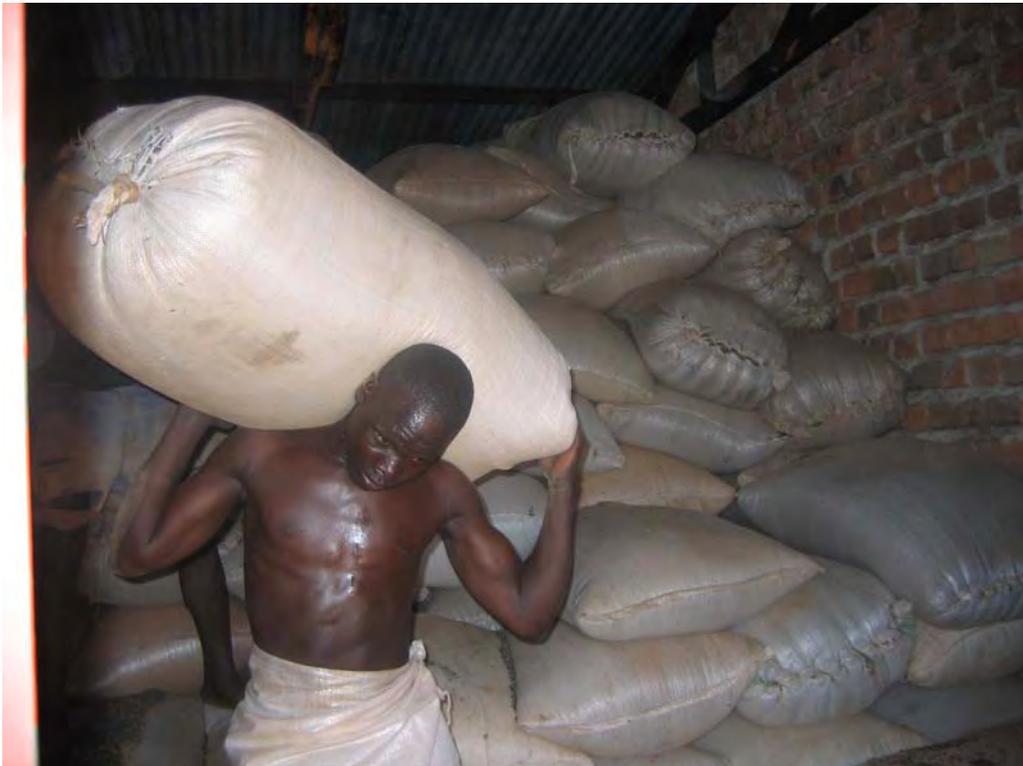




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FROM THE AMERICAN PEOPLE

A REVIEW OF CURRENT AND POTENTIAL PRACTICES FOR WAREHOUSE RECEIPTS IN UGANDA

FINAL REPORT



February, 2006

This publication was produced for review by the United States Agency for International Development. It was prepared by Kenneth L. Peoples of PRIME International, subcontractor for Chemonics International Inc.



Rural SPEED

Rural Savings Promotion & Enhancement of Enterprise Development

A REVIEW OF CURRENT AND POTENTIAL PRACTICES FOR WAREHOUSE RECEIPTS IN UGANDA

FINAL REPORT

The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

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Executive Summary

Developing public warehousing of agricultural commodities for enabling the use of warehouse receipts to facilitate financing production and trade is challenged by the productive conditions, the weak and erratic demand for the commodities to be stored, the local commercial course of dealing, and the infrastructure to facilitate storage, transport and trade. Ugandan market conditions are so challenging that it is readily understandable why commercial public warehouses have not previously appeared. The supply side of the Ugandan maize industry is characterized by a large number of small farmers cultivating an average of 1 to 2 tons per hectare for an annual production of about 530,000 metric tons. Much of the annual production is marketable surplus dependent upon variable factors that Ugandan farmers cannot perceive at planting time. So they plant a limited amount of maize as a cash crop for visiting village traders.

The demand side has few buyers—the World Food Program (WFP), Kenyan importers, Uganda public institutions (prisons, army, etc.), and some Ugandan consumers. All want inexpensive maize, and only the WFP has shown interest in paying for quality maize of good color and low moisture. The WFP has difficult timing and procurement conditions, and the Kenya importers are fickle buyers from year to year depending on the quantity of the Kenya maize harvest.

The fragmented maize trading community buys maize from farmers with cash at the farmgate. From there, each farmer's small production is slowly aggregated from the village traders through several hands until it lands in the stores of a couple dozen trading firms in Kampala. The process is slow, cumbersome, and not oriented toward preserving quality. By the time the Kampala trader receive the grain, cleaning and drying does not improve the quality much.

From producer to Kampala trader, the marketing chain is thinly capitalized. Traders have bid and won contracts without having ready stock for fulfillment. Instead, they finance the contracts with Ugandan banks to have funds to purchase the contract grain through the myriad networks of local and village traders. Banks are only willing to finance the grain contracts provided the traders store the grain in a warehouse managed by collateral management firms, which guarantee proper security, storage, and conditioning. Such fees significantly increase the cost of warehousing maize.

Over the past five years, the WFP has increasingly purchased more grain locally, and has made its intentions clear of trying to buy increasingly from producers directly to improve the maize quality by paying a premium. For the last eight months, WFP has attempted to smooth out WFP purchases by buying weekly and thereby contributing to a more orderly market. Nevertheless, the WFP minimum purchasing requirement of 50 tons limits the number of farmers that can sell directly. Very few can meet this minimum without developing an association, partnership or other alliance to aggregate production. The WFP has expressed interest in working with producers, traders, donors and donor programs to establish the infrastructure and systems needed to encourage quality production and to establish of warehouses both to improve cleaning, drying, and storing and to enable producers to aggregate grain for storage purposes. This will enable small farmers to participate more directly in large WFP contracts and to use warehouse receipts to facilitate financing new crops.

The challenges to developing public warehousing and a warehouse receipts system in Uganda are great. Ugandan farmers have suffered from so many late payment schemes that they currently demand cash. Convincing them to change and entrust their maize to a public warehouse in exchange for a piece of paper will be a hard sell. Further convincing a producer to improve his total return by accepting a discount of the value of his maize warehouse receipt today and wait for prices to go higher during the next few months before a new harvest will also be a difficult challenge.

Nevertheless, donor programs have responded by trying to improve producer prices and maize quality with technical assistance in a number of areas: drafting public warehousing legislation, development of a commodities exchange, assistance in developing farmer associations, assistance in developing pricing software for bank to establish reference prices, assistance from Rural SPEED to develop a public warehousing pilot project with a farmers association in Kapchorwa, and other programs. The challenges continue to be great. Efforts to establish a commodities exchange have stalled due to the limited number of buyers and transactions for any one commodity. A draft law for public warehousing and a warehouse receipts system has been prepared and considered by the Ugandan Parliament with a first reading.

Establishing public warehouses and a warehouse receipts system would provide Ugandan maize producers with an opportunity to receive higher prices for their maize and a higher total return from their hard labors. These producers do not now understand this. In addition, public warehouses operating close to where the grain is harvested can help solve the grain quality issue plaguing the Ugandan maize industry. Warehouses can clean and dry grain delivered by producers prior to grading and weighing, enabling producers to know the true quality of their grain. If cleaning, drying, and storage services are offered closer to where the maize is harvested, then grain quality will be better preserved. If the warehouse offers both to store and to buy their grain, producers will have options to suit their individual needs.

Warehouses offering to purchase grain daily is the beginning of more accurate local grain pricing information rather than the current “Kampala Off Truck” (KOT) pricing, which must have transport and other handling deductions before a true price is determined. Developing fungible commercial quality maize on a regular basis will take much work with producers and buyers alike—farmers to produce it and buyers to give appropriate value for the quality presented. But then, this is not sufficient. There must be a regular market both to gain current pricing information and to sell the maize—whether the seller is a producer or a banker trying to liquidate the grain collateral of a loan in default. It would be most efficient if the warehouse became the merchandiser offering daily prices. Finally, and perhaps most importantly, the farmer/producers depositing their grain in public warehouses must collaborate in an association, partnership or other entity to pool their grain to meet the minimum deposit of five to ten tons. Both warehouses and bankers alike need sufficiently large size deposits to warrant the administrative costs for storage or for analyzing and assessing a loan collateralized by warehouse receipts of maize.

Achieving this public warehousing and warehouse receipts system will require much effort to offer high quality grain handling and storage capabilities, investment in plant and equipment at suitable locations, and achieving a level of honesty, integrity and fair dealing that does not exist in Uganda today. Only the WFP is interested in developing quality production for its humanitarian purchases as the remainder of the buying public accepts what currently exists. But for the WFP purchases, traders to buy Ugandan maize do not exist for sufficient

consistent quantities to justify their investment in public warehouse infrastructure and a warehouse receipts system to facilitate quality production and marketing.

The WFP purchasing alone is not sufficient to warrant such investment, as the WFP purchases could very easily cease in the region and move to other world danger spots. This does not appear so now, but the temporal nature of the humanitarian food supply business by itself is a risky market for warranting such infrastructure and system development. Traders are making good margins now with the inefficient aggregation system, which margins are only likely to decline in the short run should they invest in public warehousing infrastructure. Therefore, it behooves the WFP to work with the international donor community and the Ugandan maize industry to use its humanitarian buying program to the extent possible to facilitate maize commercialization, including public warehousing infrastructure development and a warehouse receipts system. A more commercial system will enable the WFP to obtain the maize that it wants when it wants it. In this way, the Ugandan maize industry will serve the WFP better today and will be in a better position to survive on a sustainable commercial basis tomorrow should the WFP purchases disappear.

A Public Warehouse Round Table of the issues surrounding the development of public warehouses and use of warehouse receipts to facilitate financing occurred on February 10, 2006 at the Grand Imperial Hotel in Kampala sponsored by USAID Rural SPEED. A transcript of the Minutes of the Round Table is included in this report as Appendix II. This report reviews the most significant challenges facing the establishment of operational commercial public warehouses for maize and the ability to use warehouse receipts to facilitate improving maize quality, producer prices, and the financing of the maize industry. This discussion is followed by a few recommendations that may improve the potential for success in establishing public warehouses in Uganda.

1. Developing Commercial Warehouse Receipts System

1.1 Public Confidence in Warehousing Services and Receipts

Public warehouse owners and managers must develop confidence in the public—particularly and especially—producers and bankers. The public must have trust that commodities stored in the warehouse are safe and secure and that upon withdrawal, the holder of the warehouse receipt will receive commodities of the same quantity and quality. Everything about the warehouse operation must exude safety and security. This encourages farmers, traders, the food industry, and bankers to entrust storage of commodities in the warehouse.

Upon entering the warehouse with a deposit, the producer must have his maize professionally tested for quality and accurately weighed. The producer must have faith in the quality of the testing quality and laboratory staff as well as in the accuracy of the scales for weighing. Prior to grading and weighing, the producer may need to have his grain cleaned and dried to improve the grading. The warehouse receipt issued must correctly record the tested quality and the scale weight of the producer's deposited maize. The receipt must be special paper as difficult to forge or counterfeit as the nation's currency.¹ The holder of the receipt must take special care that the receipt is not lost or destroyed. While duplicate receipts can be issued in the case of lost or destroyed receipts, the holder usually must post a bond to cover the value of the commodity deposit for a period of time.

Each of these steps and events must occur correctly to ensure that all depositors are convinced of the veracity of the testing and grading, the authenticity of the receipt, and the certainty that a warehouse withdrawal request will be honored with precisely what is recorded on the receipt. If the warehouse does these things, then eventually producers will trust the warehouse by depositing commodities for storage and banker will trust the receipt as a document of title to the goods. Building this trust in an industry of nearly complete mistrust will be hard and take a strong commitment to honesty and integrity.

1.2 Pricing Information

Producers, traders, bankers, and insurers alike all need current maize pricing information. Producers need this information to decide whether to sell now or wait a few months after harvest for a better price, taking carrying costs into consideration. Traders need pricing information to observe trading margins carefully and constantly between buying, selling, and logistical costs—transport, cleaning, drying, storing, etc. Bankers need to price any commodity that they are holding as collateral for a loan. Should the price fall below the collateral value, then the banker must decide whether to hope the price will rise again, demand more collateral from a borrower, or call or accelerate the maturity of the loan and liquidate the underlying commodity if the borrower does not meet the repayment demand.

With a thin Ugandan maize market with few buyers, the lack of a commodities exchange, and limited public announcements of pricing of maize sales contracts, the Uganda maize industry has limited pricing information. The latest Kampala off Truck (KOT) price does not mean a

¹Electronic warehouse receipts may also be considered. The advantages of electronic receipts over their paper counterparts include: reduction in manual-paper handling; transporting paper documents is eliminated; information is moved faster; multiple keypunching of data is reduced; an audit trail of receipt activity is kept, and the electronic receipt system serves to back-up receipt data for the warehouse. Due to multiple databases holding a record of all electronic receipts, the holder can never lose or otherwise see his receipt destroyed.

seller will be able to achieve this price daily and of course, the KOT price does not identify the quality of the maize sold. To meet the needs of the various interested parties, the best alternative is to develop a simulation of reference prices based on historical pricing information, the closest regional trading markets offering prices for comparable maize qualities and quantities, and recent trends and demands from traders and buyers. Reference prices do not mean the price of actual sales for a particular day but are reasonable estimates of prices if such sales occurred. In addition, should the two largest buyers—the WFP and Kenyan importers not be buying, there may be no takers for the grain except at very low prices. Daily prices are not likely to be achieved in this thin market unless there are public warehouses offering daily to purchase maize at a minimum quality and quantity. If such merchandizing does occur, warehouse offered prices should be widely publicized.

1.3 Liquidity of Commodities

Pricing and liquidity of commodities go hand in hand. Producers and bankers need not only pricing information for what may be the price but also willing buyers actually to purchase their commodities under receipt at a moment either decides to sell. To be sure, each will be selling for different reasons—bankers to liquidate collateral of a loan in default and producers to lock in the sale of their harvest minus debt and carrying costs. The markets for sale may also be different. Producers will sell to village and other traders and bankers to Kampala trading companies.

What is needed is a liquid market enabling producers and bankers alike to liquidate stocks as needed. Should public warehouses become established, they may become merchandisers of grain offering daily prices. This will be a service to producers and bankers alike, each of whom may have maize stored in the warehouse. Until this occurs, bankers may also develop a maize liquidity capability by establishing a virtual mini-exchange via the Internet by willing bankers, traders, and buyers. The mini-exchange could easily adopt rules of an exchange by the willing industry participants adjusted to meet the limited needs of liquidating collateral of loans under default. Commodities could be offered with a given time for trading and a final period when the bidding would be closed. This approach would not likely achieve wholesale pricing but would probably be better than “fire sale” prices.

1.4 Farmer Aggregation

Farmers will need to pool their produce to achieve higher than cash prices from village traders at harvest time. This must occur for at least two reasons:

- i. **Warehousing costs.** Public warehouses incur administrative costs in administering every deposit of maize under their charge. In order to keep the deposit, grading and weighing, and storing costs low, warehouses need to require a minimum deposit size.
- ii. **Bank administrative costs.** Banks also incur administrative costs in analyzing and evaluating the creditworthiness of every borrower. The costs are generally the same for large loans as for small. For loans collateralized by warehouse receipts, Ugandan banks have administrative procedures and paperwork that must be fulfilled for each receipt regardless of quantity and value.

In order to meet these competing requirements for larger size, producers will have to establish associations, partnerships, limited liability companies or other forms of organization

to enable a group of producers to own collectively a larger amount of maize both for depositing in a public warehouse as well as for discounting with a bank. The discounted loan can enable the producers to continue planting the next crop as well as to fund their living expenses. Due to the poor past performance of agricultural cooperatives and associations in Uganda, Ugandan farmers will be reluctant to trust an association. Much work will have to occur in educating farmers about the value of storing their grain to wait for a higher price.

1.5 Bank Financing Issues

In addition to needing current pricing information and the ability to liquidate any commodities, bankers need to be secure they will be in first priority entitled to all of the proceeds to satisfy the debt in the event of a default. Under current Ugandan law, a bank must be the general creditor or primary banker of each customer to make certain that the bank has priority on the customer's entire loan collateral in the event of default. Ugandan banks will not be able to make loans based on negotiable warehouse receipts alone unless the laws are changed to allow creditors priority in loans against negotiable instruments, such as warehouse receipts, in the possession of the creditors. Alternatively, the law must permit a purchase money security interest, granting security in the collateral financed by the loan.

Should these legislative changes occur, then the bank can make a more streamlined loan analysis focused on the loan collateral alone and the credit risk of the borrower's plan for the proceeds. This will enable the bank to consider a loan application in a much shorter time period than currently is the case. Farmers and traders alike have time windows in which they need financing or their planting or trading opportunity expires. Banks have been insensitive to these financing needs and have taken their time to process a loan application. This is primarily a reflection of Ugandan creditor rights laws and regulations and the business climate.

2. Recommendations

2.1 Producer Training on Value of Public Warehousing and Use of Warehouse Receipts

In view of the reluctance of Ugandan maize farmers to accept anything but cash at harvest, the producers need education and training to understand the benefits of depositing their maize in warehouses, accepting a warehouse receipt, and waiting for a higher price. A series of training and education interventions are recommended.

i. Tour of Operational Warehouse Facilities.

When the Rural SPEED pilot project in Kapchorwa is fully operational, tours of the operational warehouse facility should be conducted for groups of maize farmers.

Tours of the facilities would be very effective to allow farmers to see how the commodity storage process work, how the grain is tested, graded, and weighed, and how grain must be cleaned and dried as required prior to graded and testing. This will enable farmers to understand how the true quality of their grain is determined.

ii. Basics on Use of Warehouse Receipts—Costs and Revenues

Farmers are likely to continue in the near term to sell their grain at harvest for cash rather than deposit their maize in a warehouse to wait for a higher price. In order for them to consider storing their grain, producers must be fully informed of the basic fundamentals of storing their grain and waiting for a higher price, including a complete understanding of all carrying costs (warehouse storage fees and interest costs).² They will need to see the typical price fluctuations that would permit obtaining a higher total return from storing their maize and waiting for a higher price. They need to see a simulation that illustrates all of the administrative, handling, and interest costs, the potential higher price obtained, and the net return over taking the village trader price at harvest.

iii. Producer Training on Farm Budgeting and Records

Most Ugandan producers do not develop elaborate annual budgets or keep accurate records of their annual operations to know precisely their yields, costs, revenues, and net income. This information alone would improve their own planting and cropping decisions. In addition, basic farm budget and record keeping training could enable the producers, either individually or collectively within a business entity, to have the minimum information that a bank will require before it will extend a loan to the producers or their organization. Some day, Ugandan bankers may extend credit collateralized only by warehouse receipts of commodities. In the near term, they will demand basic financial information about a farmer's operation, annual revenues, and net income. Any such training should be reviewed with Ugandan bankers to ensure that the minimum information that they would require is included in the farm budget training.

² Some suggest that collateral management fees must be included in this cost calculation. However, these fees must be paid by the owners of the warehouse and absorbed as a cost of running the warehouse. If these fees were required to be passed onto the producers, then the producer returns from using the warehouse would likely be negative in all cases discouraging warehouse use.

iv. Training on Developing Business Entities

Ugandan maize farmers need to learn to organize themselves into associations, partnership, or other business entities to enable small producers to combine and meet the minimum deposit requirements in warehouses and to meet the minimum requirements for consideration of bank loans against warehouse receipts. Producers need education in the benefits from such corporate entities, issues regarding appropriate governance controls, and information on how to establish such organizations expeditiously. Technical assistance providers must spend substantial time with groups of farmers following the initial training to help guide them through the association or other organization development process.

2.2. Bank Officer Training on Best Banking Practices - Lending Against Warehouse Receipts

Ugandan bankers have been treating loans against warehouse receipts as inventory financing loans and conducting the same due diligence as such loans normally require. These bank procedures are followed, among other things, to comply with current creditor priorities against a borrower's collateral in default. They also comply with bank credit policies that have served the banks well for a number of decades operating in a very tough economic environment.

The bank is unlikely to change these policies overnight even should appropriate legislation give bankers more certainty, safety, and flexibility in extending credit collateralized by warehouse receipts of maize or other agricultural commodities. What may accelerate changing their approach to financing farmers, traders, or other industry players against warehouse receipts is specialized training from a team of international and domestic bankers or public warehousing experts having strong expertise in financing warehouse receipts. These experts must be fully versed in the best international practices of managing the loan collateral, including without limitation:

- Administering the loan application through loan committee;
- Taking a security interest in the commodities through possession of the warehouse receipts;
- Managing the pricing or marking to market the commodity collateral on a daily basis;
- Appropriate documentation for maintaining the necessary information for an efficient warehouse receipt financing program;
- Using reference prices to simulate collateral value during the loan cycle;
- Calling for additional collateral to meet declines in commodity pricing; and
- Liquidating the collateral if the borrower does not meet the margin call or demand for accelerating the loan repayment.

This is a specialized area of banking and requires expertise not only in fully competitive markets, such as the US, where all laws and commercial course of action follow high standards. Also, expertise is needed on how to manage financing with warehouse receipts in difficult markets where government and corporate ethics are challenged, markets are thin, pricing is erratic, and transportation is not always timely.

2.3 Suggested Public Warehousing Legislation Improvements

The current Warehouse Receipts System Bill has many standard provisions that provide the basic fundamentals for workable commercial public warehousing and a warehouse receipts system functioning in Uganda. But it is insufficient. This bill must be made complementary with other Ugandan statutes if the access to financing is made more freely available using warehouse receipts as collateral.

A thorough review of the Uganda pledge law and the system for obtaining and perfecting a security interest in warehouse receipts is necessary. Currently in Uganda, a general creditor of a borrower has a priority security interest in any collateral owned by that borrower, even warehouse receipts. This could be amended by two approaches: a purchase money security interest or security interest of negotiable instruments by possession. For example, most countries have a purchase money security interest provision or the equivalent, whereby a banker that finances the purchase of identified commodities or goods has a security interest in those goods above all others (assuming of course that all other procedural issues for perfecting a security interest in property are followed). Security in negotiable instruments is another matter. Many countries hold that a creditor who advances funds to a borrower secured by negotiable instruments (e.g., shares, bonds, warehouse receipts, and the like) that are placed in the possession of the creditor (i.e., held in the bank vault) has a security interest in those negotiable instruments above all others.

Amendments to the bill that make adjustments, such as these, of course, have wider implications beyond public warehousing and may generate many discussions delaying passage of the warehouse receipts law. However, if these amendments or their equivalent are not enacted to change the current Ugandan pledge law, bankers will have no choice but to follow current practices.

2.4 Public/Private/Donor Partnership Collaboration on Developing Warehouse Receipts System

i. Collaboration with World Food Program on Developing an Orderly Market

The WFP is clearly the most significant buyer of maize in the Ugandan market. And though the WFP is following its procurement policies and procedures for purchasing humanitarian food aid in the regional market where it is serving internally displaced people, those purchases have historically caused periodic spiking in local maize prices. The WFP is committed to trying to improve the local maize market to enable WFP to purchase more humanitarian maize needs locally and through producers whenever possible. The WFP has shown its willingness to work with traders, bankers, and producers in developing a more orderly procurement schedule within the confines of its current procurement policies and procedures. For the past eight months, the WFP has been buying maize weekly to provide a more orderly market throughout the year. More is needed.

Several donors from several countries are working on various aspects of the maize industry to develop more commercialization. They will probably be willing to help with systems, training, and infrastructure needs if they are convinced that the result will be a higher level of commercialization. The WFP, other international donors, bankers, businesses, and producer groups need to collaborate on ways in which all can adjust their mode of operations for the greater good of developing a commercialized maize industry. This is critically important to

Ugandan farmers and businesses that must be able to continue commercial activity after the day the WFP moves out of the region and onto more exigent disaster areas of the world requiring their humanitarian support.

All donors providing technical assistance support to greater commercialization of the maize industry should meet with the WFP from time to time to coordinate purchasing with technical assistance. Specifically, the donors and WFP should collaborate on the following:

- Support pilot projects such as the Kapchorwa warehousing activity to encourage producers to deposit maize in the warehouse and then facilitate purchases through the warehouse. If Kapchorwa is successful, then select another appropriate locale for an additional pilot.
- Each donor can provide technical assistance support for various aspects that facilitate make the commercial activity viable. These include without limitation:
 - Training of targeted producers for using the facility;
 - Training producers to develop business entities to pool maize to deposit with the warehouse and receive financing back by warehouse receipts;
 - Training of producers prior to their visit to banks to ensure that they have the minimum information that banks will require prior to extending credit;
 - Subsidizing collateral management services to preserve the integrity and confidence in the warehouse;
 - Training of warehouse owners in warehouse management, particularly with respect to honest and fair dealing to work toward warehouse operations without collateral management services;
 - Training of banking staff to work with financing against warehouse receipts for short term loans;
 - Providing equipment to the warehouse or facilities improvements as needed to clean and dry grain, test and grade the grain properly, and minimize insect and pest, moisture, and other damage;
 - Providing transport support to help producers in the target area to bring their grain to the warehouse;
 - Providing monitoring oversight of the warehouse to ensure that warehouse services are properly provided, that all costs and services are clearly posted, and that all producers receive equal treatment;
 - Assessing the impact of maize production and commercialization on the producers' families and provide counseling and assistance as needed to support improved family household management;
- Develop appropriate maize contract terms that meet the WFP needs for quantity and quality of maize but are also attractive to producers to encourage them to use warehouses;
 - Try to develop a WFP contract with the warehouse to try to fulfill the contract by offering daily prices widely published to fill the contract
 - The WFP can establish their minimum price and have a right of first refusal for deposited grain should the price rise;
 - The warehouse will enforce the WFP right of first refusal;
 - The warehouse can clear all deposits with the WFP on a rolling basis, deliver at the WFP order, and eventually fulfill the entire contract
 - The warehouse performance could be supported or partially guaranteed by donor supported projects facilitating the warehouse operation and producer training.

- Use the information learned from one or more pilot projects to review the Warehouse Receipts Bill, 2005, for improvements in provisions for facilitating commercial warehouses in Uganda;

Donors do not usually collaborate so much on one particular aspect of commercial development but here it could have a positive effect. There are so many aspects of trying to commercialize the maize industry in Uganda that one organization will have difficulty succeeding alone. Having significant donors all involved in facilitating maize commercialization would promote understanding of the dynamic impacts that this project and the numerous pilots will have on the producers, their families, and the rural economy. There are many political and commercial forces that are not interested in facilitating a commercial warehouse system, as it may have negative effects on their business or constituencies. By having multiple donor support, they can be many more voices able to advise the Parliament on the need for, value of, and content of a warehouse receipts bill to ensure smoother passage through the legislature.

ii. Collaborative Efforts on Public Warehousing Legislation

The Warehouse Receipts System Bill, 2005, went through the first reading of Parliament last year but has not yet been enacted. For the reasons stated, public warehouses will need this legislation as a comprehensive legal framework to set clear rules for all public warehouse activities that are currently undertaken through contracts. Bankers, traders, producers, and warehouses alike have much to gain through the legislation's passage, though they may not see all benefits clearly now. Donors assisting development of a warehouse receipts system should want to facilitate support of this legislation. All interested parties must work together to help Parliament understand this strong need for this legislation and why Parliament should make it a top priority.

iii. Collaborative Technical Assistance Support on Public Warehousing Issues

Several donors have multiple programs that are designed to move the commercialization of the Ugandan maize industry forward. Collaboration is needed to make sure that all work toward the goal of a commercial maize industry, public warehousing, and a warehouse receipts system. Work is needed on business oriented farmer associations focused on holding and merchandising grain through public warehousing. This is a long and tedious process. Others can bring in the expertise to model and simulate usage of warehouse receipts in the Ugandan market. Rural SPEED for example can conduct tours of its Kapchorwa project to demonstrate to all producers how it works and operates. Farmers can meet with the association and its members that are depositing their grain in the warehouse and learn how they established their association and the benefits that the association provides. Educating farmers to use a commercial warehouse receipts system, developing associations to do so, and seeing the training bring about greater public warehousing use may be the most difficult challenges of commercializing the maize industry.

Joint collaboration on bank training is very important. Bank officers only have so much time that they can devote to training. Bank managers want their officers at their desks analyzing and developing loan packages. Donors planning to offer bank training programs on specific issues should coordinate these programs with others even if other bank training programs are entirely different subject matter. There may be efficiencies to combining the programs and bank management may be very appreciative that this is done.

3. Conclusions

Developing commercial public warehousing and a warehouse receipts system has many, many challenges any one of which could retard its development. Uganda will know that it has a fully commercial system when producers regularly choose to store their maize rather than sell to the village or other trader for cash at harvest. Many issues are challenges:

- The thin Ugandan maize market with a very few buyers;
- The dominance of WFP as a periodic heavy purchaser;
- Thinly capitalized traders that must obtain contracts in order to gain financing to buy the grain through a myriad of village and regional traders;
- The jaded Ugandan producers who have demand cash at harvest because they have been cheated so many times by traders and associations;
- Bankers that take so long in reviewing loan applications that borrowers do not receive the money soon enough to be useful; and
- The lack of suitable grain storage in most areas of the country outside of Kampala.

All of these characteristics are challenges to developing a commercial public warehousing system. If the Ugandan maize industry—bankers, traders, and producers—the WRP, the various donors work together to solve the many challenges, a commercial system is possible and would provide the maize industry with a long term future.

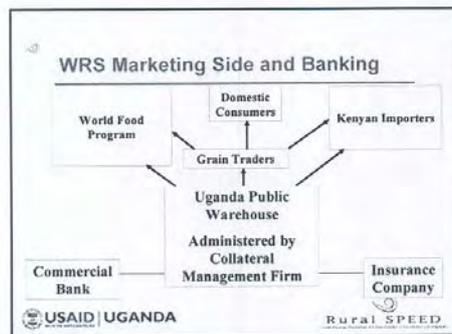
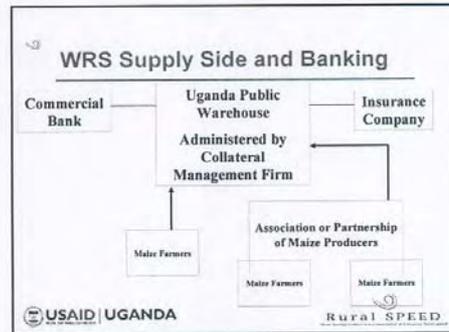
Appendix I. Round Table PowerPoint Presentation

Warehouse Receipts



Ken Peoples, Prime International Inc.

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Supply Side Issues

- Integrity of the warehouse and its receipts
 - Weighing and grading (pre-cleaned & dried)
 - Authenticity of the receipt
 - Collateral Management maintaining quality
 - Risk of loss (fire, theft, fraud, casualty)
- Farmer aggregation
- Location of warehousing
- Warehouse Association—Self-Policing

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Marketing Side Issues

- Pricing
- Quality and quality maintenance

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Bank Issues

- Liquidity of Commodities
- Minimum contract volume per party
- Warehousing Law: Creditor rights priority
- Pricing information

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Appendix II. Minutes of Roundtable Discussion

The following are the recorded minutes of the Rural SPEED Round Table on Warehouse Receipts held at the Grand Imperial Hotel between 9 am and 1 pm on February 10, 2006. The minutes are recorded in summary fashion with identification of the speaker and the main points presented.

Ken Peoples:

1. WRS must have congruence with how things work in a particular country.
2. Present the critical areas and generate discussion around impediments.
3. My presentation is operational versus legal framework.
4. a public warehouse is a bank.
 - a. Need to examine commodity at deposit
 - b. Doing that honestly and properly
5. In Uganda collateral management is handled largely by international firms
 - a. Guarantee the commodities are what is receipted
6. Must have a relationship with a bank to ensure the commodity is turned into cash
7. There are different types of depositors (groups of farmers and individual *large* farmers). Both are necessary to get adequate volumes.
8. After deposit is made to warehouse; a receipt is given where it can be held for temporal arbitrage, discount it with a bank or sell it to a trader.
9. Uganda's two harvests shortens opportunities for temporal arbitrage
10. Insurance (through bonding) is necessary for public warehouses to insure quality and weight.
 - a. Insurance is rarely full coverage
11. Receipts are held by depositors until sold to the market. In Uganda there are basically three buyers either directly or through buyers:
 - a. WFP
 - b. Kenya
 - c. Consumers
12. Supply Side Issues:
 - a. Integrity of the warehouse system relies on complete confidence by:
 - i. The depositor
 - ii. The Bank
 - b. Receipts must be authentic
 - c. Warehouses must be commercially viable
 - d. Farmer aggregation
 - i. 5 MT minimum deposit is necessary
 - e. Location of warehousing is inefficient because it requires huge amounts of handling to bring grain to Kampala. Localizing warehouses closer to production is necessary.
 - f. Warehousing associations that police themselves are more effective because they maintain industry standards and keep ineffective/efficient regulators out.
 - i. Maintain collective reserves to preserve integrity to the system.
 - ii. This develops confidence of banks and depositors
13. Market Side Issues:
 - a. Pricing (a good market prices is necessary on at least a daily, or weekly basis)
 - b. Initial quality and maintaining quality

14. Bank Issues:

- a. Liquidity of commodities.
 - i. If a customer defaults, the commodity must be capable of being sold.
 - ii. Otherwise, it fails to be collateral for a loan.
- b. Minimum contract size must be in place to lower bank transaction costs
- c. Warehouse law
 - i. Helpful but not necessary
 - 1. contracts are a good substitute
 - ii. Creditor rights priority (if the depositor uses grain as a collateral the bank needs first right to that collateral)
- d. Pricing information
 - i. Bank needs to know price daily to know exactly what the collateral is worth in order to minimize their risk.

John Engle/USAID SCOPE:

- 1. I am skeptical about WRS in Uganda
 - a. Folks are too disorganized.
 - b. Volumes are too low.

Ken Peoples:

- 1. What is the alternative? It must be tried.
- 2. Kapchorwa farmers have good yields, two markets and farmers are to be paid premiums for quality.
- 3. It will be important to see what happens in Kapchorwa
- 4. I've seen it work under worse circumstances.

Dorothy Kanyomozi/WFP:

- 1. Farmers need training to understand their benefit from WRS
- 2. Farmers may not honor large contracts as prices move

Ken Peoples:

- 1. If Kapchorwa works well; it should be used as a facility for farmer education.
- 2. Floor prices are relevant with right of first refusal are ways to avoid side selling.

Chris Kaijuka/UGTL

- 1. I didn't see in the structure you gave where processors play a role.

Ken Peoples:

- 1. The chart I presented was simplified.
 - a. Processing is definitely a piece of this picture.
 - b. Transporting is also a piece of this picture.

Amos Tumwesigye, Audit Control Expertise (ACE)

- 1. This concept is well understood by the parties involved except by depositors.
- 2. Practical training is necessary.

- a. Other sectors must be well understood.

Ken Peoples:

1. Producers must be trained.
2. Producers must understand their costs.
3. We need to learn from how public warehouses function in other places and through history.
4. In most cases, law follows commercial activity.

Bombo Agricultural Enterprises

1. Some traders will buy any quality how will you convince a farmer to clean and dry grain.

Ken Peoples:

1. Premium pricing. Steps must be taken to get a better price.

John Magnay/UGTL:

2. In Uganda:
 - a. Coffee
 - i. Raw product
 - ii. Single end buyer
 - b. Cotton
 - i. Raw product
 - ii. Single end buyer
 - c. Maize
 - i. Need a reference price
3. There are reasons why WRS work:
 - a. Zambia
 - i. One crop per year
 - ii. Major local maize consumers
 - b. Uganda is fundamentally different
 - i. two crops
 - ii. small holder producers
 - iii. low local consumption (1/3 of grain is excess of demand)
 1. regional deficits are out of sync with Uganda production (this is impetus for temporal arbitrage and WRS)
 - iv. Regional standards are ignored by regional trade partners.
 - v. Reference price information does not consider quality.
4. WFP distorts the market terribly.
 - a. They should disengage.
5. Donors are distorting pricing

Ken Peoples:

1. WFP is establishing quality standards
2. It is beginning development of a system
3. Pricing is certainly distorted

4. WFP should work with the industry
5. Kapchorwa will not prove this; but producers will learn to be paid for quality
6. The grain is not eaten in Kampala either

Chris Kijuka/UGTL:

1. In order for Uganda to kick off a WRS you need large traders
 - a. Volumes
 - b. Requires risk takers
 - c. You need quality control

Ken Peoples:

1. My analysis does not exclude traders.
 - a. Traders will learn faster; this is understood
 - b. However, traders are not enough to give you volume throughput.

Patrick Oyee/USAID/APEP:

1. The issue is to train the farmers, we have trained farmers to produce quality since 1996 in coffee, maize and cotton.

Dick Maxon/ACDI/VOCA:

1. How do you address title?
2. Where do you make your margins?

Ken Peoples:

1. Kapchorwa is a cosigned receipt (Kacofa and farmer)
 - a. Everyone must be protected.

Bernie Runnabaum/ACDI/VOCA

1. If we are to try WRS it should target farmers and go slow.
2. A lot will be learned in Kapchorwa

Taibu/USAID/SCOPE:

1. Farmers must be made to understand that WRS is not a *guarantee* of a premium
2. If there is no appreciation of price, farmers may get discouraged on the ongoing costs.

Ron Kopicki/World Bank

1. WRS must be a private, sustainable businesses. They need a *raison d'etre*.
2. Cereal Banks (funded by Rockefeller) have discovered the underlying premise for adding value. These are a first step leading to the next step of public warehouses.
3. The process should be considered a system of stepping stones and intermediate steps must be followed

Chris Baine/NRI

1. Farmers must perceive farming as a business operation
 - a. In Bushenyi with coffee we have looked at the plight of the farmers
 - b. Farmers bring coffee to traders who adjudicate the quality and quantity which disadvantages farmers as they don't know the inherent qualities of their coffee.
2. WRS has been used alone for traders using non-negotiable receipts.
3. Farmers continue to be fragmented and need good market information.
4. The receipt provides this information.
5. Without warehouse receipts backed by cash from banks farmers are forced to sell to traders.
6. Banks don't want to work with farmers unless there is an off take contract.
7. How will the banks come in to fill this gap?
8. Why do farmers need WRS if the Kapchorwa farmers have a contract.
9. We need a commodity exchange to develop further off takers.
10. Why doesn't WFP buy from a commodity exchange.

Dorothy Kanyomozi/WFP:

1. WFP uses WRS because procurement procedures require high minimum quantity and delays payments.
2. 10% of all WFP procurement comes through farmers.

Mr. Augustine/UNAFA:

1. Don't underestimate the capacity of farmers
 - a. Farmers are trainable
 - b. Farmers need to be organized better
 - c. We have trained and organized farmers to practice temporal arbitrage in Masindi.

Uganda Commodity Exchange:

1. Warehouse receipt legislation
 - a. You say that this can work without legislation.
 - i. Stakeholders are not interested to move forward without law
 - ii. This will give financial institutions confidence
2. We have been working on the system for a long time
 - a. Collateral managers have high costs.
 - i. questions sustainability
3. We don't have a commodity exchange but Rome wasn't built in a day.
 - a. WRS will guarantee quality
 - b. All traders **must** add value but with WRS ensures many of those costs will have been already handled and the producers get the value added.
 - c. Once commodities are warehoused they can be traded.

Jackie Wakhweya/USAID:

1. Integrity remains a problem
 - a. If receipts are not tradable or transferable; what is the point in pushing forth with legislation and other regulation?

Ken Peoples:

1. A statute is not a bad idea but should be based on real world experience.
2. The statute should follow the market; not the market to follow the statute.
3. Parliaments take a terrible amount of time to pass legislation.

MP/Committee for Trade and Industry:

1. The draft legislation is in final phases of approval.
2. When this issue first came up;
 - a. We asked that training of farmers be done;
 - b. We doubt training has been done.

John Magnay/UGTL:

1. What is Stanbic waiting for; why don't you finance warehouse receipts

Mr. Kagaba/Stanbic Bank:

1. When a bank is in a position to lend, they are lending depositors' money and are therefore highly regulated and must observe standards.
 - a. We must evaluate the risk of losing money that doesn't belong to us.
 - b. Discounting a receipt 20% means that the bank is taking 80% of the risk.
 - c. We have the right to carefully evaluate the risk.
 - d. Uganda's market has been using WRS on the basis of contracts for 10 years. Contracts are inter-party (not with third parties).
 - i. There are many other parties to the transaction that must be understood.
 - ii. Legislation must incorporate the interests of third parties and define rights and responsibilities.
 - iii. With the ability to bring a case to the legal system, banks will lend.
 - e. The current legislation does not address creditor priority.
 - i. If you lend for a specific purpose you should be able to attach collateral of the borrower ahead of other creditors.

Dorothy Kanyomozi/WFP:

1. How do you handle devaluation of the underlying receipted commodity?

Mr. Kagaba/Stanbic Bank:

1. You can ask for a floor price by an offtaker.
2. You can study price trends
3. You can demand other securities if prices slide.

Chris Baine/NRI:

1. Sometimes assessment criteria are too stringent for farmers.
 - a. Audited accounts, etc. are too stringent as requirements
2. Farmers should not be treated as long term borrowers when the transaction is fast and fully collateralized.
3. Two to three months to structure a deal is too long for making a WR deal.
4. It is possible to check farmers' groups registration status with MTTI.

Amos Tumwesigye / ACE

1. The product must benefit farmers.
2. Structured trade finance is meant in the fundamental to rely on collateral rather than seeking securities that are not there.

Ken Peoples:

1. Financing based on contracts will not go away with legislation
 - a. Contracts tell us that the commodity is bought, sold and liquidated.

Mr. Kagaba/Stanbic Bank:

1. Contract covers only price risk.

Patrick Oyee/USAID/APEP

1. How does this fit into a CERUDEB model?

Dorothy Kanyamozi/WFP

1. We want to start in Lira but we should discussed more broadly first.
2. WFP can be a final buyer.
3. We address price stability
4. WRS will assist farmers to achieve farmer storage
5. Ensuring quality (East African Trade Standards)
 - a. Farmers must be trained.
6. WFP contracts are clear
7. WFP ensures a market and can assist in transporting.
8. WFP limits middlemen and improve prices.
9. Build economic volumes of crops.
10. Improve income of rural poor.

Mr. Kagaba/Stanbic Bank:

1. Size matters (traders versus farmers).
 - a. We have lent to traders to achieve economies of scale.
 - b. We have lent to traders because they are sophisticated.
2. We don't generally lend to farmers' groups because of administrative costs.
 - a. MFIs can do this.

3. We are interested in farmers' groups when they get the higher volumes.

Ken Peoples:

1. Is there space for collaboration between commercial banks and MFIs to reach smaller producers to go to a warehouse? It works elsewhere.

Mr. Kagaba/Stanbic Bank:

1. That's a very complicated transaction.

Julius Ssegirinya/CERUDEB:

1. We have not done WR with smaller farmers.
2. We tried to develop a system for smaller farmers with ACDI/VOCA in Iganga
 - a. This did not really take off.
 - b. We do believe that it is feasible.
 - c. Food net informed farmers of price movement.
2. The biggest shortcoming is the collateral management costs.

Chris Baine/NRI:

1. Stanbic is all over rural Uganda and their clients are farmers.
2. Stanbic can do this by working directly with rural warehouses.
3. There are DCA guarantees:
 - a. Why not use this.

Asaph Besigye/USAID/Rural SPEED:

1. WRS can help us take the trash grain out of the market.
 - a. In the 70s Ugandans thought education was useless, but that changed.
 - b. This too can change.
2. If price drops it creates too much risk.
 - a. WRS could be bolstered with price insurance.
 Price forecasting mechanisms can also help.

Appendix III. List of Individuals met during Consultancy

1. Christian Baine
Director
DCDM Consulting (Uganda) Ltd
2. Dr. Ferdinand Bitanhirwe
Agricultural Services Manager
SGS Uganda Limited
3. Jaap Blom
Team Leader
Agribusiness Development Component
Agricultural Sector Programme Support
4. Richard Wangwe
Agricultural Finance Specialist
Agribusiness Development Component
Agricultural Sector Programme Support
5. Ken Noah Davies
Representative Country Director
United Nations World Food Programme
6. Dorothy Kanyomozi
Marketing Support Officer
United Nations World Food Programme
7. Hassan Abdelrazig
Program Officer
United Nations World Food Programme
8. John Engle
Managing Director
Strengthening the Competitiveness of Private Enterprise
9. Christopher Kigenyi, FCIB
Executive Director
Allied Bank International Ltd
10. Terri Kristalsky
Managing Director
USAID Rural SPEED
11. Richard John Pelrine
Rural Finance Advisor
USAID Rural SPEED
12. Asaph Besigye
Rural Finance Specialist
USAID Rural SPEED
13. John Magnay
Chief Executive
Uganda Grain Traders Ltd

14. Kagaba Muhumuza
Structured Finance
Stanbic Bank,
15. Godfrey Mundua
Agricultural Portfolio Manager
Standard Chartered Bank
16. Joseph Nkandu
Executive Director
NUCAFE
17. Herment A. Mrema
Senior Business Manager
NUCAFE
18. Patrick Oyee
Agribusiness Finance Specialist
Agricultural Productivity Enhancement Program
19. B.F. (Bernie) Runnebaum
Program Manager
ACDI/VOCA
20. Sandra Blanchard
Grants & Development Manager
ACDI/VOCA
21. Julius M. Segirinya
Principal Credit Officer
Centenary Rural Development Bank
22. Amos T. Tumwesigye
Country Manager
ACE Audit Control & Expertise Limited
23. Stephen Kaye Kawunde
Risk Management Analyst
ACE Audit Control & Expertise Limited