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Consultancy Report
Quarterly Progress Report: January - March, 1994

Central Asia: Food Systems Restructuring Project
CCN-0006-A-00-3072-00

Prepared for:
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March 31, 1994

**AGRICULTURAL COOPERATIVE DEVELOPMENT INTERNATIONAL
FOOD SYSTEMS RESTRUCTURING PROJECT
GRANT NO. CCN-0006-A-00-3072-00
PROGRAM PERFORMANCE REPORT
JANUARY - MARCH 1994**

PROJECT PERFORMANCE

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I. Summary

Implementation of the Food Systems Restructuring Project continued as planned during the quarter. ACDI made a significant marketing effort in the U.S. with mixed success and participated in AgroWorld '94, an international food processing exposition held for the first year in Almaty, Kazakhstan. At the show a number of significant contacts were made with Kazakhstan and Kyrgyzstan enterprises and also with U.S. companies doing or wanting to do business in Central Asia.

Koch Supplies, a company that responded to our marketing effort in the U.S., started a technical assistance project to modernize the dairy industry in the Almaty Oblast. This was the first FSRP subgrant financed project in Central Asia. A key feature of this effort is to achieve the demonopolization and privatization of this crucial food sector as a prerequisite for a Koch equity investment.

Opportunities in Taldy Kurgan Oblast and Kryrgyzstan were explored with two profiles now being developed for the former.

II. Comparison of Actual Accomplishments with Period Goals

a. Project Purpose and Strategy

To develop a private agribusiness sector by establishing long-term linkages in the region between U.S. companies and private or privatizing Central Asian partners.

b. Highlights and Actions During the Quarter

ACDI made a significant marketing effort to promote U.S. agribusiness involvement in Central Asia. Approximately 300 letters and packets were mailed to selected member and non-member agribusinesses. Ken Bader, Jerry Bahensky, and Steve Gardner met with seven companies in Minneapolis-St. Paul in January. Jerry Bahensky addressed the annual meeting of the National Council for Farmers Cooperatives where another 250 packets were handed out. The packets contained information about the business environment in Kazakhstan and profiles for eight different investment opportunities. Our office in Washington continues to follow-up on a number of inquiries.

In general, the cooperative sector has been very reluctant to expand internationally. Those that do have international activities have been reluctant to explore possibilities in Central Asia. The large private sector agribusinesses are presently highly involved and have some interest, but have maintained a degree of independence from government funded programs. However, the medium to small-sized agribusinesses have shown more interest. ACDI's goal of sending six specialists to technical assistance subprojects during the quarter fell short by three people.

Out marketing efforts in country were aided by ACDI's participation in AgroWorld '94, the first international food processing exposition to be held in Almaty. Many contacts were made with organizations all over Central Asia. Participating in the show was a very cost-effective endeavor for the FSRP in terms of the time saved by having businesses from all over Central Asia come to Almaty for an initial screening. Also, the present fuel shortages have hindered incountry travel and made scheduling difficult to predict. Another advantage of the show was to be able to interface with U.S. company participants who are or want to do business in Central Asia. Steve Gardner, Project Coordinator, traveled to Almaty to assist with the show as well.

During his first trip to the region, Mr. Gardner received first-hand knowledge of the business environment in Central Asia, which should be helpful for marketing the FSRP to companies in the U.S. He also helped facilitate and participated in ACDI's first technical assistance subproject by visiting several plants and dairy farms in the Almaty Oblast and meeting with their managers and regional oblast officials. In addition, the trip allowed headquarters to coordinate many project administrative matters with the field office.

ACDI has been working closely with the USDA to facilitate an investment and trade mission to Central Asia during the Fall of 1994. Last year, Jerry Bahensky met with Dave Schoonover from Moscow and in January of this year the FSRP team met with Doug Freeman in Washington to develop the action plan for a USDA sponsored mission. The mission is regarded as a key marketing effort for the FSRP, as it will involve a number of U.S. companies seriously interested in investing in the region.

Koch Supplies, a firm from Kansas City, Missouri, began the modernization plan development for the dairy industry in the Almaty Oblast. This is the first subgrant funded by ACDI's FSRP. The objective is to determine how the industry can be modernized with Koch becoming an eventual equity investor. A key feature is to demonopolize and privatize this crucial food sector using investment as a motivator. The progress of Koch's first visit is outlined in the attached executive summary prepared by Project Director Jerry Bahensky for the mission in Almaty.

III. Actions Planned for Next Quarter

During the next quarter, ACDI will continue to assist Koch Supplies in the modernization plan development of the dairy industry in Almaty Oblast. Jerry Bahensky will keep AID/Almaty informed on the status and direction of this project. The activity is expected to be culminated by a subgrant-funded trip to the U.S. by two or three representatives from Almaty in late summer. The purpose is to give the Kazakhstanis an opportunity to observe the U.S. dairy industry and finalize a joint venture subgrant proposal to be submitted for funding under the FSRP.

ACDI's Executive Director of NIS Operations, Michael Moran, has been invited to speak on the agribusiness panel for the Department of Commerce's U.S.-Central Asia: Partnership for Economic Progress in early May. Hundreds of U.S. businesses are expected for the two day forum. At Mr. Moran's presentation, ACDI will set up a table to hand out promotional packets and to answer questions and promote the FSRP.

Ken Bader will focus his efforts on identifying U.S. agribusinesses which have an investment (or an interest in investment) in the vegetable oil industry in Kazakhstan. Two companies that ACDI is currently promoting, the sunflower oil plant in Ust Komenagorsk and the cotton seed oil plant in Chimkent, are the country's only vegetable oil producers. They are open for tender in conjunction with the privatization program. Company profiles for each are being prepared.

Headquarters and field staff will continue to collaborate with the USDA to organize the upcoming mission for potential investors in the food processing industry in Central Asia. An evaluation team is scheduled to arrive in June with the mission to follow in September.

Develop at least one project profile for the apple industry which would lead to finished product export. Nearly 40% of the apple crop spoils either on the tree or in storage. Kazakhstan has a large surplus of apples, many apples could be packaged for consumption throughout Central Asia and in Russia.

Also during the quarter, Jerry Bahensky will travel to North Kazakhstan and to Kyrgyzstan to identify and evaluate enterprises to promote under the FSRP.

IV. Additional Observations and Comments

In January, the Kazakhstani Government began revising the tax laws in a manner that could hinder the sorely needed foreign investment in the food processing industry. The U.S. Embassy personnel and various USAID contractors have been working with government officials to dramatically revise the regulations under consideration. Another very significant government action during this quarter was the forgiving of the loans to state and collective farms by President Nazerbaev. This action helped to speed the rapid devaluation of the Tenge. In less than two months the exchange rate went from 13T : \$1 to 26T : \$1. Neither of these events will aid private sector development in the country.

ACDI recently hired Jim White, an attorney from Michigan, who has represented many food processing companies as well as cooperatives. Over the next two years, he will provide support and develop projects for ACDI in Central Asia. Two initial assignments include working with the EBRD and representing ACDI on the Joint Commission set up in March in Kyrgyzstan. He begins his assignment on April 30th. Mr. White will monitor the changing laws which impact agriculture and more specifically the food processing sector and possibly lend expertise in the land titling issues which Kazakhstan is just now addressing.

At AgroWorld '94, ACDI offered Mercy Corps and VOCA the opportunity to distribute literature from the booth and meet with prospective participants for their programs. This approach worked well for all three organizations. For visitors who were interested in lines of credit or basic technical assistance, ACDI was able to offer immediate information about other U.S. government-funded programs. Both Mercy Corps and VOCA have reported that many good contacts resulted from their participation.

V. Expenditures Through March 31, 1994

There have been no financial problems during the reporting period. Below is a summary financial statement of all project expenditures by subcomponent. The last quarterly report errantly listed budget amounts for the first budget dated 4/30/93. This report gives the correct figures from the approved, revised budget dated 9/28/93. The actual expenditure totals are based on estimates of expenditures through the end of the reporting period.

	Budget	Actual	Unliquidated
Salaries	787,280	98,422	688,858
Fringe Benefits	186,745	23,281	163,464
Allowances	121,233	62,291	58,942
Travel/Transport/PD	295,428	56,031	239,397
Consultants	185,758	7,033	178,725
Equipment	58,500	49,002	9,498
Other Dir. Costs	193,600	42,739	150,861
Indirect Costs	669,248	124,000	545,248
Subcontracts	<u>2,502,168</u>	<u>2,500</u>	<u>2,499,668</u>
Totals	4,999,960	465,299	4,534,661

ADMINISTRATIVE DATA

Region: NIS/Central Asia
Implementing Agency
Point of Contact: USAID/NIS/TF/PSI
Contractor: Agricultural Cooperative Development International
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Period of this Report: January - March 1994
Period of last Report: October - December 1993
AID Project Officer: Laurie Mailloux
Date Authorized: May 6, 1993
Estimated Completion: May 5, 1997
Total Project Cost: \$5,000,000
NIS Project Director: Gerald Bahensky
Employees in Country: Four
Project Office Address: ACDI
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Executive Summary of Dairy Technical Assistance Project for Almaty Oblast - "Jiger" (formerly the Milk Association)

On March 22, 1994, a team of specialists from Koch Supplies of Kansas City, Missouri, arrived to conduct a technical assistance project that was partially funded through a subgrant from the USAID/ACDI Food Systems Restructuring Project. The objective was to begin the process of developing a modernization plan for the milk industry in the Almaty Oblast which is primarily managed by the joint stock company "Jiger". Another objective was to build a business relationship between the two companies which would have the potential of future investment by Koch. Jiger is made up of 9 milk plants and the dairy operations of 81 collective and state farms. It is owned by the milk producers (51%), workers in the plants (38%), a bank (2%), and (9%) unallocated. It was certified to be privately owned and managed in a private manner.

Seven days of intensive study revealed the following:

1. Capital for massive investment, which Jiger does not have, will be required to modernize the industry to meet world standards in terms of product quality.
2. The large plants in the city of Almaty are in immediate need of packaging systems, but the plants themselves will need to be replaced near term. Jiger was advised not to make major plant investments at this juncture and instead build their cash reserves. When the time comes that rebuilding of the plants is a necessity, Jiger could more easily find a foreign partner.
3. Some of the smaller plants have a longer life expectancy and have some potential of adding value-added products such as hard cheese and condensed milk.
4. Milk production is dropping at an alarming rate. There is an inadequate amount of capital to invest in feed harvesting and processing equipment, crop production inputs, feed storage, and feed concentrates, as well as improved genetics and milking equipment.
5. State interference in the production, pricing, and marketing of milk is exacerbating an already difficult economic situation. The establishment of production goals at lower than cost of production and processing is a primary cause of lower production, poorer product quality, a demoralized and underpaid work force, and the emergence of an uncontrolled

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- (in terms of quality) private retail system.
6. The dairy product needs of the Almaty Oblast will probably not be able to be met in the near future without a significant restructuring of the industry.
 7. It appears that Jiger management is unstable and participation with them in a partnership or joint venture might be unwise.

Koch Supplies and the Regional Oblast Administration have agreed that Koch will develop a modernization plan for the Chilik Raion as a first step toward Koch's investment in a joint venture with the milk producers and processors (excluding Jiger) of that area. Conditions of the potential joint venture are to be as follows:

1. Koch will make a best effort to identify very low-cost packaging equipment for the two milk plants in Almaty. The equipment will likely be used.
2. The potential joint venture will be able to produce, process, price, and market dairy products free of any state interference with the exception of meeting state quality standards.
3. The potential joint venture will compete directly with Jiger with most products going to the city of Almaty.
4. Initial products will be fluid milk with a longer shelf life, condensed milk, hard cheese, kafil, ice cream, and cream.
5. The joint venture will develop their own retail system and marketing scheme.
6. The modernization plan will be comprehensive in that it will include all phases of the business including production of feed and the crops that make up the feed.
7. Koch is anticipated to be a major investor if the joint venture is consummated.

A protocol is now being drafted and a team from Koch Supplies plan to return about the end of April to complete the modernization plan. USAID Private Sector Office/Almaty and ACDI Project Management/Almaty are pleased with the progress of this technical assistance project.



Gerald Bahensky
Project Director
Food Systems Restructuring Project

April 4, 1994

cc: Craig Ruck, Director, USAID
Lyn Dunn, USAID
MaryAnn Hoirup-Bacolod, USAID
Craig Carp, Commercial Office, US Embassy