COMMON MARKET FOR EASTERN AND SOUTHERN AFRICA

AAMP Policy Briefing December 2008

Trade in Food Staples: Promoting Price Stability and Food Security through Intra-Regional Trade

- Two upcoming developments in regional trade policy – the COMESA customs union and the COMESA, SADC, and EAC free trade zone – have the potential to promote regional economic integration and trade.
- International markets prices affect cereal markets of Eastern and Southern Africa differently in different countries.
- Cross-border trade within the region can help to smooth price volatility and alleviate domestic food shortages. Variability in climatic conditions and staggered harvesting in the region allow surplus areas to supply food to deficit areas within and between countries.
- Enabling policies and public investments remain necessary for these benefits to occur.

Recent developments in regional economic and trade integration

Enhanced regional economic integration in eastern and southern Africa promises several key benefits to businesses and consumers: relieving the constraints posed by small, segmented national markets; providing a market large enough to attract meaningful investment; economies of scale leading to increased competitiveness, internally and abroad; benefits of risk sharing and regional comparative advantage.

Progress to date includes the following regional trade agreements:

- COMESA Free Trade Area: 2000
- SADC Free Trade Area: 2008
- EAC Customs Union: 2008

A Free Trade Areas (FTA) abolishes duties and quotas among member countries. Currently, the COMESA FTA offers investors access to a market serving over 400 million consumers.

Customs union agreements imply even greater economic integration, including:

- duty-free and quota-free trade amongst the constituent customs territories;
- a common level of protection and common trade policy against imports from outside the Customs Union; and
- a common administrative structure to manage trade policy, customs operations and revenue collection.

Two upcoming developments stand poised to harmonize regional trade systems even further. The **COMESA customs union** agreement is scheduled to take effect in 2009. And COMESA, SADC, and EAC have agreed to create a **free trade zone** including 26 countries, with a GDP of over US$ 600 billion and a population of over 500 million. This expanded FTA aims to enhance intra-regional trade, boost economic growth, and strengthen the bloc's bargaining power in international trade negotiations. Harmonization of the free trade areas and external tariffs, particularly within COMESA and EAC, is the current priority.

Legal Basis for Export and Import Bans under the COMESA Treaty

The COMESA treaty mandates duty and quota free trade among member states. However, Article 50, Section 1, Items c,e and f allow governments to impose trade restrictions under the following special circumstances:

- to protect animal and plant health
- to ensure food security in the event of war or famine
- for items of national importance.

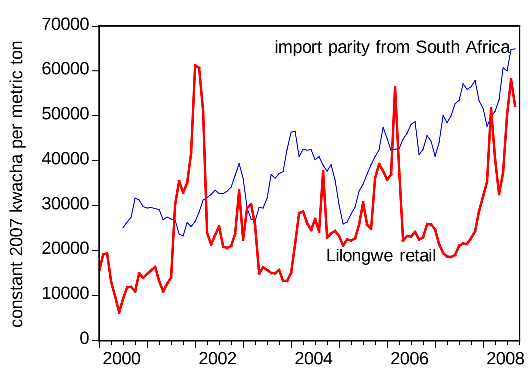
Before imposing trade bans, however, the member government must notify the COMESA Secretary General and prove to Council that these conditions apply.

International markets and intra-regional trade in food staples

World food and fertilizer prices have soared to unprecedented levels during 2008. However, the situation in eastern and southern Africa is more nuanced.

When examined in nominal US dollars maize prices in most of eastern and southern Africa reached all time highs in 2008. Yet when examined in real local currency units the picture is different. In inflation-adjusted terms maize prices in Mozambique and Malawi are at or near historic highs. In Kenya and Zambia there has been an upturn in real maize prices from late 2007 to mid 2008, but this follows a long period of gradual decline in real prices, so even during 2008, real prices were no higher than their mean levels over the past 15 years.

Lilongwe White Maize Price



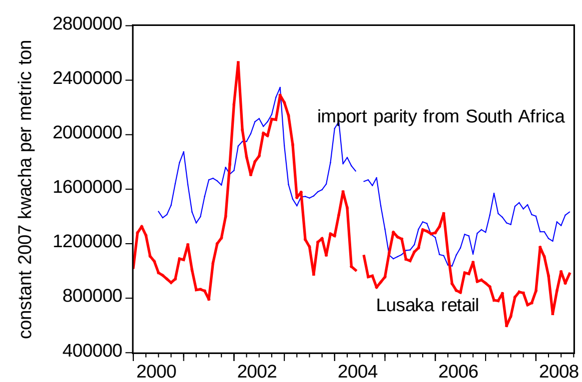
Source: Jayne et al. (2008)

Global price changes have not fully transmitted to domestic markets. Between March 2007 and March 2008, the FAO food price index (FPI) jumped 56%. In the same period, the FPI increased 39% in Ethiopia, 20% in Kenya and 11% in Tanzania. In several other countries including Zambia, Uganda, and Malawi, the increase was less than 10%, suggesting a weak association between global food prices and domestic food prices in some cases.

Countries in eastern and southern Africa have responded in different ways to the situation. Common short run responses have aimed to ensure there are safety nets in place for the most vulnerable and an adequate and affordable food supply for the majority of consumers. Ethiopia has sought to increase fertilizer imports. Kenya and Ethiopia have sought to increase food imports. Tanzania, Malawi, Zambia and Ethiopia have sought to restrict exports. Long run responses will focus on supply and productivity. Unfortunately, some of the short term responses, such as export bans, will hinder long term food security. In small, fragmented markets, trade is crucial for maintaining producer incentives and moderating price volatility.

In early 2009, some indicators suggest potential food shortages emerging in Zambia and Malawi, not because of world food price levels, but because of physical shortages, which are likely to send maize prices higher over the coming months. Because of nervousness in the markets, high marketing board maize floor prices and export bans in much of the region, maize prices are very high in some areas, and substantial spatial price spreads seem to be emerging. Maize prices in Malawi, for example, were bid up very quickly in the 2008 season, and by December 2008 they were roughly \$100 per ton higher than in neighbouring Zambia and Mozambique. Yet trade barriers currently hinder opportunities to moderate these price spikes through regional cross-border trade.

Lusaka White Maize Price



Source: Jayne et al. (2008)

The African Agricultural Markets Programme (AAMP) was launched in 2008 by the COMESA Ministers of Agriculture to enhance regional capacity, policy dialogue, and coordination on agricultural input and output markets through a series of policy seminars, training, and analytical work. The programme currently covers COMESA members and non members: Ethiopia, Kenya, Malawi, Mozambique, Tanzania, Uganda, and Zambia.

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Intra-regional trade can contribute to agricultural growth, food security and price stability

Production of food staples – for growing urban markets and food-deficit rural areas – represents probably the largest growth opportunity available to African farmers. But Africa's arbitrary political boundaries cut across natural market sheds, posing an obstacle to this growth. They separate food surplus northern Mozambique from deficit markets in Malawi and eastern Zambia; food surplus zones in eastern Uganda and northern Tanzania from deficit markets in Kenya, and surplus cassava and maize producing areas of northern Zambia from the deficit mining towns of Katanga and Kasai provinces in the DRC.

Value of Agricultural Production in Sub-Saharan Africa, 2000 ($US billion)

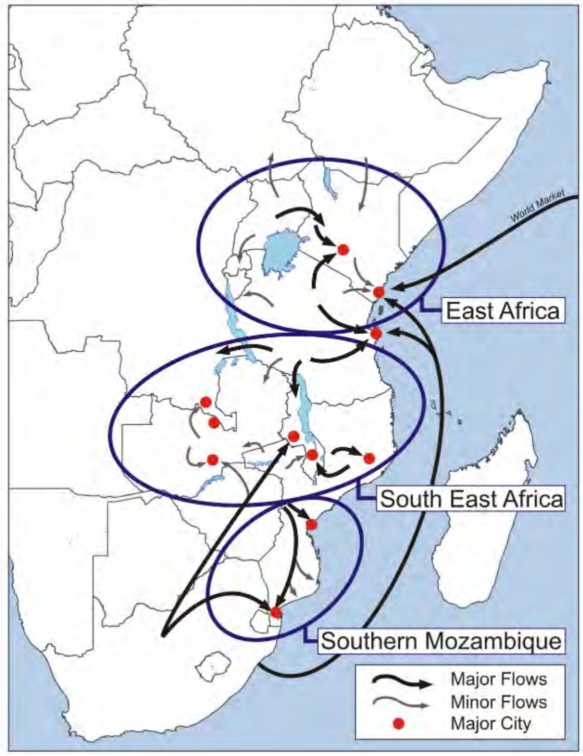
	Value	Percent
Ag. exports	17	25%
Domestic staples	50	72%
Other	2	3%
Total	69	100%

Source: Diao and Hazell (2004)

Because political borders frequently separate surplus food production zones from the deficit markets they would normally serve, open borders become necessary for stimulating the investments needed to accelerate growth of food staple production in the medium run and to moderate production and price volatility in the short run.

For farmers, production surges, when confined within small national markets, can quickly lead to price collapse. In Zambia, for example, a 30% boost in maize production can lead easily to a 50% price fall, if borders remain closed. However, when policy makers allow maize exports, to neighbouring DRC, the export parity price forms a price floor, cutting the price fall roughly in half.

Maize market sheds in eastern and southern Africa



Source: Haggblade et al. 2008

Estimated maize price in Zambia under alternate trade regimes (% change from normal)

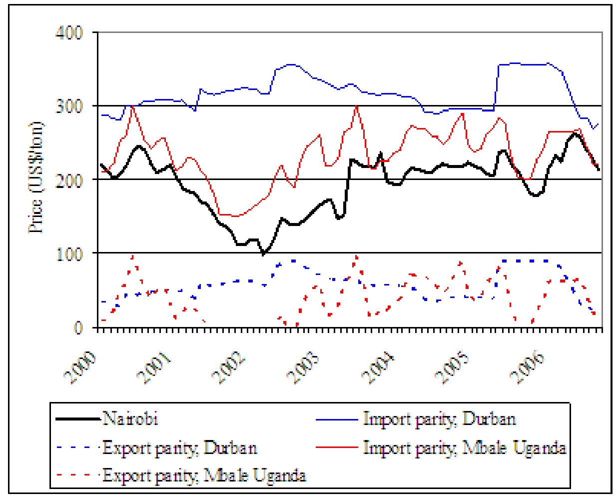
	Closed Border	Open Border
Bumper harvest (30% above normal)	-50%	-26%
Drought (30% below normal)	163%	36%

Source: Haggblade et al. (2008)

For consumers, a fall in domestic production, because of a drought for example, leads to price spikes and a fall in food consumption, particularly among vulnerable groups. Simulations for Zambia suggest that a drought which reduces national maize production by 30% can trigger a price rise in excess of 100%, if the borders are closed. But under open borders, the import parity price caps price increases. In this way, maize exports from Uganda help to moderate maize price levels in Nairobi.

In exceptional cases, domestic prices may rise above import parity, as with Ethiopian wheat in 2008 and with maize prices in Malawi and Zambia in 2002 and 2005. A review of these anomalies reveals that import parity may fail to cap domestic price increases when governments place restrictions on trade, when traders are uncertain about government intentions, when subsidized government sales discourage private imports, or when shortages of foreign exchange prevent private imports. In normal situations, when policy environment favours cross-border trade, import parity prices limit domestic price rises.

Nairobi White Maize Price



Source: Haggblade et al. (2008)

Policy implications for supporting intra-regional trade in food staples

Key policy instruments for encouraging cross-border trade include cessation of quantitative controls, tariff reductions, and harmonization of customs procedures. Major constraints to liberalizing trade include mutual mistrust between governments and private traders and reluctance by governments to give up control over maize pricing.

Export bans. Commodity price controls and export bans may help to contain short term pressures on domestic prices, but they also serve as a disincentive to farmers and exacerbate price instability in regional markets. In the long run, export bans are a significant detriment to food security and agricultural growth.

Transport infrastructure. Improved regional infrastructure can complement trade reforms by lowering transport costs. Public investment in transport corridors can help to link surplus production zones with cross-border deficit markets, thus benefitting farmers in surplus zones and consumers in the deficit markets.

Market information. Accurate and timely information on crop forecasts, price movements, stock levels, and public sector purchases and stock releases underpin the effectiveness of trade to exploit regional diversity. The example of Malawi in 2007/08 shows how inaccurate crop production estimates can exacerbate food insecurity. On the basis of its forecast of a record maize harvest in 2007, the Government contracted to export over 400,000 tons of maize. However, it was only able to source some 300,000 tons and this sent the price to levels seen only in the most severe drought years.

Trust and communication. Ultimately, increased reliance on cross-border trade requires trust. Governments must have confidence that competitive markets will deliver food staples at low cost and in adequate quantity. And traders must trust that governments will not change policies unexpectedly. Experience suggests that increased competition, improved transparency, open communication between governments and traders, predictability in policy making, plus good market information, provide necessary underpinnings of growing regional trade in food staples.

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