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PRIVATIZATION OF FERTILIZER DISTRIBUTION IN BANGLADESH

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USAID's assistance to Bangladesh's fertilizer sector involves six projects dating back to 1974 and totalling \$430 million (see Table 1 below). These projects have financed fertilizer imports, warehouse and factory construction, and support for marketing improvements. In early 1978, officers of the Bangladesh Agricultural Development Corporation (BAIC) held meetings with USAID on how to improve the marketing system of fertilizer. As a result of these discussions, BAIC, with the approval of the Bangladesh Government, decided to try a new system of distribution in one quarter of the country for one year. If the new system proved successful (which it did), it was to be extended throughout the country (which it was). Through the Fertilizer Distribution Improvement I (FDI-I) Project, USAID provided assistance in this endeavor with the purpose of increasing fertilizer use through a new marketing system.

Fertilizer Distribution Improvement I

FDI-I is basically a policy reform project with a focus on entry of the private sector into fertilizer distribution and marketing. With marketing technical assistance, the project provides \$150 million of fertilizer imports and \$70 million of fertilizer warehouse construction as leverage for the policy reform needed to privatize the nation's fertilizer distribution system at the local retail level. The Mission strategy encourages this private sector participation as a cost effective means to more rapid national economic growth. The goal of FDI-I is to increase foodgrain production through the increased use of fertilizers. When FDI-I began in 1978/79, foodgrain production totalled 13.3 million metric tons. In 1983/84, this figure reached 15.7 million metric tons. Fertilizer sales increased from 754 thousand metric tons in 1978/79 to 1.1 million metric tons in 1983/84 nearly a 50 percent increase over the 5 year period (see Figures 1, 2, and 3 below).

The fertilizer distribution system which was in place before FDI-I is referred to as the Old Marketing System (OMS). Under the OMS, BAIC distributed fertilizers from factories and ports to intermediate godowns (warehouses), Thana Sales Centers (TSCs), and Thana Central Cooperative Association (TCCA) godowns. The intermediate godowns served as supply depots for the country's 448 TSCs and TCCAs. Sales to fertilizer dealers were made only from the TSCs and TCCAs. All dealers were appointed by BAIC only after approval by a thana committee composed of BAIC's thana inspector, the thana extension officer, the local union council chairman and an officer representing the deputy commissioner at the thana level. On approval of this committee, a memorandum of agreement between the dealer and BAIC was drawn up. The dealer could purchase fertilizers only from the

TSC or TCCA at which he was registered and could sell his fertilizer (at retail prices fixed by the Government) only in his specified union. To compensate for transportation costs by dealers, Government-administered-dealer-commissions were established and determined by the distance of the dealer's shop from the TSC or TCCA warehouses.

The principal focus of the New Marketing System (NMS) was on the mitigation of fertilizer market related constraints. The original concepts of the NMS were as follows: a) allow any person, group, or organization to register as a fertilizer dealer without restrictions, b) provide quantity discounts to attract and create wholesalers, c) remove location restrictions and permit any individual or group to buy, sell, or transport fertilizers anywhere in the country, and d) encourage institutional dealer/farmer credit programs. In addition, there was a commitment that BAIX was to 1) develop a new staffing pattern and organizational structure which would complement the NMS, and 2) develop and implement a dealer training program. Furthermore, the Government agreed to deregulate retail prices nationwide in phases and to consolidate its sales outlets to roughly 100 major commercial centers or primary distribution points (PDPs), rather than having BAIX transport fertilizers to each of the country's 448 agricultural thanas.

During initial stages of the NMS, uniform commissions for dealers were established at PDPs, and minimum lifting levels were imposed. Quantity discounts were introduced in 1982, when private fertilizer wholesalers were sanctioned and permitted roughly a one percent discount. At the same time the retail prices of fertilizers were deregulated in one quarter of the country. One year later, dealer commissions were eliminated as retail price decontrol went into effect nationwide.

Perhaps, FDI-I's most significant contribution to development of Bangladesh's fertilizer sector has been the introduction of the NMS. The development of an expanded, proficient, and competitive private dealer network is the cornerstone of the NMS. Both the Joint Bangladesh and U.S. Government Evaluation of the Fertilizer Distribution Improvement Project I, November 1982, and the IFDC Third Evaluation of the NMS, March 1982, have concluded that under the NMS, Bangladesh's private sector has successfully demonstrated the potential for marketing fertilizers at the retail level and that private dealers have established a reliable marketing network which could be utilized by large-scale private wholesalers.

The effectiveness of the NMS has depended upon its ability to make fertilizer available to all categories of farmers on an equitable basis. An USAID-funded study* of four crop seasons indicated that the proportion of small farmers (less than 2.5 acres) using fertilizer was approximately the same as that of the larger farmers, and that small farmers used slightly more fertilizer per acre and obtained higher output per unit of fertilizer than larger farmers. This is indicative of the relative equity of fertilizer use in Bangladesh.

* IFDC, "Agricultural Production, Fertilizer Use and Equity Considerations (Results and Analysis of Farm Survey Data)." Bangladesh 1982.

On BADC's own initiative and using its own funds, BADC hired a local firm to evaluate the New Marketing System for fertilizer. The following is a quote from this report, dated June 1983: "Given the reliability of data collected and the method used by us, three conclusions stand out: First and large, the NMS seems to have ensured relatively lower prices to the farmers. Second, the remote farmers are not relatively worse off because of the NMS. Third, the effects of price deregulation in Chittagong Division have been more or less similar to those of price regulation in the Rajshahi Division."

The (August 1983) Assessment of the Agricultural Sector in Bangladesh, by Dr. E. Boyd Wennergren (et al.) of Utah State University, concludes the following: "The Mission's commitment to fertilizer development was well-founded, especially the emphasis given to policy reform which has led to development of the New Marketing System and towards privatization of the distribution process." Overall, FDI-I has accomplished its primary objectives and is viewed by the Bangladesh Government, USAID, and other international donors and lenders as a success. Over the past five years, increased foodgrain production and increased fertilizer sales (see Figures 1, 2, and 3) attest to this success.

Fertilizer Distribution Improvement II

The next step in the evolution of Bangladesh's fertilizer marketing system will be the development of large-scale private wholesalers with a potential for nationwide distribution and sales of fertilizers. With the goal of increasing agricultural production through increased fertilizer consumption, USAID's Fertilizer Distribution Improvement II (FDI-II) Project will continue the process of developing greater private sector involvement in the distribution of fertilizers. Under FDI-II, the Government will reduce substantially its number of fertilizer sales outlets and will eventually allow private wholesalers to purchase fertilizers at the factories and ports thus ending the Government's monopoly in this area.

By building upon the foundation set by FDI-I, FDI-II is aimed at the successful conclusion of reducing the resource burden that the Bangladesh Government presently incurs from executing its fertilizer distribution function. FDI-II is a policy reform project which offers \$65 million of assistance as an incentive for the Government to fulfill the conditions of the project, i.e. allowing development of large-scale private wholesalers. The project funds which are to be obligated over five years may be used for the following: (1) a fertilizer wholesaler and retailer credit program and/or fertilizer imports (\$52 million), (2) technical assistance and training (\$6 million), and (3) small infrastructural improvements to ease physical constraints in the distribution network of fertilizer wholesalers (\$7 million).

During the past year, implementation of FDI-II has been delayed both by BADC and a national fertilizer shortage. In November 1984, national fertilizer buffer stocks reached a critically low level which has recently been corrected with stocks presently approaching recommended levels.

BADC's concerns regarding FDI-II have centered around job security for its employees. BADC distributes fertilizer, HYV seeds, and irrigation equipment. It has approximately 25,000 employees of which only 4,000 are involved with fertilizer. However, BADC's fertilizer sales generate more revenue than its irrigation and seed divisions combined. In fact, BADC's fertilizer revenue helps to finance the other BADC activities. Therefore, the majority of the BADC employees have felt threatened by FDI-II which is expected to substantially reduce BADC's scope of activities in the fertilizer sector.

Due to BADC's resistance and the political concern it has generated, FDI-II's development has been extremely slow as indicated by the following:

<u>Event</u>	<u>Date</u>
PID approved	September 1982
PP approved	March 1984
PROAG signed	August 1984
Initial CPS met	Has not occurred

As of this writing, indications are that FDI-II implementation will commence soon. Initiating implementation may require further negotiations and adjustments in initial CPS; however, project objectives will remain intact.

The FDI-II PID which was shared with BADC and the Bangladesh Government and which was praised by AID/W for being thorough and well written was extremely blatant regarding the fate of BADC under the proposed project. The PROAG was signed at a time convenient for AID funding cycles and before the Bangladesh Government and BADC were in agreement regarding elements of the project. At the Government's request, the PROAG signing took place without the usual public announcement. Perhaps two lessons can be learned from the development of FDI-II. First, the AID/W version of the PID should not have been shared with BADC and the Government. Secondly, in terms of project implementation nothing was gained by the premature signing of the PROAG.

Summary and Conclusions

In summary, FDI-I has (i) developed large-scale private retailers and small-scale private wholesalers, (ii) supported sales promotional training and materials for fertilizer dealers, and (iii) encouraged private sector involvement with bagging of bulk imported fertilizers and the distribution of gypsum (a byproduct from the country's TSP factory) as a sulfur fertilizer. FDI-II will develop large-scale private fertilizer wholesalers

who are expected to utilize the existing network of over 20,000 fertilizer retailers. The reformed fertilizer marketing system under FDI-II is founded on the firm belief that if given the opportunity, the private sector will be just as successful at the national wholesale level as it has been at the local retail level.

Generalizing from USAID/Dhaka's experience with the development of FDI-II, the following conclusions emerge: 1) Policy dialogue is a long-term process which requires much patience; 2) This process requires mutual trust and understanding; 3) If ultimate goals are potentially shocking or threatening, they should be revealed slowly; 4) Since means to ends are negotiable, ultimatums should be avoided; 5) Successes should be anticipated only in small increments; 6) The continuity of negotiators as well as the country's political conditions are critical factors which can affect the policy dialogue process; and 7) A bilaterally signed PROAG offers little, if any, assurance that a project implementing agency will act in accordance with the agreement.

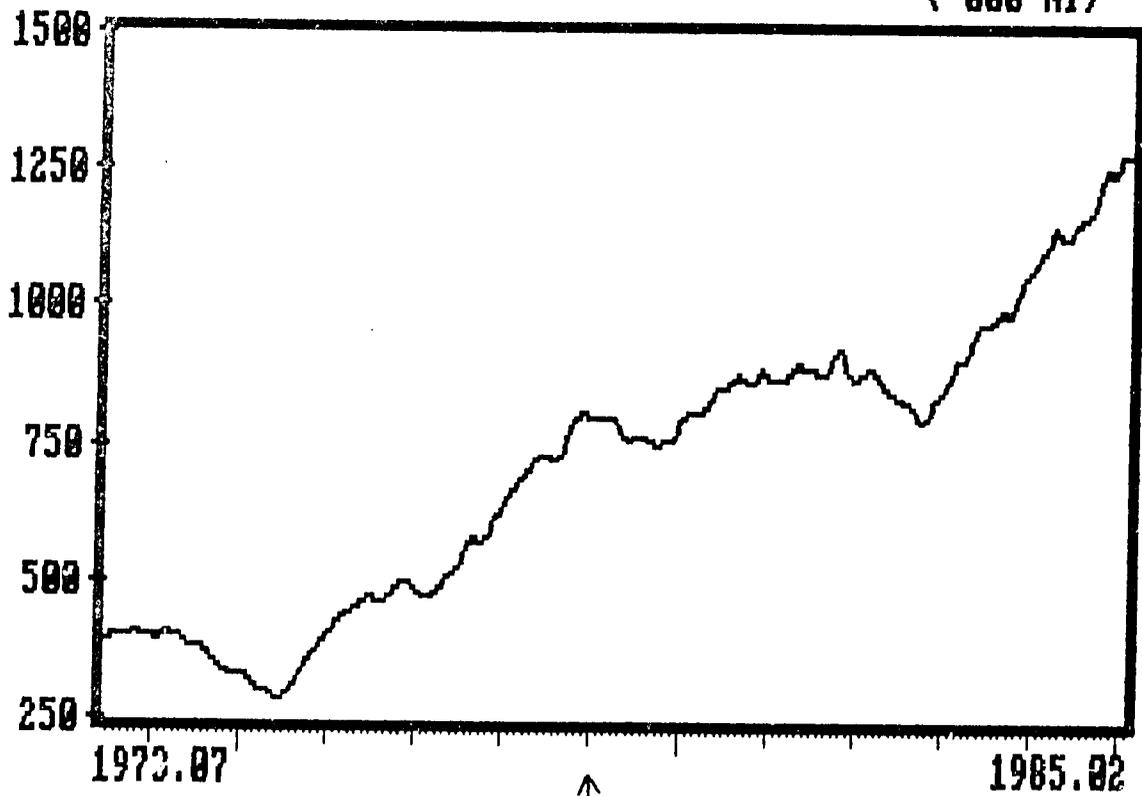
Table 1. U.S. Assistance to Bangladesh's Fertilizer Sector

	<u>Dates of Funding Obligations</u>	<u>Major Project Activities</u>	<u>Amount of Assistance (in \$ million)</u>
1.	1974-75	Fertilizer Imports	55
2.	1975-78	Zia Fertilizer Plant	53
3.	1976-77	Warehouse Construction	5
4.	1977	Fertilizer Imports	27
5.	1978-82	Marketing Improvements Fertilizer Imports Warehouse Construction	225
6.	1984-88	Marketing Improvements Fertilizer Credit/Imports Infrastructural Improvements	65
		Total:	430

Items 5 and 6 are on-going projects entitled, Fertilizer Distribution Improvement One and Two, (FDI-I and FDI-II) respectively. The goal of both projects is to increase agricultural production through increased fertilizer use. These objectives are being achieved by increasing the role of the private sector in the distribution of fertilizers.

FIGURE 1.

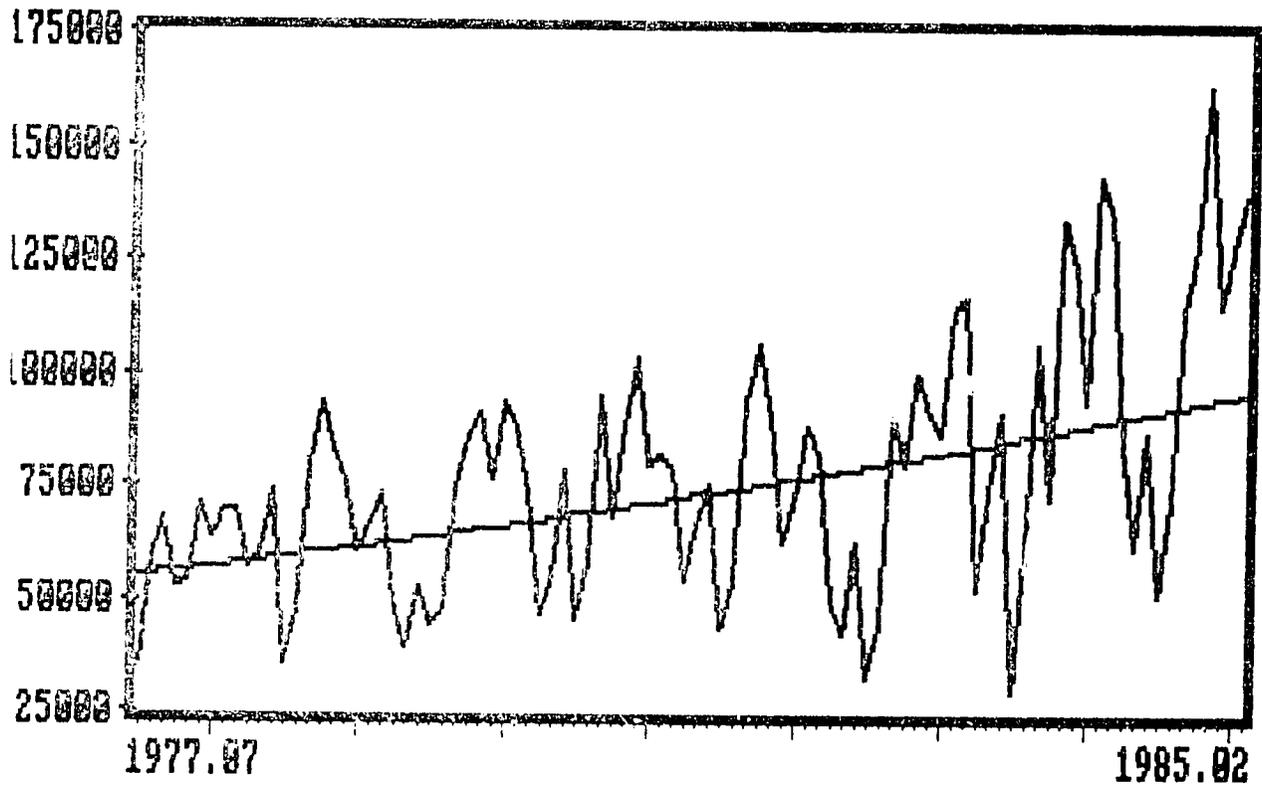
Fertilizer Sales by 12-month moving totals, 1973/74-1984/85
(' 000 MT)



INTRODUCTION OF
NEW MARKETING SYSTEM

Figure 2.

Monthly Fertilizer Sales and Long-run Trend Line (7%/Year)



2-

FIGURE 3.

FERTILIZER PRICES AND SALES BY 12-MONTH MOVING TOTALS 1978/79 - 1984/85

