and outline priority actions and policy recommendations that regional bodies, policy makers, practitioners and development partners would implement in order to develop viable and accessible WRS and commodity exchanges in the region. The Workshop is also expected to build the capacity of key players in advancing WRS and commodity exchanges, in close collaboration with regional organizations. Finally, it will

⁶ UNCTAD (2007) "Overview of the world's commodity exchanges 2006", prepared by the UNCTAD Secretariat.

provide a forum for sharing evidence-based lessons and experiences, as well as for building consensus on the key issues regarding the development of WRS and inventory credit.

General Objective: The overall, long-term objective of the workshop is to strengthen the capacity of private and public stakeholders to develop viable WRS and commodity exchanges as well as other related market institutions which will improve the functioning of agricultural markets in Eastern and Southern Africa.

Specific Objectives:

1. To share relevant experiences and lessons derived from case studies and specific reviews as a basis for formulating a framework for future action by practitioners and other stakeholders in developing these market-based institution instruments;
2. Identify regional priorities concerning the enhanced functioning of commodity markets and opportunities for strengthening complementarity between initiatives to promote WRS and commodity exchanges and other agricultural sector development programmes.
3. Formulate public policy recommendations (and/or priority actions) and strategy for sustained policy advocacy at regional and national levels. The framework will form the basis for annual reviews by the membership of EAGC regarding progress made at relevant national and regional levels.

Participants: The Workshop will gather approximately 100 participants among which 85 from the Region, principally practitioners from the private sector, and representatives from Governments. Donors, the AAACP involved organizations and concerned regional organizations will also be invited to participate.

Approach:

The workshop programme will consist of main sessions focusing on the following:

(1)The context:

This will consist of one presentation setting out how the promotion of WRS and commodity exchanges fit into on-going regional agricultural and trade development initiatives. The rationale is to ensure that the complementarity between these programmes is fully tapped.

A preliminary report on a study of warehouse receipt financing in Eastern and Southern Africa, commissioned by UNCTAD in March 2009 will be presented and discussed.⁷ The report provides analysis of features and modalities of WRS creation and development, as well as critical issues that need to be addressed by practitioners, with the support of policy makers and donors.

(2)Lesson-sharing on development of WRS and commodity exchanges:

During these sessions, practitioners will make presentations on the state of development of receipt systems and commodity exchanges, focusing in particular on the following:

- Achievements and challenges in the use of these instruments in the ESA region,;
- Emerging best practices as well as relevant lessons and experiences; and

⁷ The report does not reflect the view of UNCTAD. It has been circulated for comments and will be further reviewed based on the outcome of this Workshop.

- Evidence-based suggestions on how challenges can be addressed and/or successes replicated.

(3) Identifying opportunities and strategy for moving forward:

There will be parallel working group sessions, during which participants will discuss specific challenges and based on lessons shared, propose strategies to consolidate and build on successful initiatives as well as encourage uptake by other countries and regions. A panel discussion session will also be organised for managers of various programmes and representatives of relevant donor missions to outline how to strengthen links between their agricultural and trade development programmes and initiatives to promote market-based institutions so as to optimise benefits to key stakeholders in the region.

At the end of the workshop, participants are expected to endorse the conclusions and recommendations, which will highlight possible actions forwarding support of the development of viable WRS and exchange initiatives in the region. These recommendations will be linked to the objectives of ACTESA under the CAADP's Pillars 2 and 3 and to the strategic development of the regional agro-industries sector – and they will be submitted to development partners' consideration for funding. The EAGC in particular intends to use the recommendations of the workshop as a basis for reviewing plans adopted by their members to develop these market-based institutions. The background study commissioned by UNCTAD will be reviewed based on the outcome of the workshop, published and disseminated by UNCTAD.

ANNEX 1: The All ACP Agricultural Commodities Programme

The “All ACP Agricultural Commodities Programme” (AAACP) is an EU-funded programme that seeks to address “the commodity problem”. Its *overall objective* is to improve incomes and livelihoods for ACP (Africa, Caribbean and Pacific) producers of traditional or other agricultural commodities, and reduce income vulnerability at both producer and macro levels. The *specific objective* is to build the capacity of stakeholders all along the commodity value chain to conceive and implement sustainable commodity strategies. These will contribute to:

- enhance farmers’ productivity and competitiveness
- increase returns to labour
- reduce income fluctuations
- open up new market opportunities, including through diversification and
- facilitate recourse to market-based risk management instruments.

Eastern and Southern Africa Region Countries from the ACP

Eastern Africa ACP group of countries

Burundi
Comoros
Djibouti
Eritrea
Ethiopia
Kenya
Madagascar
Malawi
Mauritius
Mozambique
Rwanda
Seychelles
Somalia
Sudan
Tanzania
Uganda

Southern Africa ACP group of countries

Angola
Botswana
Lesotho
Namibia
Swaziland
Zambia
Zimbabwe

ANNEX 2: Regional Programmes and Partners concerned

The Alliance for Common Trade in Eastern and Southern Africa (ACTESA) was launched in September 2008 by COMESA as an answer to the food crisis. ACTESA is a regional alliance between COMESA, the EAC and SADC which aims to develop efficient and effective regional markets for staple foods.

It is intended that regional cross-border trade and partnerships will strengthen innovative market institutions and link food insecure smallholder farmers with growing national and regional markets. ACTESA is a multi-partner initiative led by COMESA which arose through the recognition that the growing structural food deficits in staple foods cannot continue to be indefinitely met by food aid.

The Alliance thus targets the enhancement of intra-regional trade of staple crops, principally maize, rice, cassava, banana and beans through enhanced policies (trade, investment, specific sectors), services (financial services, contract/arbitration services, grading/standards, market information) and commercialization (strengthen producers associations, traders, education/training, marketing, new technologies uptake).

The Comprehensive Africa Agriculture Development Programme (CAADP) was established by the African Union's New Partnership for Africa's Development (AU/NEPAD) in July 2003 with the overall goal to "help African countries reach a higher path of economic growth through agriculture-led development, which eliminates hunger, reduces poverty and food insecurity, and enables expansion of exports."

CAADP is a growth-oriented agriculture development agenda, aimed at increasing agriculture growth rates to six percent per year and at reaching the Millennium's Development Goal of reducing by half hunger and poverty by 2015.

CAADP focuses its interventions in four key pillars: • *Pillar 1*: Extending the area under sustainable land management and reliable water; control systems; *Pillar 2*: Improving rural infrastructure and trade-related capacities for market access; *Pillar 3*: Increasing food supply, reducing hunger, and improving responses to food emergency crises; and • *Pillar 4*: Improving agriculture research, technology dissemination and adoption.

COMESA is supporting the establishment of CAADP agreements at national level (called "Compacts") that will lead to a regional agreement (regional "Compact") highlighting the key policies, strategies and programs, existing gaps, required alternative investments, appropriate investment levels and necessary dialogue mechanisms for consistent broad based implementation of CAADP⁸.

The Agricultural marketing Promotion and Regional Integration Project (AMPRIP) has the goal to promote economic growth and foster regional economic integration in COMESA member states, and to enhance safe intra and extra COMESA-agricultural marketing. This AfDB supported COMESA programme focuses *inter alia* on the development of the regional Food and Agriculture Market Information System (FAMIS) through the capacity building of its regional and national focal points, the development and adjustment of the required

⁸ To date, Rwanda, Malawi, Zambia, Kenya, Uganda and Burundi have launched their CAADP country processes, and the other countries are in the process of establishing them.

software of the building up of the regional market information database. AMPRIIP also promotes the improvement and harmonization of sanitary and phyto-sanitary measures and food safety standards, while strengthening national and regional SPS institutions.

The African Agricultural Markets Programme (AAMP) was launched by the COMESA Ministers of Agriculture in 2008 with the aim to enhance capacity building, policy dialogue, and regional coordination on agricultural input and output markets in the Region. It is managed by the COMESA Secretariat in Partnership with the World Bank and supported by DIFID, and covers COMESA member and non-member countries (Ethiopia, Kenya, Malawi, Mozambique, Tanzania, Uganda and Zambia). By stimulating the use of policy instruments related to markets functioning enhancement, the Workshop's objectives directly match AAMP objectives: they both aim at sharing knowledge and lessons learned and at stimulating policy dialogue so as overcome obstacles that impede the development of regional commodities markets.

The "Programme for Building African Capacity for Trade (PACT) is an ITC executed and Canadian International Development Agency (CIDA) funded programme in which COMESA, ECOWAS and ECCAS are the leading regional partners. It aims at the promotion of policy dialogue among regional communities, and at championing regional trade development within and between the three African major sub-regions. It focuses on strengthening trade support networks, upgrading business skills and market linkages, and at promoting women as successful exporters. There is thus an obvious convergence of interest with the planned UNCTAD/COMESA collaboration on the enhancement of the functioning of regional commodity markets.

Competitiveness and Trade Expansion (COMPETE) Programme: builds on the success of two prior USAID programs, the Regional Agriculture and Trade Expansion (RATES) program and the East African Community Trade Hub. By combining the best aspects of these programs, COMPETE takes a holistic approach to addressing the constraints and promoting the opportunities available to African companies to increase their competitiveness and trade with the United States and global markets. It will work to:

- Reduce barriers to trade;
- Increase competitiveness and market access in selected value chains including staple foods, and
- Increase trade and investment between the U.S. and Eastern and Central Africa (ECA) via the ECA Trade Hub.

COMPETE will partner with private sector-led Regional Trade Associations, COMESA and the EAGC to enhance competitiveness and trade in targeted sectors and create tools that will allow small farmers to participate more effectively in regional trade. The goal is to reduce barriers to trade and help firms adopt international quality standards that make them more competitive in regional and global markets.

ANNEX 3: The region's agricultural commodities markets

The All ACP Agricultural Commodities Programme has ranked in 2008 68 agricultural products for the group of 7 Southern African ACP countries, and 86 agricultural products for the group of 16 ACP Eastern African according to their potential for growth. This ranking is based on a combination of indicators relative to world market trends, import dependency, and current export and production performance.

For *Southern Africa*, the results are the following:

The top five products in terms of high and accessible international demand (*World Market Index*) are Maize, Oil palm fruit, Green coffee, Wheat, Soybeans, and Bananas and plantains.

The top five products in terms of the relative *importance of imported products (Import Index)* are Maize, Dry cow peas, Sorghum, Oil palm fruit, and Dry beans.

The top five products in terms of *proven export performance (Export Index)* are Seed cotton, Grapes, Green coffee, Grapefruit, Pomelos, and Oranges.

The top five products in terms of *proven supply capacity and efficiency (Production Index)* are Cassava, other roots and tubers, other pulses, Millet, and dry Beans.

For *Eastern Africa*, the ranking is the following:

The top five products in terms of high and accessible international demand (*World Market Index*) are Maize, Green Coffee, green, Oil palm fruit, Bananas, plantains, and Wheat

The top five products in terms of the relative *importance of imported products (Import Index)* are Wheat, Lentils, Sorghum, Dry peas, and Oil palm fruit.

The top five products in terms of *proven export performance (Export Index)* are Sesame seed, Coffee, green, Seed cotton, Tea, and Beans.

The top five products in terms of *proven supply capacity and efficiency (Production Index)* are Tea, Sisal and other textile fibres of agave, Vanilla, Bananas, plantains, and Cloves⁹.

⁹ For more detail on the methodology and on the full analytical results, see the Trade Opportunity Scan for the Southern African Group of ACP countries and the Trade Opportunity Scan for the Eastern African Group of ACP countries, available on the website of the AAACP Programme : <http://www.euacpcommodities.eu/introen>