TAB K

8. "Deregulation and Privatization of Marketing Boards"

by Ian Marceau

DEREGULATION AND PRIVATIZATION OF MARKETING BOARDS

by

Dr. Ian W. Marceau
Senior Economist,
Hassall and Associates, Pty. Ltd.
Canberra, Australia

Presented at the U.S. AID International
Conference on Privatization,
Washington, D.C.,
February 17-19, 1986

Canberra, A.C.T. 2601
Australia

January 1986

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Introduction

Agricultural marketing boards are used widely by governments in developed and developing countries alike. They implement official marketing and pricing policies. Their aims are usually to maintain domestic food security while nurturing agricultural exports, the largest source of foreign earnings for many nations. To fulfil social contracts, most governments pay at least lip service to the principle that domestic consumers should have access to "adequate" food supplies at "affordable" prices and producers should receive "reasonable" returns.

In trying to meet these often-conflicting conditions, governments use the marketing, pricing and regulatory functions of the marketing boards to intervene in various ways in the factor and product markets. These interventions inevitably reduce economic efficiency by sending distorted price signals to producers and consumers that result in production and consumption patterns that would not exist if free-market-clearing forces were permitted to operate.

It is argued by some that the marketing boards are unwarranted governmental intrusions in the market-place and that they should be abolished forthwith, to be replaced by private interests operating under the "rules" of the free market. The proponents of this form of privatization, divestiture, argue correctly that only under market conditions free of governmental interventions will full economic efficiency be attained.

Others argue that while attaining full economic efficiency is desirable it is not paramount in and of itself and must be sought within the limits of the sociopolitical environments in which economic activity takes place in all countries. This argument is that governments have to fulfil social contracts, address questions of equity and cater specifically to interest groups to retain their power and often, their physical safety. Further, they contend, even in cases where neither political nor physical survival are threatened, the volatile nature of agricultural production, often inadequate distribution and marketing systems, and arbitrary and rapidly changing policies affecting markets in developing countries pose such great risks to entrepreneurs that private interests will not organize effective markets. Therefore, marketing boards are needed to fill the void, to provide orderly marketing and to provide a food production and distribution safety net for the less-privileged in society.

These proponents of governmental involvement in agricultural markets contend that in any event the problems commonly attributed to the Boards' market intrusions are not due to their existence *per se* but rather to the ways in which they are (mis)managed as well as to their use by governments to implement the wrong policies, to reward political friends and to punish enemies. Therefore, this argument goes, given the social, political and perceived security importance to governments of the marketing boards, making their abolition

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highly unlikely, the key policy issue is to find ways to reduce the barriers to private-sector participation in the factor and product markets, parallel to or in competition with the Boards. At the same time, they contend ways need to be sought to apply profit-seeking practices to the Boards' operations.

While the attainment of maximum economic efficiency through the interplay of free market forces appeals as the preferred objective of privatization, socio-political realities dictate that all governments will succumb to the temptation to intervene in markets in ways that improve their political positions. Therefore, realism requires that the operating definition of privatization should not be "divestiture", but instead, "the mobilization of private resources -- energy, skill, money -- to more effectively serve the needs of economic and social development". This definition includes the creation and existence of various forms of private sector-public sector competition and cooperation in agricultural markets in forms that fulfil social and political needs in the most efficient ways possible within real-world constraints.

Background and Current Situation

Modern-day marketing boards evolved from formal agricultural marketing schemes backed by powers of compulsion, which were created in Australia, Canada and East Africa in the early 20th century as results of agricultural interests seeking to increase their bargaining power with respect to product prices.

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During the world depression of the 1930's price breakdowns under the weight of excess supplies of agricultural products led governments in Australia, New Zealand, Canada, the United Kingdom, the United States of America and South Africa to establish compulsory marketing schemes for many agricultural products. Statutory marketing agencies were granted powers to compel producer participation in domestic price support schemes based on subsidies, regulation of quantities sold and pooling of returns from domestic and export markets.

The need during World War II for colonial powers, especially Britain, to ensure reliable supplies of agricultural products prompted the establishment of marketing boards in numerous developing countries. Their success led to their proliferation after the war, especially in Sub-Saharan Africa.

With the advent of independence from colonialism, leaders of new governments were faced with the problems of providing basic food supplies at cheap prices to low income consumers and of maintaining the agricultural export base. Since agriculture is in many cases the principal economic sector, it became the logical "milch cow" from which could be obtained financial and raw material resources to satisfy the new leaders' perceptions of the need for an industrial base to create urban employment, for economic diversification and for import substitution.

Therefore, export-related marketing boards were retained and new ones created to deal with the basic domestic food staples. The former were sources of foreign exchange, the latter a drain on the Treasury, requiring heavy subsidization of

product handling and sales to consumers. All provided means for selective taxation of agriculture to finance development in other sectors, usually benefitting urban areas at the expense of rural dwellers. All became labour sinks providing sinecures for friends, relatives and cronies of ruling elites. The results have been increasing drains on the public purse, increasingly distorted economic signals and major disincentives to domestic suppliers of food staples to produce marketable surpluses.

The damaging effects of the Boards' actions have been exacerbated by the well-meaning, no-strings-attached assistance of international donors in providing food staples at highly concessional rates. Availability of cereal grains through this mechanism has reduced the incentives for many governments to pay more than lip service to the necessity of undertaking the policy reforms needed in the areas of production, marketing and pricing which stimulate domestic production by small farmers. Instead governments have spent lavishly on prestige projects which have contributed only to the drain on the treasury and to the need to further tax the agricultural sector through discriminatory pricing in order to bolster urban areas.

At the same time, foreign donors have for the most part taken a project-oriented approach to technical assistance rather than a farming - systems approach which would allow decisions on development to be taken in the context of the entire socio-economic and political environment of which agriculture is but a component, albeit an important one. The results have been, too

often, defeats snatched from the jaws of victory. The well-documented case of the bankruptcy and governmental abolition of the Senegalese groundnut and cereal grains marketing board, ONCAD, in 1981, is a classic example. This Board offered high producer incentive prices to stimulate increased maize and sorghum production, along with a purchase guarantee. The stimulus worked so well that ONCAD incurred substantial costs to the Treasury in honouring its commitments. Furthermore, the incentive to produce the cereals was so great that the substitution by growers of cereal production for groundnuts caused a significant drop in the latter, a major export earner.

However, despite the dismal records of marketing boards in many developing countries, their operations in some places have not caused evident harm. Australia, New Zealand, South Africa and Canada still rely on the Boards to regulate production, handling and marketing of agricultural products. In the U.S.A., production and marketing of many fruit and nut crops is controlled through statutory marketing orders administered by cooperatives, while cereal grain production and marketing is heavily subsidized by the public purse. The same is true of the European Economic Community. Certain developing countries; Turkey, Philippines, India and Mexico for example; have succeeded in markedly increasing agricultural production by a combination of new technologies and price incentives provided by government. The distinguishing feature of these successes appears to be that these nations have been able largely to self-

finance the costs of providing subsidies to the agricultural sector without undue strain on limited resources such as has occurred in many developing countries.

In contrast, Mali is an interesting example of an ongoing attempt by a donors' group in cooperation with a host country to reform the operations of a marketing board and to privatize the marketing of cereal grains. The Government of Mali agreed in 1980 to restructure the cereals market over a six-year period, during which time incentive prices to producers and subsidies to consumers would be adjusted gradually to reflect market conditions. OPAM, the marketing board, would no longer enjoy a grain marketing monopoly but would act instead as a market coordinator and buyer and seller of last resort. In return, the donors' group pledged food aid on highly concessional terms for domestic resale by the government. The counterpart funds thus generated are committed specifically to financing the subsidies required over the six-year period. Reportedly, this program has been successful in meeting the initial goals. The nascent private sector is growing and the role of the marketing board has devolved to that of coordination rather than intervention.

Issues in Privatizing Marketing Boards

Marketing boards are used by governments to implement policies in three areas:

* Pricing and price administration
* Production management
* Marketing of products.

In most developing countries, the principal constraint on agricultural production is the lack of incentives to farmers to grow marketable surpluses. These incentives are lacking in respect to their price expectations, their self-determination as to the crop-mix to be grown and the degree of certainty they can attach to the timely marketability of their products.

Pricing. In most developing countries, prices are kept as low as possible for the benefit of poor, urban consumers who rely on traditional staples. To the ruling elites of such nations, the operational definition of an "affordable" consumer price is that which is sufficiently low to buy-off the potential political opposition of the urban populace. Since most governments do not have funds sufficient to provide heavy subsidies to consumers while paying realistic prices to producers, the latter suffer by receiving very low prices paid by the marketing boards, which are usually the sole legal product outlets. In such cases, the working definition of a "reasonable" return to farmers is what is left over after the consumer subsidy and the excessive management costs incurred by the bloated bureaucracy of the Board itself. This "reasonable" return is often so low as to provide no incentive for production above subsistence levels. Worsening this problem is the fact that in many countries, for reasons usually linked to foreign exchange shortages, there is a dearth of consumer goods on which the farmer could spend excess cash if he had it. Therefore, even if realistic prices were paid by the Boards, they would in many cases not induce production of marketable surpluses since money, in the absence

of goods to purchase, becomes of little meaning. The lack of incentives to earn excess disposable income is, of course, one reason that governments get away with subsidizing urban consumers at the expense of farmers in many countries. The lack of a rallying point makes small farmers difficult to organize and renders them politically impotent.

The costs of running the bureaucracy of the Boards themselves is a major contributor to the shortage of financial resources that could be used to pay a truly reasonable return to farmers. Often, these organizations have as their primary purposes the "employment" of the politically and otherwise favoured members of society, and the provision of questionable income to the powerful. Their role in the agricultural productivity of the nation is at best secondary.

Thus, the price-related issues to be considered in privatizing marketing boards are:

* prices paid to producers
* prices charged to consumers
* the costs of running the Boards
* availability of consumer goods.

Production Management. In addition to and related to their roles in setting and administering prices, marketing boards are often used to enforce production quotas, usually production ceilings, but sometimes minimums imposed by cropping area regulations.

The limitation of production is a common feature of the agricultural policies of developed nations. These ceilings inevitably create ecoomic inefficiency which is exacerbated by

susidies of various sorts paid to compensate farmers for reduced output.

In cases where minimum cropping requirements are imposed on producers, inefficiencies are introduced by the forced product-substitution and associated inputs and by the resulting price signals.

Therefore, the production-related issue in privatizing the Boards is the role of production quotas in the agricultural economy and the appropriateness of their continuation.

Marketing of Products. Marketing boards in developing countries are usually the sole legal purchasers and sellers of products within their purview. Fortunately for private sector interests, enforcement of the monopoly role is usually ineffective, the result being a flourishing informal marketing sector with products reaching consumers through entrepreneurs in a parallel and illegal marketing channel. Governmental efforts to use their official marketing channels to eliminate or restrict the role of private operators, while largely unsuccessful, usually result in the misallocation of national resources and the introduction of costly inefficiencies.

As noted earlier, all governments intervene to some extent in agricultural markets, and there is justification for this in cases where governmental involvement is necessary for reasons of social equity and market stability.

The marketing issue to be addressed in the process of privatizing marketing boards is that of the degree to which public agencies should be involved. Price stabilization and

buffer stock programs may be valid public objectives, whereas involvement in direct trading should be left to private interests. The question to be answered is that of how to accomplish this end.

Options for Privatizing Marketing Boards

To promote effectively the production of basic food staples and to create a viable, self-sustaining agricultural capability in developing nations it is necessary to strengthen the role of the private sector in production and marketing of agricultural products. This requires that governments abandon their costly monopoly over product markets and reduce their regulatory intrusions in the production and distribution process to the minimum level required to ensure market stability and to provide for the deprived in society. All operational production and marketing processes that can be undertaken by the private sector should be divested by the marketing boards, whose functions should devolve to those of market organization and buyers and sellers of last resort. Similarly, all official controls over producer and consumer prices should be phased out and market-clearing prices allowed to occur.

Given the socio-political value of the marketing boards, considerable external assistance is likely to be needed to induce governments to cede control over markets to the private sector. For developing countries with scarce resources, there are really only two feasible options:

1. recurrent financial assistance from donor agencies to back up the efforts of government to stimulate the private sector. Especially important would be the provision of funds to support increased producer prices and to compensate consumers for the reduction of subsidies;

2. an initial financial contribution from foreign sources, conditioned on a host government schedule to bring producer prices and consumer costs into equilibrium by phasing out governmental interventions.

The likelihood of the first option finding acceptance by donors is low, since it involves the unattractive prospect of long-term commitments by donors without any real leverage on their part to induce the government to change its policies.

The second alternative, in which financial assistance is both finite and conditional, is likely to find acceptance. In fact, this is precisely the model followed by the donors group assisting Mali in privatizing OPAM, as described earlier. This option appears feasible for adaptation to different marketing boards in numerous countries.

The taking of such steps to allow free markets to develop and to permit private interests to operate in them is a necessary but not sufficient condition for establishment of a viable agricultural base. Other matters affecting farmers' incentives to produce must be taken care of if marketable surpluses are to exist. Consumer goods must be made available for purchase by these producers using their disposable income;

access to credit markets must be facilitated; availability of technical assistance and advice on new technologies must be increased; and the means of increased production, machinery, fuel, seeds, fertilizers and other chemicals must be made readily available in free markets at affordable prices. To accomplish all of this, it is necessary to privatize not only the marketing boards, but the other parts of the agricultural sector and other sectors of the economy that provide resources to and use the products of the farmer. This is the subject of a companion paper by this author.