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CAMEROON FERTILIZER SUBSECTOR REFORM PROGRAM

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Background

In September 1987 the subsidized fertilizer subsector became the target of the Government of the Republic of Cameroon's (GRC) first efforts to scale back its involvement in commercial activities when it signed an agreement with USAID/ Cameroon to liberalize and privatize the importation and distribution of subsidized fertilizers under the Fertilizer Subsector Reform Program (FSSRP). Up through 1987 the GRC had relied on a system of public tenders and administered distribution to supply small holder farmers in the southern part of the country with five types of fertilizer -- three formulations of NPK, urea and ammonium sulfate. The purpose of the FSSRP has been to replace this public procurement system with a private system that is competitive, sustainable, and subsidy free.

To achieve this goal, the FSSRP contains three major policy thrusts: (1) subsidy elimination, (2) economic liberalization and (3) privatization. The *subsidy elimination plan* consists of a clear definition of the fertilizer subsidy and a timetable for its elimination over five years. In the first two years of the FSSRP, unit subsidies have declined over 70 percent.

Economic liberalization encompasses those actions necessary to dismantle the monopolistic public procurement system. Included in this component of the FSSRP are: elimination of public tenders, cancellation of import quotas, abolition of quantitative allocations to cooperatives and other eligible users, termination of distribution monopolies and abandonment of uniform pricing. These liberalization objectives were achieved in the first year of FSSRP as the GRC, through decrees and public statements, completely withdrew from direct involvement in fertilizer procurement and turned these functions over to the private sector.

Privatization involves replacing public procurement with a private system which will be sustainable, competitive and subsidy-free by the end of the program. Critical to establishing the new system are: (1) financial incentives which are sufficiently attractive to induce sustained private sector participation, (2) new institutional arrangements[1] that enable economic operators to function with minimum transaction costs and (3) increased private entrepreneurial capacity. This article will not further discuss the importance of institutional arrangements and promotion of private entrepreneurial capacity in FSSRP's privatization process.[2]

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[1] Institutional arrangements are defined here as the full range of formal and informal rules, regulations, procedures and incentive sets in the economic, political and social spheres that guide human interaction.

[2] For a detailed discussion of these elements, see: Tham V. Truong and S. Tjip Walker, "Policy Reform as Institutional Change: Privatizing the Fertilizer Subsector in Cameroon" in Derick W. Brinkerhoff and Arthur A. Goldsmith (eds.) Institutional Sustainability in Agriculture and Rural Sustainability in Agriculture and Rural Development: A Global Perspective. New York: Praeger, 1990.

Turning to financial incentives, three are paramount: a differentiated pricing structure, a revolving credit fund and the subsidy fund. Differentiated pricing allows for variations in prices that reflect nutrient value, distribution costs, risk, and, thus, marketing margins. The credit fund (capitalized with USAID's grant money) provides working capital at preferential interest rates to fertilizer importers and distributors and redresses growing liquidity problems in the commercial banking structure caused by the continuing economic recession in Cameroon. The subsidy fund (capitalized annually with resources from the GRC's budget) enables commercial banks and importers to reduce commercial risks and lowers the retail price to farmers. The FSSRP's subsidy fund and revolving credit fund are managed by a designated fiduciary bank under contract to the GRC. This arrangement removes the government from the day-to-day management of the subsidy and credit funds.

Each of the three incentives have served its intended purpose. However, the role of the subsidy fund has been the most surprising. Not so much in its role of moderating increases in retail prices as the subsidy has been gradually removed, but in its role as a form of guarantee to commercial banks and importers. Under the FSSRP, the appropriate subsidy amount is disbursed by the fiduciary bank to an importer's commercial bank once a shipment has arrived at the port. It is these commercial banks which bear all the commercial and credit risk associated with fertilizer importation. As the subsidy payment is sure and automatic, commercial banks have treated the subsidy payment essentially as an inter-bank guarantee. And as the subsidy payment has represented approximately 60 percent of the value of a letter of credit to cover fertilizer imports in 1988 and 40 percent in 1989, the availability of this "guarantee" has significantly lowered the apparent risk of fertilizer financing while simultaneously lowering the requirements that the banks demand of importers in order to cover the remaining value of the letter of credit.

Impact

The impact of the privatization measures has been the active participation of the private sector in financing, importing, and distributing fertilizer. Table 1 shows that essentially the same amount of fertilizer was imported in each year that FSSRP has operated as was imported under the last year of the public monopoly. As can be seen from Table 2, private sector interest in the FSSRP has remained steady over the first two campaigns. Indeed the increase in 1989 in the number of both private cooperative and "for-profit" distributors and in the number of provinces covered has been particularly encouraging. At the same time, it has become clear that the limited size of the FSSRP market constrains competition at the importation level. For this reason the GRC is moving ahead to merge the FSSRP with an European Economic Communities'-financed program in northern Cameroon in 1991. This will increase the market by about a third to approximately 100,000 tons per year.[3]

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[3] Once the subsidy has been totally removed from these two programs and merged with the existing unsubsidized sector, Cameroon will have a single unsubsidized market of around 115,000 to 125,000 tons.

[Tables 1 and 2 about here]

In addition to concerns about private sector participation, the GRC is also interested in the impact that FSSRP has had on government revenue and retail prices. Continued GRC commitment to the process of liberalization and privatization can only be ensured if FSSRP yields budgetary savings for the GRC and tangible benefits to farmers. For these reasons FSSRP is monitoring the subsector closely. At the end of each campaign, annual reviews are undertaken and both achievements as well as problems were discussed in an open forum grouping representatives of the GRC, commerical banks, private fertilizer importers and distributors and USAID.

Table 3 shows that compared to the last year of operation of the public monopoly in 1987, total GRC budgetary savings have amounted to FCFA 8.5 billion (US$ 28 million) as unit subsidies have been cut over 70 percent in two years.[4] However, declines in the subsidy rates have largely been offset by gains in efficiency at both the importation and distribution levels brought about by market forces. Total delivered cost to the farmgate has declined 37.8 percent in two years, with both CIF import prices and internal distribution cost registering drops of over 30 percent. As a result, the average retail price to farmers has increased only 28.4 percent over the same period.. In fact, one large cooperative is selling fertilizer in 1989 at the same prices as those in 1987 when the subsidy was three times as high.

[Table 3 about here]

Rivaling the importance of the efficiency gains achieved so far has been the increase in the timeliness and certainty of fertilizer delivery. Interviews with retailers and end users underscore the importance of product availability in maintaining demand. FSSRP project data show that the time between orders and delivery has been reduced from 12-18 months to 4-6 months since private contract have replaced public ones.

For these reasons, GRC commitment to the FSSRP policy reform program remains strong. Despite very acute budgetary problems, the GRC has met its projected subsidy disbursements of FCFA 2.0 billion (US$ 6.7 million) in 1988 and FCFA 1.5 billion (US$ 5.0 million) in 1989.

Effects of the Economic Crisis

While FSSRP has, thus far, succeeded in inducing private operators to take over responsibility from the GRC for importing and distributing subsidized

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[4] The data presented in this article are drawn from the two annual review held to date. The findings are reported in Richard Abbott, Privatization of Fertilizer Marketing in Cameroon: First Year Assessment of the Fertilizer Sub-Sector Reform Program - Technical Report, Bethesda,MD: Abt Associates, June 1989 and Richard Abbott, Privatization of Fertilizer Marketing in Cameroon: A Second Year Assessment of the Fertilizer Sub-Sector Reform Program - Technical Report, Bethesda,MD: Abt Associates, June 1990.

fertilizer, continued progress is somewhat dampened by the economic crisis that has engulfed Cameroon since late 1986. Between 1987 and 1989 gross domestic product has declined by approximately 20 percent at current prices.

One manifestation of the economic recession is the accumulation of over FCFA 12 billion (US$ 40 million) in debts owed by produce marketing board to cocoa and coffee producers and their marketing cooperatives (approximately 80 percent of the fertilizer provided under FSSRP is destined for the small holder coffee sector). Exacerbating the debts was the 40 percent drop in producer prices for cocoa and coffee in 1989. With revenues from sales of coffee and cocoa representing, on the average, 50 percent of rural income, the existence of arrears and low producer prices has introduced considerable uncertainty in the demand for fertilizer.

In addition, the banking sector has acute liquidity problems due to bad loans (estimated at FCFA 300 billion or US$ 1 billion) and to arrears owed by the national produce marketing board (estimated at FCFA 24 billion or US$ 80 million). This lack of liquidity has tended to make Cameroon's already risk-adverse banks even more so and has limited the amount of credit available to fertilizer importers and distributors, despite the existence of FSSRP credit facilities.

On the positive side, Cameroon has been implementing its first Structural Adjustment Program (SAP) with the support of the IMF, World Bank and other donor organizations since 1988. The reforms envisioned in the SAP to liberalize the banking sector and the marketing of coffee and cocoa will enhance the chance of success of FSSRP and its sustainability.

Table 1. Comparison of Imports, 1987 - 1989

	Public Monopoly	Fertilizer Sub-Sector Reform Program	
	1987	1988	1989
Total Imports (tons)	64,000	63,000	64,171
Of which:			
NPK 20-10-10	unavailable	26,300	23,230
NPK 12-06-20	"	12,000	2,000
NPK 10-30-10	"	0	0
Urea	"	12,200	24,941
Ammonium Sulfate	"	12,500	14,000

Table 2. Private Sector Participation in FSSRP

	1988	1989
Fiduciary Bank	1	1
Accredited commercial banks	4	4
of which actually participated	2	2
Active importers	14	10
of which actually imported	3	2
Active distributors	6	16
of which actually distributed	4	10
of which are cooperatives	4	6
of which are "for-profits"	0	4
Provinces covered (out of max. 7)	3	5

Table 3. Comparison of Marketing Costs, 1987 - 1989

	Public Monopoly	Fertilizer Sub-Sector Reform Program		Total Pct. Change
	1987	1988	1989	
1. Subsidy disbursed (FCFA billion)	6.0	2.0	1.5	-70.8%
2. Average unit subsidy (FCFA/ton)	88,600	31,504	24,923	-71.9%
3. Actual subsidy rate (row 2/row 4)	66.2%	36.2%	30.1%	
4. Total delivered cost (FCFA/ton)	133,600	86,939	82,699	-38.1%
Of which:				
Avg. CIF cost (FCFA/ton)	97,600	57,216	57,872	-40.7%
Avg. distribution cost (FCFA/ton)*	36,000	29,723	24,827	-31.0%
5. Avg. retail price (FCFA/ton)	45,000	55,435	57,776	28.4%

Note: * Average distribution costs include importers' margins.