PD-ABT 958
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UNCLASSIFED

PRIVATE SECTOR SUPPORT PROGRAM

656-0208 & 656-0218

PAAD AMENDMENT

NUMBER TWO

USAID/Mozambique
July 1990

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MOZAMBIQUE

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Agency for International Development
Washington, D.C. 20523

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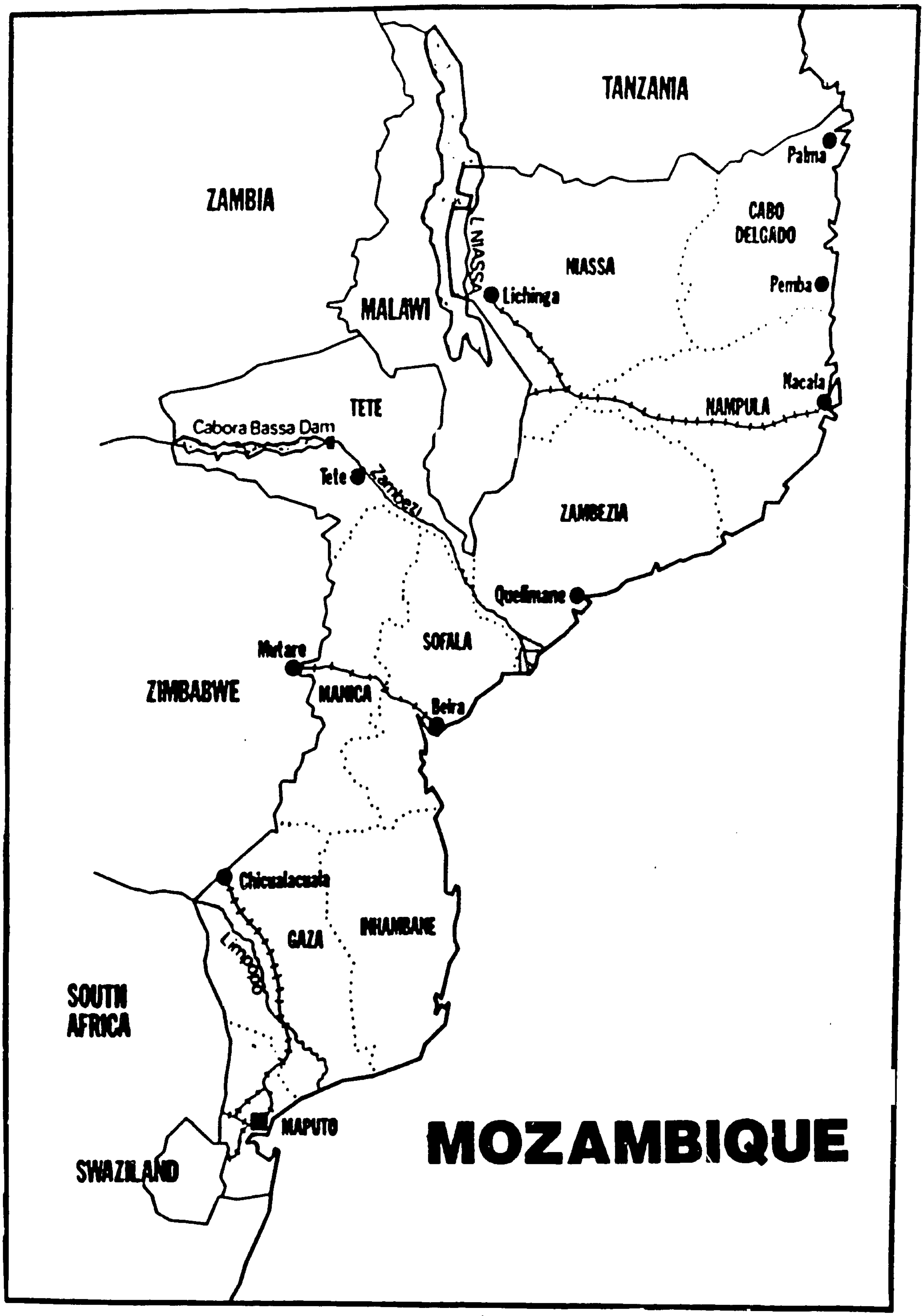
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ACTION MEMORANDUM FOR THE ACTING DIRECTOR, USAID/MOZAMBIQUE

FROM: Carlos Pascual, Program Officer

SUBJECT: Amendment to the Private Sector Support Program (656-0208/0218)

I. Problem

You are requested to: (a) approve an amendment to the Private Sector Support Program (PSSP) to increase nonproject assistance funding by $10 million to $54.05 million and to increase the LOP total to $55.55 million; (b) authorize $10 million for obligation in FY1990; and (c) reconfirm a waiver of agency policy to allow placement of local currency generations under the program in a non-interest bearing account. This PAAD Supplement is being funded through the Africa Economic Policy Reform Program (AEPRP), which provides supplemental funds to Mission OYBs in support of specific sectoral-level policy reforms.

II. Background

The purpose of the PSSP is to improve incentives for private sector agricultural production in order to enhance the private agricultural sector's production and income. To achieve this purpose, the original PSSP addressed four fundamental constraints to private agricultural production -- prices, land access, availability of inputs, and availability of foreign exchange -- through policy reforms to increase incentives to produce. Funds were provided to increase the availability of foreign exchange ($44.05 million) and for technical assistance ($1.5 million) for an LOP total of $45.55 million.

When the PSSP was developed, the Mission identified marketing as another constraint, but did not have sufficient knowledge of the sector to include it in the PSSP policy agenda. The PAAD proposed that an amendment be developed in FY1990 to focus on market reform issues. AID/W approved this approach with the approval of the PSSP PAAD. In 90 Maputo 0135 USAID presented to AID/W a concepts paper which set forth an initial policy framework for this amendment and proposed adding $10 million to the non-project assistance component to be financed under the AEPRP. 90 State 101281 gave AID/W's formal concurrence with further program development.

Policy reform progress under the PSSP has been fully satisfactory during the program's first year. USAID submitted a detailed policy progress report to AID/W in 90 Maputo 1336. AID/W indicated its concurrence in 90 State 235374.

III. Discussion

A. Policy Framework

USAID completed a detailed analysis of marketing constraints in order to develop the policy reform agenda for this amendment. Table 3 in the PAAD Supplement summarizes these constraints. USAID's analysis in the PAAD Supplement concludes that changes in the Government's marketing policies can significantly enhance incentives to agricultural production and marketing by removing both pricing and administrative regulations that currently discourage the development of competitive rural markets. A revised matrix that incorporates the proposed marketing reforms into the overall PSSP policy agenda is provided in Figure 1.

Pricing reforms will address disincentives associated with inadequate marketing margins between producer and consumer prices, panterritorial and pantemporal prices that do not reflect transport and storage costs, and transport tariffs that do not cover costs and risks. In developing the reform package, USAID and the Government sought to maximize the role of the market in determining prices and to avoid instituting new regulations that would impose additional administrative demands on government. The above pricing concerns were addressed through combination of (1) producer floor prices (as opposed to previously fixed producer prices) to protect producers from limited competition for their crops, and (2) phased liberalization of consumer prices, thereby allowing the market to determine seasonal price variations and appropriate marketing margins.

A second set of marketing policy reforms will lead to the elimination of administrative regulations hindering free trade and open competition. The reforms will secure free movement of commodities across geographic areas, unrestricted participation and competition in wholesale trade, and efficient licensing of traders and transporters. The PAAD Supplement proposed to focus these market reforms on the provinces of Cabo Delgado, Nampula and Zambezia, which are highly productive areas with high population concentrations, and to use the experience from these three provinces as the basis for expansion to national policy. However, the Government agreed during the agreement negotiations to implement these measures immediately on a national basis given their prospective boost to rehabilitating the country's deteriorated private trade networks.

B. Disbursement Mechanism and Commodities

All funds obligated under this amendment will be disbursed through a commodity import program (CIP) which will finance trucks and spare parts for the provinces of Cabo Delgado, Nampula, and Zambezia. Although the marketing policy reforms will be implemented nationally, it makes sense to focus the commodity

Figure 1

Mozambique Private Sector Support Program (656-0208)
Summary of Policy Objectives and Workplan
July 1990 Revision

BEST AVAILABLE DOCUMENT

POLICY AREAS	1989/90	1990/91	1991/92	POLICY INDICATORS	IMPACT INDICATORS	MEANS OF VERIFICATION
1. Agricultural Pricing Policy	OBJECTIVE: To maximize the liberalization of the agricultural pricing system and, for crops where full deregulation may not be presently feasible, institutionalize procedures for basing agricultural prices on world parity.			- Price changes and announcements.	- Production increases on family and commercial farms. - Farm income increases on family and commercial farms. - More consistent supply in markets throughout year.	- Production statistics by crop, province, farm type. - Estimated farm income calculated from production functions. - Selected market surveys.
a. Maize, beans, rice	- Establish parity producer prices; plan for floor price system. (Note: beans actually moved to floor price in 1989.)	- Move white maize and rice to parity-based producer floor price system;continue parity-based producer floor price for beans; assess impact and make recommendations.	- Adjust producer floor prices to maintain parity base.			
b. Cash crops	- Establish parity-based floor price system.	- Adjust floor prices to maintain parity base.	- Adjust floor prices to maintain parity base.			
c. Consumer prices		- Deregulate consumer price for white maize; assess impact; make recommendations re: beans and rice.	- Implement recommendations.			
Timing	- Before planting decisions.	- Before planting decisions.	- Before planting decisions.			
2. Divestiture of State Farms	OBJECTIVE: To develop and initiate the implementation of a divestiture program (including supporting policies for rational land redistribution, titling and registration) to redistribute state farms to commercial farmers.			- Declared policies on land redistribution including divestiture and titling procedures. - Development and promotion of divestiture program.	- Farms privatized. - Production increased on divested farms. - Farm income increased.	- Statistics on actual and planned divestitures. - Production statistics by crop in divestiture areas. - Estimates of farm income calculated from production functions and verified by sampling.
a. Planning and implementation	- Continue case-by-case divestitures of state farms. - Identify issues and policies to be addressed in divestiture program. - Complete terms of reference for additional tenure analyses and design of divestiture program.	- Implement analysis program on tenure issues. - Complete general divestiture program design. - Complete design of USAID-specific program for pilot divestitures.	- Implement USAID-specific pilot divestiture. - Continue divestitures in accordance with general program. - Refine divestiture policies, as needed, based on pilot divestiture.			
3. Private Ag. Sales and Service	OBJECTIVE: To demonstrate the effectiveness and viability of private sales and service networks for providing agricultural inputs to commercial and family farmers throughout the country.			- Percentage of private companies/traders participating in program. - Elimination of "credential system" for end users.	- Wider and better access to agricultural inputs. - Expansion of privatization.	- Statistics on numbers of private importers and dealers by input type and province. - Sampling of farmer attitudes toward supply networks. - Sampling of dealers to assess constraints to expansion.
a. For importers/distributors	- Continue private importation and distribution of all A.I.D. commodities; exemption for lubricants and limited spares.	- A.I.D. commodity imports fully private; plan to privatize ag-related public enterprises.	- Begin privatization plan.			
b. For end users	- Replace GOM administrative allocation system with direct private sales.	- Maintain.	- Maintain.			

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Mozambique Private Sector Support Program (656-0208)
Summary of Policy Objectives and Workplan
July 1990 Revision

POLICY AREAS	1989/90	1990/91	1991/92	POLICY INDICATORS	IMPACT INDICATORS	MEANS OF VERIFICATION
4. Access to Foreign Exchange	OBJECTIVE: To establish a process of testing foreign exchange allocation options that will increase the access of private entrepreneurs in the agricultural sector to foreign exchange and institutionalize market signals as an allocation mechanism.			- Implementation of FX allocation options agreed upon with donors.	- Increased access to foreign exchange at market-determined price.	- Survey of OGL users to determine private sector access.
a. Allocation mechanism	- Establish limited trial of OGL system.	- Evaluate effectiveness of OGL trial (with IBRD with USAID followup). - If trial is generally successful, modify and expand eligible sectors under OGL; otherwise formulate new options.	- Plan to extend OGL framework to larger portion of FX or test other allocation options.	- Range of eligible OGL sectors and volumes of FX increased.		- Trends in official and parallel exchange rates.
5. Private Marketing Channels	OBJECTIVE: To reduce restrictions on competitive private sector trade and transportation serving agricultural producers in Cabo Delgado, Nampula, and Zambezia provinces.			- Announcement and promotion of deregulations.	- Increased number of active traders and transporters.	- Sampling of traders/transporters/farmers.
a. Movement of commodities		- Rescind regulatory restrictions on inter-district and inter-provincial movement of agricultural commodities.	- Assess impact.		- More consistent supply of commodities in markets throughout the year.	- Market surveys.
b. Wholesaling		- Open district wholesaling opportunities to any licensed trader desiring to compete.	- Assess impact.		- Increased producer access to consumer goods and other "incentive" commodities.	- Sampling of farmers.
c. Licensing		- Analyze licensing requirements for private marketing agents at all levels to assess disincentive effects.	- Simplify licensing requirements based on analysis and encourage new competitors.		- Improved food balances between deficit and surplus production areas.	

support on provinces which have the highest agricultural potential, and which have relatively secure transport corridors. Financing for transport equipment will address one of the marketing constraints identified in the PAAD supplement, and will complement policy reforms leading to a more competitive marketing environment. Private firms will import and distribute all financed commodities.

In 90 State 101281, AID/W expressed concern that the Mission consider financing the maximum number of small-size, lower cost vehicles under this amendment in order to facilitate new entrants into the marketing sector. This concern was addressed in the range of vehicles to be imported over both the normal increments of PSSP commodities and those financed under the marketing supplement. Previously, the PSSP financed trucks in both the two-three ton range and the eight-ton range. Imports under the previously approved PSSP will now be concentrated on three-ton vehicles. Larger vehicles, mostly between eight and twelve tons, will be financed under this supplement. The overall impact is to increase the number of smaller range vehicles to be imported, while ensuring that an adequate number of mid-range vehicles are also provided to support commercial marketing.

C. Local Currency

The local currency use plan will not change from that described in the original PAAD. The PAAD identified several priority areas of Government budget support which are consistent with "the proposed sector of the reform program", in accordance with the Africa Bureau's guidance of July 1988 and Agency guidance contained in State 327494, dated October 1987. One of these priority areas is road rehabilitation and maintenance. Should the Government, in collaboration with the World Bank, successfully establish a new road maintenance fund, highest priority would be given to using local currency generations under this amendment for that purpose.

D. AID/W Concerns

AID/W, in 90 State 235374, responded to the Mission's progress report on the PSSP and concluded that satisfactory progress had been made. In addition, AID/W raised several concerns which it requested to be addressed in this PAAD Supplement. Key issues are discussed below.

1. Agricultural Producer Prices. AID/W was concerned that the producer floor price system would be costly to administer and implement, and therefore urged quick movement beyond the floor prices to market-determined prices. The Mission shares AID/W's interest in having the market determine prices, and we in practical terms have achieved this objective. The proposed floor price system *de facto* acts as a guide to producers and traders in an environment with limited market information. Use of the

official exchange rate to calculate the floor prices insures that actual prices are, in practice, market determined. The administrative cost of calculating and announcing the floor prices is minimal, and is generally done in conjunction with the World Bank. The financial cost of implementing the floor price will also be minimal. As discussed in the PAAD Supplement, the Government has withdrawn Agricom, the marketing parastatal, from primary level (i.e. farmgate) purchases, in effect relieving it of the requirement to enforce floor prices. Retaining the floor price system serves useful internal political purposes and is consistent with the general policy agenda agreed upon by the donor community in the context of Mozambique's Policy Framework Paper.

2. Divestiture of State Farms. AID/W points out that, although substantive and adequate progress has been made toward divestiture of state farms and rationalization of land policies, the overall objectives and policy benchmarks in the original PAAD may need to be revised. This has been done in the new policy matrix, which drops reference to an action plan specifying individual divestitures and incorporates the concept of a divestiture program which is policy-based and consistent with the need to approach each divestiture on a case-by-case basis. Design and implementation of the divestiture program is being done with the assistance of the Land Tenure Center at the University of Wisconsin.

3. Private Networks for Agricultural Inputs. AID/W compliments the Mission for the progress made in this area and notes the potential spin-off effects of liberalized input sales/service on the rural economy. AID/W encourages the Mission's proposal to work with the Government to identify specific agriculture-related public enterprises for divestiture. However, it also queries whether it might not be possible to move beyond identification of enterprises to developing a divestiture action plan. This could be a desirable step, but it is difficult to judge at this stage whether it would be practical or useful. Similar issues were confronted in formulating an action plan for state farm divestitures. Both the Government and USAID found that an action plan would have limited utility if buyers were not interested in the enterprises proposed for divestiture. Such interest will, in fact, depend on a range of factors including the financial terms of the divestiture, the handling of past debts, the cost of rehabilitating and restructuring the enterprise, and its estimated productive capacity. The Government and USAID therefore propose to focus attention on identifying solid divestiture candidates. Once such candidates have been identified, actual divestitures are most likely to evolve through case-by-case negotiations which are generally initiated by private parties.

4. Access to Foreign Exchange. AID/W indicated that if it is not possible to decide whether USAID will support the OGL (locally called the SNAAD) in 1990/91, specific steps should be outlined

for further expansion and analysis of the SNAAD. The Government has, since the submission of the PSSP progress report to AID/W, already expanded the SNAAD to a limited range of agricultural inputs. They have completed the fieldwork component of an evaluation with the World Bank. USAID will supplement this evaluation with its own internal assessment which will cover, among other issues, importer attitudes toward the SNAAD, the capacity of the banking system to provide complementary services, and whether the SNAAD's accounting and operating systems will enable A.I.D. to meet its accountability/tracking requirements. These measures comply with AID/W's guidance.

5. AEPRP Financed Activity. AID/W delegated authority to USAID to authorize the AEPRP activity proposed in the PAAD Supplement. It requested that the Mission submit to AID/W for informal comment the new policy matrix (Figure 1), the draft letter of intent, and a revised local currency use plan only if substantive changes are contemplated. The first two items have been transmitted by FAX. As indicate above, no substantive changes were made in the local currency use plan.

E. Financial Plan

Table 1 below provides a new financial plan for the private sector support program. Of the $10 million to be obligated under this amendment, $4 million will be immediately eligible for disbursement given the satisfactory progress on the PSSP and the fact that the Government has already submitted a letter of intent to USAID which satisfactorily addresses all of the 1990/91 policy benchmarks identified in Figure 1. The remaining $6 million from this obligation will be disbursed in FY1991 when the Government satisfies the conditionality for disbursements in excess of $30,050,000. (See discussion under "Prior Actions" below.)

TABLE 1
SUMMARY FINANCIAL PLAN
($ 000s)

	FY 1989	FY 1990	FY 1991	TOTAL
Commodity Import Assistance	13,550	12,500	13,000	39,050
AEPRP Amendment	0	10,000	0	10,000
OGL Financing	0	0	5,000	5,000
Subtotal Generating L/C	13,550	22,500	18,000	54,050
Technical Assistance	0	600	900	1,500
T O T A L	13,550	23,100	18,900	55,550

IV. Prior Actions

A. Letter of Intent

USAID's practice has been to obtain from the Government prior to obligation of funds a letter of intent which sets forth the Government's policy program in accordance with the policy objectives summarized in Figure 1. The Government has submitted, and USAID has accepted this letter of intent, a copy of which is included in the PAAD Supplement as Annex F.

B. Disbursements in Excess of $13,550,000

Prior to disbursing funds in excess of the $13,550,000 obligated in FY1989 and up to a total of $26,050,000 (i.e. a difference of $12,500,000 already obligated under Amendment 1 to the PSSP in FY1990), the Government must submit to USAID an update on policy progress in 1989/90 and a work plan for 1990/91. This was included in the above mentioned letter of intent, thus allowing for immediate disbursement of these funds.

C. Disbursement in Excess of $26,050,000

Prior to disbursing funds in excess of $26,050,000 and up to $30,050,000 (i.e. an amount of $4,000,000 out of the proposed FY1990 incremental obligation for $10 million), the Government must submit to USAID a letter of intent which discusses, to USAID's satisfaction, the market reform issues identified in the policy matrix in Figure 1. Again, these issues were incorporated into the above mentioned letter of intent. These funds may therefore be disbursed immediately after obligation.

D. Disbursements in Excess of $30,050,000

Prior to disbursing funds in excess of $30,050,000, the Government must furnish USAID with evidence that adequate progress has been made on the 1990/91 policy agenda, and submit a policy workplan for 1991/92. This condition precedent to disbursement will apply to the $6 million balance being obligated in FY1990 and to any obligations in FY1991.

V. Special Concerns

A. Waiver of Interest Bearing Account Requirement

The Acting Assistant Administrator for Africa waived, with his approval of the original PAAD, the requirement that local currencies generated or deposited under the program be placed in an interest-bearing account. This waiver was in compliance with Agency policy as stated in 87 State 327494 which indicates that deposits in interest bearing accounts may be waived if such deposits might "undermine internationally supported stabilization agreements and sound monetary policy." Such a case applied at the time of the approval of the PAAD and continues to exist due to excess liquidity in the banking system. It is therefore considered appropriate to reconfirm the waiver of the requirement for an interest-bearing account and instead establish a non-interest bearing special account.

B. Responsible Officers

Elaine Kelly is now the Commodity Management Officer responsible for the CIP component. Carlos Pascual remains the Program Officer responsible for the technical assistance and policy component. Sidney Bliss, AFR/PD/SA, continues to be the responsible backstop officer in AID/W.

C. Source and Origin of Commodities

The source and origin of commodities financed under this amendment shall continue to be as set forth in the Africa Bureau instructions on Implementing Special Procurement Policy Rules Governing the Development Fund for Africa, dated April 4, 1988, as may be from time to time amended.

D. Clarification of Original PAAD Facesheet

The original PAAD facesheet contained a typographical error as a result of a line being excluded. AID/W requested that this error be noted in this Action Memorandum to avoid any confusion in the future. The PAAD face sheet should have indicated that "...the PAAD facesheet may be amended by the USAID/Maputo Director to increase the authorized level of funding for CIP disbursement. AID/W approval is required to increase the authorized level of funding by the amount to be obligated for disbursement to the Open General License (OGL) system in Mozambique..."

E. Notification of Congress

A Congressional Notification expired without objection on July 12, 1990, as indicated in 90 State 229550.

F. Authority

In 90 State 235374, the Acting Assistant Administrator for Africa delegated authority to the Mission Director, USAID/Mozambique, to amend the authorization for the Private Sector Support Program to increase the approved life-of-project financing to $55.55 million.

VI. Recommendation

That you: (a) approve an amendment to the Private Sector Support Program to increase nonproject assistance funding by $10 million to $54.05 million and to increase the LOP total to $55.55 million; (b) authorize $10 million in additional obligations in FY1990; and (c) reconfirm a waiver of agency policy to allow placement of local currency generations under the program in a non-interest bearing account.

APPROVED ______________

DISAPPROVED ______________

DATE 19 JUL 90

DRAFTED: C.PASCUAL, PRM, JULY 3/17, 1990

CLEARANCES

L.CAPELAO, PRM draft, 7/5/90
E.KELLY, CMO emk
T.RIEDLER, RLA FAX 7/9/90
M.ROCHA, CONT MR 7/17
AFR/PD/SA Bliss/Pascual Telecon, 7/16/90

David Hutchner
(A) Director, USAID/Mozambique

8. OYB INCREASE

. FROM:
Carlos Pascual
Program Officer

TO BE TAKEN FROM:

9. APPROVAL REQUESTED FOR COMMITMENT OF:
$ 10,000,000

10. APPROPRIATION - ALLOTMENT
72-1101014; GSSA-90-31656-KG32

11. TYPE FUNDING	12. LOCAL CURRENCY ARRANGEMENT	13. ESTIMATED DELIVERY PERIOD	14. TRANSACTION ELIGIBILITY DATE
☐ LOAN ☒ GRANT	☐ INFORMAL ☒ FORMAL ☐ NONE	7/89 - 6/93	Date of Obligation

15. COMMODITIES FINANCED

Seeds; fertilizers; tractors, tractor spare parts, implements and harvest equipment; trucks and truck spare parts; and irrigation equipment, pipe and spare parts. (This is the full range of authorized commodities; only trucks and spares will be financed under this amendment.)

16. PERMITTED SOURCE	17. ESTIMATED SOURCE
U.S. only:	U.S.:
Limited F.W.:	Special Free World (935): $10,000,000
Free World: $10,000,000	Local:
Cash:	Selected Free World (941):

18. SUMMARY DESCRIPTION

Pursuant to the Foreign Assistance Act of 1961, the Foreign Operations, Export Financing, and Related Programs Appropriations Act, 1990, and the delegation of authority contained in 90 State 235374, I hereby authorize an additional increment of $10,000,000 of non-project assistance funding for the Private Sector Support Program ("Program") for FY 1990, and otherwise amend the original Program Assistance Approval Document ("PAAD") approved by the A/AA/AFR on August 24, 1989 as follows. The additional funding of $10,000,000 brings the total authorized Program funding to $36,000,050. The total anticipated A.I.D. funding approved for the Program is also increased by $10,000,000 to $55,550,000, with $54,050,00 for non-project assistance and $1,500,000 for project assistance. No funds authorized herein will be used for OGL financing. The reduction of restrictions on competitive private sector trade and transportation serving agricultural producers in Cabo Delgado, Nampula and Zambezia provinces is added as a fifth policy areas under the Program.

(Continued)

19. CLEARANCES	DATE
CMO: E. Kelly emk	7/19/90
CON: M. Rocha MR	7/17
RLA: T. Riedler FAX	7/11/90

20. ACTION

☒ APPROVED ☐ DISAPPROVED

D. Hutchner 19 July 90
AUTHORIZED SIGNATURE DATE

(A) Director, USAID/Mozambique
TITLE

CLASSIFICATION: UNCLASSIFIED

The addition of this fifth policy area to the Letter of Intent attached to the Program Grant Agreement as Annex C is a condition precedent to disbursement of the first $4,000,000 of the additional $10,000,000 authorized herein, and the condition precedent to disbursement of the final tranche of funds approved for the Program, as described in the original PAAD, will apply to disbursement of the $6,000,000 balance of the additional $10,000,000 authorized herein. Except as specifically amended herein, the terms and conditions of the original PAAD approved August 24, 1989, as previously amended, remain in full force and effect.

Mozambique Private Sector Support Program (656-0208)

Supplement to the Program Assistance Approval Document for Marketing

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Summary of Tables and Figures

Figures

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I. Program Factors

A. Macroeconomic and Policy Climate

Mozambique's economy has been dramatically transformed since 1987, when the government (GOM) began an Economic Rehabilitation Program (ERP) with IMF and World Bank support. The overall objective of the ERP is to restore macroeconomic balance through strengthened financial, exchange rate, and pricing policies. Market-oriented macroeconomic and sectoral policy reform measures undertaken in successive Policy Framework Papers (PFPs) have yielded measurable improvements in economic and financial indicators. Through these reforms, the government has:

- Devalued the real exchange rate by two-thirds;
- Introduced a non-administrative system of foreign exchange allocation for a limited range of raw materials and spare parts, with the intention of broadening the system as foreign exchange availability permits;
- Reduced the fiscal deficit including grants from over 13.5 percent of GDP in 1985/86 to an estimated 4.8 percent in 1989;
- Steadily reduced the growth rate in banking system assets;
- Reduced the number of commodities subject to fixed consumer prices from 46 to 20 and reset those prices with respect to border parity; and
- Reduced the number of products subject to administrative allocation from 43 to 15 so that private enterprises can now participate in most trading activities.

IMF-World Bank review indicates that the most striking feature of the ERP to date has been an increase in GDP in real terms of four to five percent annually, reflecting a substantial rise in marketed agricultural production of the family and private commercial sectors, a pickup in light industrial activity, and recently an upturn in transport volume.

The government's adjustment strategy is determined by the long-term nature of the adjustment process and of the transition to economic and financial viability, as well as by the need to reduce poverty.

The Program Assistance Approval Document (PAAD) for the Mozambique Private Sector Support Program (PSSP) describes in detail the approach and progress of the ERP through mid-1989. The government remains committed to rigorous implementation of the next round of adjustments as laid out in the latest PFP, which covers the 1990-92 period and recharacterizes the ERP as the Economic and Social Rehabilitation Program (ESRP). Key targets under the 1990-92 PFP are:

- economic recovery at an annual average rate of six percent;
- gradual reduction of the inflation rate to 10 percent by 1992; and
- reductions in the external current account, including grants and overall deficits.

The ESRP and donor resources in support of it have allowed Mozambique to stem its economic decline, but the continuation of the civil war imposes sharp constraints on the ability of the ESRP to generate economic recovery (and in the longer term, economic growth). Insecurity continues to restrict the responsiveness of agriculture and act as a major obstacle to the restoration of production, particularly in placing an extremely high risk premium on any potential private investment. Nonetheless, where security conditions permit, the GOM, with support from donor agencies and PVOs/NGOs as well as private investors, has begun the transition from emergency relief to rehabilitation activities, as the necessary next step toward investment and growth.

The government also is making courageous political reforms which will reinforce and amplify the benefits of a more market-based economy. A new constitution is expected to be approved in late 1990, after nationwide public debate. Provisions of the draft under discussion include among other significant reforms a fundamental change in property rights to permit private ownership of productive assets, including land. In addition, general elections are planned for 1991. These factors, together with pointed efforts to engage the insurgents in direct discussions leading to peace, demonstrate the GOM's determination to lay the groundwork and establish the incentives necessary to achieve the objectives of the ESRP.

Within this overall economic and political climate, phased reforms of policies affecting food and agriculture are paramount. Although emergency relief continues to be essential, measures are being taken to increase domestic food production and improve the ability of the marketing system to serve the needs of both producers and consumers. According to the 1990-92 PFP,

> "The Government's [ESRP] strategy is focused on the recovery of the agricultural sector, in particular the family sector, where the incidence of poverty is especially severe and the potential for growth is the highest. The implementation of this strategy rests fundamentally on continuing the restoration of price incentives to producers, providing them with improved agricultural support services and markets for their products, and maintaining an appropriate flow of consumer goods to the rural areas. A key element in this strategy is the revitalization of the distribution system, including private trade, and the rehabilitation of the transport infrastructure, particularly rural feeder roads."

Policy reform in food and agriculture centers on:

- Phased rationalization and deregulation of producer prices;
- Increased reliance on private sector actors and networks for the distribution of agricultural inputs, domestic production, and consumer goods;
- Improved effectiveness of the urban "food safety net," through consumer price reforms and targeting of subsidies;
- Restructuring and divesting extensive state farm holdings to enable more productive use of agricultural land and related enterprises;
- Increased availability of foreign exchange for agriculture-related imports under the system for non-administrative allocation of foreign exchange (SNAAD);
- Greater investment in rural road rehabilitation and maintenance; and
- Phased investment in agriculture in "priority districts" of each province as resources become available.

Mozambique's policy direction and progress are clearly attributable to the firm commitment of the government to relieve widespread misery in an effective and sustainable manner, but the nation's dependence on foreign aid cannot be overemphasized. Exports provide only 15 percent of the cost of imports, the rest being covered by foreign assistance; food aid provides nearly 90 percent of marketed grains; donor support covers nearly half of budgetary expenditures. These figures are unlikely to improve in the short run; indeed, the gaps may widen even further as the adjustment process proceeds. The GOM recognizes that donor coordination as well as intra-governmental coordination are critical to pursuing a coherent reform process and maximizing the impact of limited resources. These factors influence discussions on policy reform.

B. Role of Marketing in Overall Economic Development

As described above, the government's recovery strategy relies on increasing productivity and production in the agricultural sector, which employs 80 percent of Mozambique's labor force and whose output has grown at about 6 percent annually over the past three years. Agricultural productivity overall is extremely low for some of the same reasons as in other countries in the region: the extremely low level of technology and limited producer access to productive resources. As experience all over Africa has shown, these constraints to productivity will take generations to address, through research, human resource development, and legal and political adjustments.

In Mozambique, however, there is an opportunity for relatively quick production increases. Considerable land, labor, and financial resources lie dormant (some since independence) and unproductive, due to a combination of policy and security constraints. Policy adjustments have been made to provide production incentives (see Section III-C). These, and improved security in key districts that are historically high agricultural producers, have already resulted, sometimes over the span of a single agricultural cycle and sometimes even without new inputs or investment, in localized agricultural surpluses. It is critical to husband these production responses as they occur by ensuring that producers are able to find markets.

In the current war-affected situation, marketing channels and activities will continue to be geographically limited and the reach of their benefits similarly constrained. Nonetheless, in areas becoming secure from insurgent activities, the production responses to policy changes already are leading to increasing market activity, which of course further encourages production.

In the post-war situation and in the longer term, marketing will be key to bringing Mozambique's large and substantially underproductive rural populations into the national economy, by linking them to each other and to the rest of the nation. Given sufficient incentives, increasingly efficient marketing channels will enable goods and services to flow to producers as well as produce to flow to markets, mills, and ports. Over time, if allowed to develop in accordance with local and national market forces, these same channels will provide the rural populations new access to information, technology, training, and secondary industry and employment. Efficient, competitive marketing networks are thus far more than commercial vehicles; they are central to economic development.

Insecurity and emergency conditions prevailing throughout the country have generally discouraged, if not precluded, Government and donor investments in marketing, but that situation is beginning to change. For its part, the Government has begun to identify secure zones for investment and to encourage donors to focus resources in these areas. With the World Bank, the Government is developing a rural roads rehabilitation and maintenance strategy. UNDP and ILO have already helped the Government to undertake several successful pilot projects in labor-intensive road rehabilitation; techniques from these projects will be adopted in the World Bank/Government strategy. In Zambezia province, Save the Children (UK) has developed with the provincial transport authorities a program to rehabilitate key road stretches and to put in Bailey bridges at crossing points where bridges have washed out. In Nampula Province, the EEC plans to finance construction of storage facilities (generally small warehouses); it has already financed the import of 1-2 ton trucks, although these have been found too fragile to contribute usefully to commercial trade. The EEC has also worked with the Government to establish a local currency reserve, using food aid counterpart funds, to fund certain commercialization costs such as contracts with private transporters to transport agricultural commodities from surplus areas to market centers. (See Section II-B for further discussion and analysis of current marketing activities and patterns.)

The increasing attention being given to marketing issues reflects a growing awareness on the part of Government and donors that marketing constraints must be addressed to facilitate economic recovery as security conditions improve. However, most attention has been focused on physical and financial constraints, with very little analysis done on the policy environment for marketing activities. As is discussed in detail in the constraints analysis in Section II-C, there are many policies which create financial disincentives to private sector participation in marketing or which discourage the emergence of competitive markets. The reduction of these policy constraints is the focus of this PAAD Supplement.

C. Importance of Marketing in Mission's Assistance Strategy

As described in detail in the Mozambique Country Program Strategic Plan for FY 1990-92, the challenge for both the GOM and its donors is to continue to mitigate the worst effects of the emergency and, where security permits, to begin the transition toward self-reliance. In assisting Mozambique to meet this challenge, USAID's long-term program goal is to promote food security. Since attention to emergency needs runs parallel to the absolute necessity to regenerate productive infrastructure, the two sub-goals for the program are: first, to meet the subsistence food and basic health requirements of the absolute poor; and second, to increase food supplies through production and trade to levels that meet domestic consumption requirements. The strategic objectives defined for the 1990-92 period are:

One: Sustain an effective food safety net for the urban poor and those displaced and severely affected by war.

Two: Reduce, among target population groups, dependence on external food aid to meet subsistence requirements.

Three: Establish a policy environment conducive to private agricultural production and marketing.

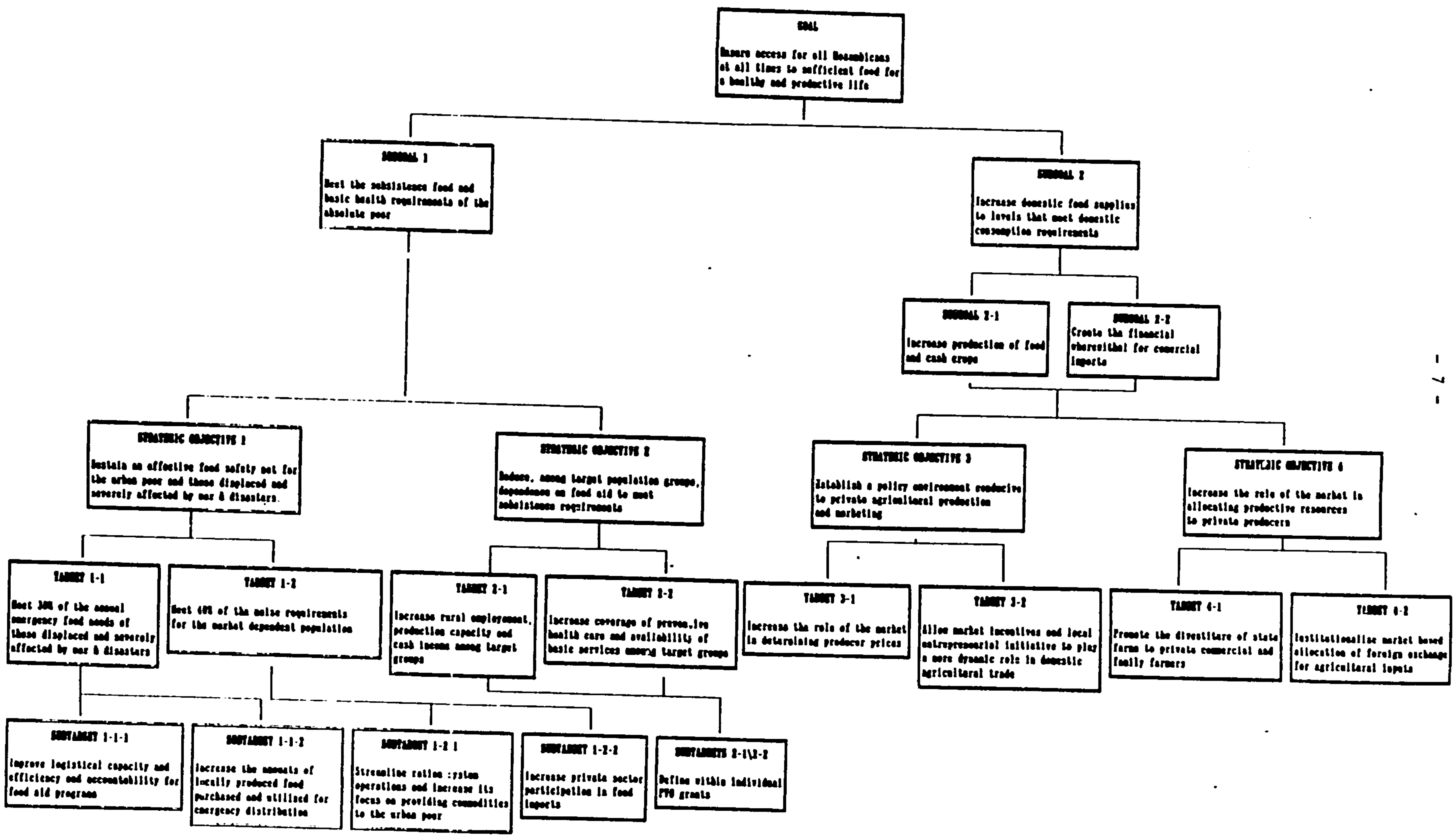
Four: Increase the role of the market in allocating productive resources to private producers.

Figure 1 summarizes this strategic framework. The policy reform agenda targeted under this supplement to the PSSP will directly contribute to achievement of strategic objectives three, particularly target 3-2: allowing market incentives and local entrepreneurial initiative to play a more dynamic role in domestic agricultural trade.

Specifically, USAID seeks to help the government make the full transition to market-based policies that reduce the scope for administrative discretion, institutionalize market-clearing prices, and encourage competitive marketing of commodities that supply national needs and earn the foreign exchange needed for input purchases. For most commodities, the government has phased out controls that limited marketing exclusively to the state sector, but many regulatory restrictions still create disincentives to private participation. The security situation makes central control of marketing policy particularly problematic as it pits bureaucratic decision-making directly against the risks and costs confronted by transporters and traders. The reforms targeted in this supplement will help the government phase out administrative controls on transport and marketing in order to allow those who have investments at stake and detailed knowledge of local conditions to exercise their judgment of marketing risks and profit.

Figure 1

USAID MOZAMBIQUE STRATEGIC FRAMEWORK - FY1990 - 1992



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II. Analysis of Marketing Systems

A. History of Agricultural Marketing

Mozambique's rural marketing system before independence consisted of some 6,000 rural traders, mostly of Portuguese origin, who acted as both the collectors of surplus produce from small farmers and the principal distributors of agricultural inputs and consumer goods for the family and small commercial sectors. Large export-oriented commercial operations did their own marketing, and sometimes also provided market services to smallholders in their areas of operation. Although marketing was left to private traders, there were restrictions on who could become intermediaries, where they could operate, which commodities they could trade, and what prices they could pay. Transport and trading functions were thus specialized and controlled; informal or local markets where farmers traded with each other as well as merchants did not exist.

At independence, the departure of both rural traders and large producers resulted in the complete collapse of the rural marketing network. The government tried to fill this vacuum by establishing "people's stores" (now defunct), consumer and producer cooperatives, and a host of government and parastatal operations. Government and donor support for marketing concentrated on these parastatal operations, initially for ideological reasons and later because a series of natural disasters and continuing insurgent attacks demanded direct government intervention to ensure food flows to displaced and affected populations. The government retained the principles of the colonial pricing and marketing system, but simplified it to eliminate quality differentiation, establish pan-territorial prices, and fix transaction margins at every marketing level from producer to consumer.

Although officially discouraged and vilified, a few private traders and transporters began to re-emerge in the mid-1980s, albeit in such scattered and tentative fashion that they did not adequately serve the rural populations in the areas where they operated. For many years, private traders and transporters received essentially no allocations for imports of new vehicles or spares; consumer goods, which have always been essential barter goods for primary-level marketing, were strictly rationed and their distribution determined centrally, which constrained development of local trading functions.

The government now recognizes that re-establishment of the agricultural marketing network depends on increasing competition among greater numbers of private operators, but their existence and activities continue to be limited in many ways by residual laws, regulations, practices, and attitudes of the pre-reform, central-control era. Agriculture-linked marketing today is extremely fragile, thin, informal, and costly.

B. Description of Agricultural Marketing Today

1. Overview of the Marketing System

One way to understand the agricultural marketing system is to trace the marketing chain from producers toward the end users. The flow of commodities from producer to consumer is overlayed by a contrary flow, through many of the same transaction points and actors, of food products, consumer goods, and agricultural inputs back to the producers. Describing these flows is not a simple task, given the diversity of factors affecting production and marketing of different crops in different areas of the country. The following description is heavily based on agricultural marketing in Nampula province. Among the provinces, Nampula is fairly typical in the variety and mix of crops produced, types of farms, population density, and variability of marketing options in different areas within the province; but it is atypical in other respects -- infrastructure less damaged by the insurgency, existence of a functioning private transporters' association, and some of the country's best soil and climate conditions for agriculture. (See Annex D for data on marketed production of principal crops by province and nationally from 1980 through 1989 and current estimates for the recent 1990 harvest.)

The family sector, as shown in Table 1 below, is the primary base for marketed agricultural production in Mozambique. For most crops smallholders account for upwards of 80 percent of marketed production. These marketing estimates are generally conservative since they are based on quantities marketed through the parastatal, Agricom. The portion of smallholder production which is not marketed through Agricom includes both household subsistence stocks and the unknown quantities which are marketed but do not at any stage enter public marketing channels. While no reliable estimates of the last-named quantities exist, there is widespread agreement that the importance of such entirely private sector marketing grew growing over the past two to three years for many crops, in particular cashew, but shrank in the case of maize.

The first marketing transaction point is at the farmgate. Commonly, the farm family will move its produce to the nearest location visited by a trader. Traders at this primary level are generally small operators; they may have trucks (either their own or rented) and deal in a range of barter goods and cash. (In Nampula, as in other provinces, the marketing parastatal Agricom has virtually abandoned earlier attempts to reach down to the producer level.) Usually there is one buyer, who is also the predominant supplier to the producer of sugar, oil, soap, and similar basic consumables. Smallholder producers in some areas benefit from visits by several traders or by the same trader at different points in the agricultural cycle; this situation is particularly evident in the

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Table 1

Marketed Production of Principal Crops
(Metric tons)

Product Farm Type	1981	1982	1983	1984	1985	1986	1987	1988	1989
Maize	78,322	89,151	55,803	82,581	58,581	21,474	27,331	44,579	80067
Family	36,843	36,454	24,984	40,432	29,651	11,678	16,315	34,247	64813
Others	41,479	52,697	30,819	42,129	28,930	9,796	11,016	10,332	15,254
Rice	28,860	41,542	17,268	19,088	17,894	19,018	31,587	31,725	22327
Family	1,172	1,689	1,562	3,581	3,083	5,888	9,033	4,126	10104
Others	27,688	39,853	15,706	15,507	14,811	13,130	22,554	27,599	12,223
Sorghum	977	1,561	1,314	2,141	1,812	672	512	880	2947
Family	590	1,023	915	1,628	1,372	597	411	827	2775
Others	387	538	399	513	440	75	101	53	172
Cassava (Dry)	10,909	9,506	8,542	3,512	6,367	6,006	7,270	12,304	6141
Family	10,755	8,991	8,501	3,388	4,290	5,867	7,083	12,282	6141
Others	154	515	41	124	2,077	139	187	22	0
Beans	14,879	6,873	4,724	3,549	3,612	2,821	9,205	7,146	14879
Family	14,000	6,162	3,304	2,803	2,692	1,926	8,657	6,739	14103
Others	879	711	1,420	746	920	895	548	407	776
Groundnuts	4,952	1,453	668	2,044	2,019	883	2,130	1,805	2061
Family	4,937	1,416	648	1,944	1,986	863	1,973	1,757	2005
Others	15	37	20	100	33	20	157	48	56
Sunflower	12,080	10,800	7,269	5,018	5,449	1,014	1,062	1,022	1644
Family	6,740	9,358	6,120	4,305	4,987	831	902	739	1295
Others	5,340	1,442	1,149	713	462	183	160	283	349
Copra	54,399	26,617	30,218	24,836	23,414	28,400	25,533	22,814	12505
Family	26,665	7,961	10,259	9,120	7,533	12,800	13,170	14,783	3505
Others	27,734	18,656	19,959	15,716	15,881	15,600	12,363	8,031	9,000
Cashews	92,000	56,600	16,800	25,200	29,100	40,169	37,535	43,641	50078
Family	92,000	56,600	16,800	25,200	29,100	40,169	37,535	43,641	50078
Others	0	0	0	0	0	0	0	0	0
Total Production	297,378	244,103	142,606	167,949	148,248	120,457	142,165	165,916	192,649

SOURCES: AGRICOM - Informacao sobre Comercializacao
Agricola em 1988/89
- Documento Final da Reuniao do
Colectivo de Direccao Alargado
de 12/03 a 24/03/90

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growing cashew trade in districts surrounding the processing plant at Angoche. In some cases, smallholders may join together to hire a truck to market their produce, avoiding the farmgate transaction altogether. Commercial producers, even those of relatively smaller scale, move their produce themselves and do not commonly trade at the farmgate.

The second key transaction point is at the district wholesale level in larger towns or district capitals, where several traders, retail and wholesale, may be present, as well as Agricom. Farmers bringing their own produce to this level generally trade with retailers for consumer goods. Primary-level traders bringing produce from the farmgate principally trade it with wholesalers who often provided them goods (oil, soap, etc.) on credit; the repayment is generally made in commodities, with implicit interest. For some crops, the wholesaler will transport the produce to the provincial capital or to a processing center or port. In the case of maize, however, wholesalers (and some of the retailers) as well as larger producers bringing their produce to market themselves will immediately sell directly to Agricom, principally due to price distortions discussed further below.

Commodities are next traded in provincial capitals or other larger towns. In Nampula province, most transport is done through private transporters. For maize, Agricom contracts with private transporters to move stock to provincial warehouses. Other commodities tend to be held and transported by private wholesalers. Once moved, commodities are sold to mills (largely parastatal operations but sometimes private) or to private or public enterprises acting as either wholesale or retail buyers. These may be, for example, factories or export-oriented commercial farms with large workforces, agriculture-linked industries such as oil or sugar refineries, or poultry farms. Agricom holds the major stocks of maize at this level also, but other food crops move into the markets, and export crops into processing plants or ports.

Domestically produced food staples may cross with the massive quantities of imported food* now entering Mozambique at any of these transaction points, but such intermingling occurs mostly at the mills and at the retail consumer level in the larger towns. At the

*Maize imports (an estimated 30 percent of national cereal needs) are provided entirely through food aid, and totaled about 250,000 metric tons in 1989. These imports are used for both free distribution to populations displaced or otherwise affected by the insurgency (40 percent of the total), and commercial distribution through normal channels (60 percent of the total), including the ration systems of Maputo and Beira. See the November 1989 World Bank Food Security Study for a more detailed description of the distribution channels for food aid.

district wholesale level of the marketing chain such intermingling is not common (although instances are reported of imported food intended for free distribution under the rural emergency program finding its way into the commercial system in the districts).

2. Key Actors

Among public actors affecting rural markets, the most important is Agricom, the parastatal marketing enterprise established in 1981 under the Ministry of Internal Trade (now the Ministry of Commerce) to undertake the marketing of crops produced by the family and cooperative sectors. Agricom has played the lead role in inter-district and inter-provincial movement, bulking, and storage of smallholder food and cash crops. In this effort, Agricom uses its own truck fleet and also hires transport from both parastatal enterprises and private fleets. For much of its life, Agricom also acted as residual (and often only) primary-level buyer in many rural areas, and was also virtually the only source of agricultural inputs and basic consumer goods for small producers. Recently, Agricom's policy has been to withdraw from primary-level marketing, leaving this to private operators, and concentrate on storage, including maintaining of local stocks, and inter-district movements.

Private sector marketing intermediaries at various levels are extremely diverse:

(i) Farmers range from semi-subsistence family enterprises to sizeable modern commercial operations.* The former may be virtually isolated from market opportunities, the latter oriented to export or industrial markets, and there are all kinds of variations in between. The remoteness of a producer from markets is not strictly physical distance; level of education, availability of resources beyond family labor, and many other factors contribute to this economic distance. The rapidity and extent of benefits to farmers of improvements in private marketing channels will vary considerably according to this remoteness. There is evidence that even those who might be expected to be most isolated and last to perceive the benefits of marketing improvements, i.e., the truly rural smallholders, are already responding promptly to price incentives. Increased marketing opportunities must follow quickly to reinforce these initial production responses.

(ii) District-level retailers also vary enormously. Some proportion of traders at the primary level are individuals operating informally; considerable numbers of new entrants may become visible as restrictions are lifted. Other primary-level buyers are town-based enterprises with their own or rented trucks, making annual forays into producing areas to buy particular crops. Some sources indicate that some town-based agents do not presently trade at the primary level but are considering doing so; lifting of price and trade controls, and/or increasing availability of transport vehicles, could catalyze these to begin district-level trade. With

*See the World Bank's Mozambique Agricultural Sector Survey, 1988.

the recent re-establishment in Nampula of former colonial agricultural enterprises under new private or joint (government-private) concession arrangements, primary-level marketing of certain export crops may actually become more consolidated, while that of non-concession crops, including food crops, becomes more competitive.

(iii) Provincial-level wholesalers and retailers vary in size and range of activities. Wholesalers play the dual function of bringing consumer goods into districts and purchasing goods for resale, principally in provincial capitals. Wholesalers could serve the same function for agricultural inputs (seeds, tools and fertilizers) and for investment goods (cement, small mills, bicycles), although at present they seldom do so. As is discussed below in the constraints analysis, the Government has followed a policy of naming one authorized wholesaler per district for controlled consumer goods. Wholesalers have tended to honor the Government's district level divisions (except for, say, cashew areas in Nampula). This has generally made district traders dependent on a single wholesaler for supplies and reinforced the wholesaler's position as the single buyer for most agricultural commodities.

(iv) Transporters provide services to traders, farmers, or government agencies. Transporters may carry goods on their own account, but usually only on a backhaul or in addition to the goods carried for their clients. Transport agents range from those whose single 20-year-old truck may be operational only half the time, all the way up to enterprises with fleets of a dozen or more vehicles. Transporters may be very local, serving only a few districts with small (three-ton) trucks, or long-haul operators with 20-ton trailer rigs. In Nampula and Cabo Delgado, private sector transporters have established associations to share security and maintenance costs. Overall, such associations are positive indicators of private transport activity. Nonetheless, the concerns of established transporters may not always be conducive to increased competition; in a situation where trucks are in short supply, association members may begin to expect preferred access or simply be better placed to mobilize cash or credit for vehicles or repair parts, thereby limiting opportunities for new entrants. Informed sources indicate that a number of small or medium enterprises are ready to begin transport services if a single truck can be acquired and if the tariff structure is revised to permit such investments. Private transporters at present depend heavily on government or donor-financed contracts, particularly for deliverly of emergency relief goods.

(v) Small-scale market trade occurs both in established retail shops and at public markets and parallel street markets. Shops are likely to be family operations in towns, although some mobile retail shops ("tents") are reported to exist in more rural areas in some districts. Stallholders in the markets are typically (perhaps 95 percent) women in the South;* there is a predominance of men in the muslim North. Commodities are sold in small quantities, since most clients of these markets buy daily to satisfy immediate needs. The stallholders in urban markets generally do not sell their own produce, but buy from wholesalers or from producers. A recent study of maize marketing in selected districts* described an "explosive growth" in this type of operation due to: limited consumer income which requires them to buy in small quantities; employment for unskilled and otherwise unemployed or underemployed (including landless) persons; supplemental income for the vendor's family; and apparent government tolerance of informal operations. As private marketing channels develop in secondary towns, these same factors have contributed to the creation of similar local markets. The small investment necessary to start such an operation suggests that this end of the marketing chain, like the informal primary-level end, is where numerous new entrants into marketing are likely to appear.

The marketing chain for maize merits particular comment because of the extreme inefficiencies and price distortions that existed until price reforms were announced in June 1990. Private traders typically bought maize from family farmers and sold it to private wholesalers, generally in partial repayment of credit on consumer goods. Wholesalers sold it to Agricom district warehouses at the official wholesale price (154 Mt/kg in 1989/90). In the northern provinces, Agricom then typically contracted with private transporters to move it on its behalf to provincial capitals or other large cities. At such points wholesalers could buy maize from Agricom for onward sale at less than the district level selling price (151 Mt/kg). Private retailers completed the marketing chain with end sales to consumers. Although the private sector was dominant in the marketing chain, previously prevailing pricing policies distorted any sense of standard commercial marketing practices. Current pricing policy, developed in conjunction with USAID as part of the dialogue leading to this PAAD Supplement, is discussed in Section III-C.

As Mozambique begins to overcome some of the constraints to agricultural production, there are clear signs of a resurgence of marketing activity and of significant private sector participation in that recovery. Private sector marketing agents, to the extent that they are emerging, appear to be responsive to market forces and successful in bypassing many of the government's interventions. Private sector activity in fruit and vegetable marketing increased

*May 1990 Maize Marketing System Appraisal (USAID).

dramatically following a 1985 liberalization of prices.* What is even more astonishing although not quantified is the immediate private marketing response observed in areas newly accessible due to security improvements: traders go into such areas along with the very first emergency assistance convoys.** Such quick response indicates traders exist, are poised to work, and are willing to undertake considerable risks to buy and sell. However, the networks as they now exist are uncompetitive (since the numbers of operators at all levels are still small), vastly inefficient, and subject to numerous distortions.

C. Analysis of Constraints and Disincentives

Constraints to an improved domestic marketing structure for Mozambique fall into two broad categories. The first category of constraints consists of agriculture-related policy controls that the government has instituted to meet its consumption and production objectives. Two distinguishable sub-categories of such constraints are price controls and trade controls, with the need for the latter primarily occasioned by the institution of the former. The second broad category of constraints is of physical and systemic deficiencies, comprising three sub-categories: (i) infrastructure deficiencies, such as poor roads (including feeder roads) and bridges; (ii) capital deficiencies, such as rolling stock, trucks and other vehicles, boats, and spare parts for all these; and (iii) deficiencies in agriculture support systems, such as credit.

The insecurity situation in the countryside might be seen as a third broad category of constraint, although from an economic perspective it is more properly a factor that seriously exacerbates an already constraint-laden rural income environment. The insecurity situation has been used as a rationale for continuing with many marketing controls, and in some cases may have occasioned their original imposition, even though these controls were integral elements of the socialist economic and development strategy pursued by the government prior to 1987. Insecurity *per se* will not be discussed as a constraint; its constraining influence on Mozambique's economic recovery and its relevance to the USAID strategy in Mozambique are discussed in the Mission's March 1990 Country Program Strategic Plan.

*See the 1988 World Bank Agricultural Sector Survey.

**An important additional actor that enters the picture at this stage is the military. In most areas of the country outside major towns, due to the security situation cargo is usually transported in convoys guarded by the military. Estimates of the level of military participation in a convoy are roughly twenty percent. The military furnishes the troops and ammunition; the traders and transporters must furnish transport and pay salary and food costs. The necessity for convoys imposes other costs on transporters, such as waiting time while the convoys are consolidated.

1. Physical and Systemic Constraints

The physical and systemic deficiencies that constrain market development in Mozambique are linked in several ways with the policy environment. As discussed further below, policy reforms can have a significant impact on marketing activities, but the effects may be partial or temporary if physical constraints are not eventually addressed. Thus, although the focus of the PSSP is policy reform, an appreciation of the extent of these other constraints is critical to analysis of the policy elements. The following brief discussion outlines the key problems and refers to more detailed sources of information.

a. Infrastructure Constraints

Mozambique's road infrastructure has deteriorated since independence, and particularly since insurgency activities intensified in 1980, due to lack of maintenance. Roads of all classes are very bad, including highways and rural feeder roads. Responsibility is divided between the central Ministry of Transport and Communications for major highways and local (provincial and district) governments for secondary roads, tertiary roads, and feeder roads. As is usually the case in foreign-exchange-poor developing countries which are in addition experiencing large budget deficits, road infrastructure has been ignored. The insecurity situation has exacerbated the usual problems, as the insurgents destroy roads and bridges in many parts of the country. Given the risks involved, it is likely that even with increases in allowable transport tariffs many private traders or transporters would still be reluctant to take vehicles on many roads.

Although donor agencies have exhibited considerable interest to date in assisting with the rehabilitation of rail and port facilities, which are major foreign exchange earners for Mozambique and critical to macroeconomic recovery, interest in the road network is only starting to emerge. In part this has been due to the inability of the government to provide the donors with a solid, integrated proposal based on a realistic strategy. An IBRD Transport Sector Review*, currently in draft, will help the government develop such a strategy and permit donors to consider assistance in this sector within the larger GOM-IBRD-IMF Policy Framework Paper. In the meantime, some assistance on road infrastructure has begun by agencies such as the IBRD, the ILO, UNDP, NGOs/PVOs, and the EEC (through local currency generations under its programs). As discussed in the original PAAD's local currency use plan, government budget support for road maintenance and repair is one of the designated priority areas for local currency counterpart funds generated through USAID's commodity import and commercial food aid programs.

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*World Bank, Mozambique Transport Sector Review, October 1989 (draft).

b. Capital Constraints

As a result of a combination of infrastructure deterioration and uneconomic government allocations of the limited foreign exchange available to cover Mozambique's massive import bill, capital stock in the road transport sector has severely declined. Very old vehicles are very commonly used (the average age in rural areas is over 20 years), and a significant number of vehicles potentially available to move agricultural surpluses, inputs, and consumer goods are out of commission due to unavailability of spare parts.

Recently, donor agencies have begun to provide increasing support for imports of vehicles and vehicle spare parts (although regretfully much of this assistance has been provided only to parastatal entities). In addition, spare parts for transport are among the first three categories of commodities eligible for the government's newly established system for non-administratively allocating foreign exchange.

Recent changes in import distribution have allowed the private sector to gain access to vehicles and spares, long available only to public sector fleets, but private sector demand for these products is still vastly in excess of supply. Overall, the additional transport capital requirements are daunting (see Annex E for a demand assessment for the areas targeted in this amendment). Informed sources indicate many private sector operators are ready to increase their fleets significantly in key production and transport corridors, even outside of major urban areas, even though the utility of new and rehabilitated vehicles will depend in large part upon improvement in the road system. In addition, smaller operators who have never had access to their own trucks reportedly would be quick to purchase if foreign exchange could be found and if local currency credit were available. For private transporters, investment in vehicles also will depend on rationalization and increases in the allowable transport tariffs (currently regulated and currently probably too low, although widely ignored; see discussion below). However, this constraint does not affect the retailers and wholesalers who are likely to be the immediate purchasers of most of any new or rehabilitated transport vehicles available in the near future.

A similarly dire situation exists at present in coastal shipping, which formerly provided an efficient and necessary complement to road transport, connecting coastal towns with each other and serving agricultural areas more easily reached by river than by road. The World Bank Transport Sector Review also discusses this subsector, and the government has recently appealed to some donors for assistance to coastal shipping.

c. Systemic Constraints

Although research, extension, and credit problems are systemic constraints to overall development of Mozambican agriculture, of the three only credit can be considered a constraint to the development of better marketing systems. Credit to producers has been analyzed in several sources and found to be insufficient; but the same degree of analysis has not been applied to marketing system credit constraints. On the supply side, however, even tighter controls exist for marketing and trade than for agriculture. Demand for credit appears to be high, but is tempered by greater liquidity among traders and transporters than is generally found among farmers.

As in the case of production credit, commercialization credit where available has historically gone primarily to the state (or "intervened"*) sector, rather than to the private sector; although the proportion available to the private sector has increased marginally in the past three years from a very low base. Availability of commercialization credit may become much more important as levels of marketed production increase. At present, most commercialization credit, at least below the level of provincial wholesalers, is private and informal.

Unmet demand for bank credit for major investments related to marketing, such as trucks or boats, already appears high. Under present economic and security conditions operators prefer to risk borrowed capital rather than their own and thus apparent demand for such credit may not perfectly reflect the resources already available to private marketing agents for these investments. As marketing activities increase over time, private sector demand for trucks and boats, as well as for other high-cost, long-amortization marketing investments such as storage facilities or permanent shops, will require credit.

Successive PFPs negotiated under the government's economic rehabilitation program have set strict ceilings on domestic credit. The PFP fiscal targets for 1990-92 include a net repayment by the government to the banking sector in order to release financial resources to the rest of the economy; the objective is to provide to the non-government sector the maximum amount of credit compatible with the PFP monetary targets. Thus, in coming years, credit availability may not increase much, but (along with other economic resources) will shift from the public sector to the private sector. Under the ESRP, the banking system can distribute available credit according to market signals; unfortunately, however, technical skills in the banking system are weak, and the banks' outreach is limited. These constraints must be addressed if credit recipient selection is to begin to be based upon sound banking principles.

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*Intervened enterprises were abandoned by the Portuguese at independence and taken over by the State. The state does legally own intervened enterprises.

USAID indirectly supports provision of credit to the private sector through our general support to the ESRP and through program-generated local currency counterpart funds. As described in the PSSP's local currency use plan, these enter the normal government budget, cover a sizeable portion of regular government expenditures, and thereby assist the government to reduce public dependence on bank credit. This reduction means more credit available within the ESRP ceiling for the private sector, including agriculture and agricultural marketing.

2. Policy Constraints to Market Development

Policy constraints to market development, inhibiting as they do the PSSP objective of improving incentives for increasing production and income in the private agricultural sector, are the primary focus of this proposed amendment to the PSSP. Two categories of policy constraints have been identified: administrative trade controls and price controls.

a. Administrative Trade Controls

Many administrative controls exist, whether by law, regulation, or tradition, which undermine Mozambique's efforts to invigorate private marketing in the agriculture sector. Enforcement of controls may be sketchy, highly dependent on personal attitudes and example set by key authorities at provincial and local levels; but to the extent that they are grounded in explicit government policy as expressed in law and related regulations, these administrative controls limit private sector response to market forces. Three such controls are particularly striking: (i) barriers to movement of commodities between districts within a province or between provinces; (ii) designation of exclusive trading rights in specific districts and commodities; and (iii) licensing requirements for traders and transporters.

i. Geographic Trade Restrictions

The National Commission for Salaries and Prices annually publishes prices for goods still subject to controls. These announcements also specify that government authorities at provincial and district levels must regulate the flow of domestic foodstuffs from their areas in accordance with production targets. The purpose of this regulation is to ensure that local officials can control stocks, with the objective of ensuring availability of food for local populations. Because these restrictions require an explicit determination that sufficient local stocks exist before a trader or transporter can legally move produce out of an area, they provide an opportunity for officials to exercise discretionary control on marketing -- who can act, when, and where -- and thus provide an opportunity for rent-seeking behavior.

Decisions on permitting movement of commodities out of districts or provinces are even less likely to address social concerns because information on production and needs, even at quite local levels, is scanty and local authorities have little, if any training, in food management. Recognized surpluses, as they occur, are not likely to move quickly or efficiently. In practice, these controls have resulted in excess supplies in some areas deteriorating due to long or poor storage conditions, while neighboring districts have suffered acute shortages.

In the current security situation, local authorities are reluctant to permit a surplus to move out of the district, fearing that in coming months the district may be cut off from sources of supply. Even in a normalized security situation, local carry-over stocks from year to year have a role in ensuring food security, since highly variable production conditions (weather or pests) may lose an entire harvest. Such stocks are routinely maintained (generally by Agricom); but there is no provision made for the deterioration of the stocks or for turning them over by selling them off at prices that differ from the controlled prices. Furthermore, it is only in the past year, and on an ad hoc basis, that efforts have been made to actually utilize existing Agricom stocks to meet emergency food needs. Thus, losses due to these controls carry both an overall economic cost and a social cost for Mozambique.

Private sector operators are unlikely to undertake the risk of maintaining stocks under these conditions. Their willingness to enter the market at all or to expand their activities in response to production increases is constrained because of the uncertainty that they will be able to respond to perceived profits and risks. Certainly, inter-district or inter-provincial movement of commodities by private operators does occur; but because it is "illegal," such movement is informal and costly, perhaps providing significant individual benefits but few benefits to the economy. This situation provides an opportunity for quickly increasing the efficient and economic movement (including non-movement, i.e., stocking) of food crops by the private sector within and between districts and provinces, if restrictions are lifted to permit market forces rather than administrators to determine movements.

ii. Designated Wholesalers

The practice of designating at provincial level a single wholesaler for each district dates from colonial times.* Its purpose was to guarantee that government-supplied and controlled consumer necessities were delivered equitably to all districts in accordance with a centrally determined plan. The array of goods provided in this way has varied over the years; in recent years the list of still-controlled goods has been much reduced, with the key items being soap, sugar, cooking oil, and kerosene. Because of continuing overall scarcities, these high-demand products are provided in quantities insufficient for any district's needs.

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*This practice was actually a law of the Portuguese colonial administration that was incorporated into Mozambican law.

A wholesaler can have only one designated district, and it must be his "home" (origin, not necessarily residence) district. The wholesaler typically delivers the controlled goods along with a range of non-controlled consumer goods (and, rarely, agricultural inputs) to retail traders in the district in exchange for the area's agricultural surplus. Because the controlled goods are those basic consumables in general demand and critically short supply, and because only the designated wholesalers are legally permitted to bring these goods into their assigned districts, this practice effectively restricts the development of competitive marketing activity. Potential competitors desiring to deal even in non-controlled commodities at the district wholesale level, or those interested in wholesale buying of surplus agricultural production, will seldom find trading partners, since district retailers must barter the local surplus production to obtain the controlled goods from the designated wholesalers. Clearly the designated wholesaler is placed in a monopolistic/monopsonistic position with significant advantages over local retailers and producers.

While this practice might bring wholesalers begging for the right to a desirable district, in other cases, due to remoteness, poor road conditions, insecurity, undependable agricultural surpluses, or sparse population, the provincial government may have to exert considerable influence to encourage a wholesaler to take on a district. There is anecdotal evidence that, for example, a trader operating in one area may be threatened with the loss of license unless s/he takes on the official wholesalership for a remote or otherwise unlucrative district.

Recent information, confirmed during field visits and discussions with provincial authorities, indicates that some localized competition in district wholesaling is occurring, and in some districts more than one wholesaler may now be designated. There are potential benefits of these informal and localized changes, but even in these cases the need to be "designated" at all continues to provide an occasion for rent-seeking behavior and favoritism.

iii. Licensing

Licensing of traders and transporters is required at all levels, and usually specifically limits the operator's activities in terms of goods traded or areas served. Trader licences are issued by the Ministry of Commerce; those for transport enterprises by the Ministry of Transport and Communications. Application and enforcement of the licensing regulations are variable.

Interviews during recent field visits indicated that in fact larger operators or those based in the provincial capitals and applying to operate at provincial level do not find it difficult to obtain licenses. However, traders and transporters also reported, and provincial Ministry officials agreed, that bureaucratic problems exist in trying to obtain district-level licenses. Such licenses are likely to be the type sought by many new entrants into the private sector marketing network, who would probably begin operations with highly localized primary-level trading. There are reports that sometimes low-level traders are given a "letter" from the district authorities which is intended to provide provisional permission to trade while the license application is being reviewed.

Because of the wide variations and decentralized authorities in enforcing licensing regulations, it is not known to what extent these regulations and practices actually discourage market participation, especially at the primary level. Even where enforcement is not rigorous, however, the existence of the regulations still provides a potential disincentive to potential private sector operators as it provides an opportunity for rent-seeking behaviour by authorities. One recent marketing study,* unable to confirm negative effects of the licensing regulations and procedures, nonetheless urged that any attempt to improve marketing channels should ensure that licensing did not unduly restrict entry.

b. Price Controls

The price policies put in place by the government were designed to protect the consumer of foodstuffs, in the first instance at the explicit expense of the producer and then, when marketed production not surprisingly fell off, at the expense of intermediaries as production price incentives were improved in relation to consumer prices. Recent increases in producer prices have been clearly intended to provide additional incentives to increase marketed surpluses, given the country's high dependence on cereal imports. Currently, both production and consumption prices are officially fully protected only for rice; producers of the crops under the minimum pricing system are theoretically still protected; and fixed prices for basic foodstuffs still theoretically protect consumers. The poorly developed market systems existing in many areas suggest the need to retain some type of protection against monopsonistic practices. On the other hand, the counter effectiveness of controls utilized to date, as well as the govenment's limited capacity to administer an effective control system, suggest faster movement toward a market economy while restricting government regulations to functions it can usefully perform.

*"Market Intervention and Price Policies for Agricultural Marketing in Mozambique," Stockholm Group for Development Studies, October 1989 (draft).

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Despite the fact that the government has recently increasingly deregulated prices in the economy, and that this trend is likely to continue, several noteworthy aspects of the pricing system still represent potential constraints to the healthy development of Mozambique's domestic marketing networks. We have identified four such constraints in particular:

- Established margins between various stages of the marketing process may be too narrow to encourage the private sector to compete with subsidized state marketing agents;
- Controlled transport tariffs may be too low to permit private traders (or transporters) to compete with their public sector counterparts;
- The pan-territorial nature of fixed prices discourages competition and indeed any private sector activity in remote or insecure areas; and
- Pan-temporal pricing at the producer and the wholesale level encourages producers to sell their crops as quickly after harvest as possible and wholesalers to sell stocks as quickly after acquisition as possible, usually to Agricom.

i. Inadequate Price Margins

There is strong evidence not only that price margins on maize and rice, between fixed producer prices, factory gate (mill) prices, and consumer prices, have been extremely low in the past, but also that, despite a more recent move to somewhat more realistic margins, they still remain depressed. Although at official exchange rates the prices are now more reflective of realistic transport and handling costs, this is less true when a more appropriate exchange rate is used. In a theoretical situation where the government might completely exclude the private sector from participating in marketing, the economic effect of excessively low margins would be primarily on the size of the government's subsidy of the parastatals involved. However, in the case of Mozambique today, with private traders involved (however scantily) at the primary and higher marketing levels, inadequate marketing margins either discourage private trade or leave no alternative to the creation of parallel markets. It is reported in some areas that actual farmgate prices on maize and rice are lower than the official fixed prices, as traders presumably pass the insufficiency of the fixed margins onto the producers. In other areas, producers are paid at (or even in excess of) the fixed producer price and consumers are charged much higher prices than the fixed consumer prices, again to compensate private traders for the real margins. It is also reported, in contrast, that actual farmgate prices for crops whose prices are not fixed (such as cashew) are often higher than the established floor prices since factory gate prices are high enough to allow for real margins.

ii. Understated Transport Tariffs

The government has long controlled the prices of all types of transport in Mozambique, and the bulk of transport in the country has been carried out by public transport companies or parastatals with own-account fleets. Established tariffs are commonly considered insufficient to meet the real costs of road transport. Small tariff increases have not reflected the large import content of transport costs, a depreciating metical, declining road conditions, and increasing security risks. Table 2 summarizes the World Bank's analysis of actual 1989 transport cost for a 10 ton Mercedes truck. The analysis assumes a 50 percent load on the return trip and the need for military escort. It clearly demonstrates that, under realistic assumptions, the official tariff in 1989 did not cover transport costs even with the best of road conditions. To the extent that tariffs continue to be fixed at unrealistic levels and state transport firms continue to be given an advantage in access to foreign exchange and a subsidy in covering at least part of the transport cost differentials, it is difficult for private sector firms to compete with the public sector or indeed to invest at all in transport enterprises.

Table 2

1989 Vehicle Operating Costs and Tariffs

	Road Type				
	Rough Normal	Rough Paved 1	Paved 2	Earth 1	Earth 2
Actual Cost (Mt/TKm)	55.5	89.5	102.3	146.4	86.7
1989 Tariff	46.0	46.0	46.0	46.0	46.0
Shortfall (Mt/TKm)	9.5	43.5	56.3	100.4	40.7

*NOTES:

1. Financial costs for a Mercedes Benz model axle truck with 10 ton payload.
2. Normal: 45000 km annual utilization, 8 year service life, paved road good condition, 3.5 IRI, 1.5 positive grade, 1.5 negative grade, 320000 km total life, 45000 km/year, 2000 hours utilization/year, crew 230 mt/hr, mechanic 290 mt/hr, annual interest rate 24%, new tire price 49500 mt.
3. Rough: same as 2 but pavement roughness (IRI) at 12 (bad road).
4. Current: same as 3 but utilization 20556 km/year, 6 year service life, 150000 km/year, 1400 hours utilization/year.
5. Earth1: same as 2 but bad earth road, IRI=18, utilization 16000 km/year, 120000 km total life, 1400 hours/year.
6. Earth2: same as 5 but IRI=6 (acceptable road).

iii. Pan-Territorial Pricing

The margins at different levels of the agricultural distribution system are officially and centrally fixed without regard for differential costs of moving goods various distances under vastly different road and security conditions. As private trading begins to emerge throughout Mozambique, differential costs are reportedly being factored into prices actually paid and received. But with the state still the overwhelming participant in the marketing process, such differential costs continue to be covered by government subsidies, despite government attempts to price at an average level throughout the country. In fact, these subsidies are exaggerated because market influences ensure that private traders leave the higher-cost marketing functions to Agricom as the "buyer of last resort" while outpricing Agricom in lower-cost situations. To the extent that pan-territorial pricing is binding, it acts to discourage private sector competition with the more easily subsidized state marketing and transport firms. It further acts to inhibit normal market flows from surplus to deficit areas, since scarcities and abundances cannot be reflected in prices, thus reducing marketing activity and, eventually, if surpluses cannot be marketed, reducing production.

iv. Pan-Temporal Pricing

The pricing system does not permit variations to reflect the costs associated with maintaining stocks between harvests or changes in supply and demand over the course of the agricultural year. Such variations should be possible if market influences are to operate. Evidence suggests that intertemporal price differentials exist in areas where the private sector operates, with prices immediately following a harvest lower than they were immediately preceding the harvest. However, where producers sell to the state or to wholesale traders in monopsonistic or oligopsonistic situations, prices do not generally vary within the marketing year. In areas where pan-temporal pricing is enforced, trade at the primary and even wholesale levels is concentrated at the beginning of the marketing year because producers and private traders have no incentive to store the harvest.

D. Relative Importance of Constraints

The list of constraints to the development of markets in agricultural products is clearly daunting. Distinguishing the extent to which each of these constraints has influenced the dramatic gap between potential and actual marketing of agricultural surplus in Mozambique is an impossible task. An indicative attempt in the Swedish study suggests that over 50 percent of the shortfall is attributable to the security problems, while another 25-plus percent is attributed to poor agro-ecological conditions during the 1980s. The study mentions but does not differentiate among the remaining constraints, which are those discussed above. One approach might be to examine the supply response of marketed surplus over the past three years, in areas where security and climatic conditions have improved, in relation to the other identified constraints. Clearly, quantification problems for many of the constraints would preclude doing such a sensitivity analysis without the most heroic assumptions. Even though prices are themselves quantities and we might test the responsiveness of supply to prices alone, the data on marketed surplus include only that part of the marketed surplus that passes through public channels. Consequently, we have not attempted such an analysis.

Table 3 presents a ranking of the constraints and disincentives discussed above, according to the following criteria: immediate importance to improved private sector marketing; perceived priority in the government's eyes; other donor interest and support; susceptibility to improvement through A.I.D. non-project assistance; and the timeline for perceiving and measuring impact. The security constraint to marketing cannot be addressed by any A.I.D. program and therefore ranks at the bottom even though it ranks high on all other criteria.

The constraints ranked in Table 3 are elemental. Nearly all are amenable to relief through market-oriented policy reforms. Among the policy constraints identified, the illustrative ranking of the relative importance of the various controls is of limited utility. Certainly, the constraining effect of the whole web of controls is probably greater than the sum of individual restrictions. Faced with one or two of these constraints, some private sector operators would accept the risk; faced with the synergy of all of them, only a few operators are likely to be so courageous. Our goal is to remove the key policy-related constraints, and to act on all of them at the same time. Such liberalization can only improve the agricultural marketing systems, even if the other conditions that act as constraints continue. (See Annex C for an economic analysis that demonstrates that only a small productive response to marketing policy changes is required to justify the proposed $10 million investment under this PAAD Supplement.)

Table 3
Analysis of Constraints and Disincentives

(1) Category	(2) Constraint/Disincentive	(3) Immediate Importance to Mktg	(4) GOM Priority	(5) Other Donor Interest	(6) Susceptibility to Improvement thru NPA	(7) Timeline for Impact	(8) Overall Ranking
Policy	- Inadequate price margins	High	High	High	High	Short	1
Policy	- Restrictions on commodity movements	High	High	Medium	High	Short	2
Policy	- Understated transport tariffs	Medium	High	High	High	Short	3
Physical	- Capital stock	High	High	Medium	Medium	Short	4
Policy	- Pan-territorial pricing	High	Medium	Medium	High	Short	5
Policy	- Pan-temporal pricing	High	Medium	Medium	High	Short	6
Physical	- Road infrastructure	High	Medium	Medium	Medium	Medium	7
Policy	- Admin designation of exclusive district wholesalers	High	Low	Low	High	Short	8
Policy	- Licensing requirements for traders and transporters	Medium	Low	Low	High	Short	9
Physical	- Other infrastructure	Medium	Low	Medium	Low	Medium	10
Systemic	- Credit	Medium	Low	Low	Low	Medium	11
Security	- Risk to life and property	High	High	High	Nil	Short	12

III. Program Description

A. Purpose and Rationale

The purpose of the PSSP is to improve incentives for private sector agricultural production in order to enhance the private agricultural sector's production and income. To achieve this purpose, the PSSP addresses four fundamental constraints to private agricultural production -- prices, land access, availability of inputs, and availability of foreign exchange -- through policy reform to increase incentives to produce. When the PSSP was developed, the Mission identified marketing as another major constraint, but did not have sufficient knowledge of the sector to include it in the PSSP policy agenda.

This amendment to the PSSP contributes to the purpose through additional policy reforms intended to increase the responsiveness of supply among private sector agricultural producers, beyond what would have occurred under an unamended PSSP, by relaxing a number of important constraints to the development of markets in agricultural produce and related commodities. In doing this, the amendment will also benefit other private sector participants in the agricultural marketing chain, such as traders and transporters.

Policy reform progress under the PSSP has been fully satisfactory during the program's first year (Annex A contains 1990 Maputo cable 1336 which reports in detail on this progress). In the course of implementing the targeted reforms, within the context of its wider Economic and Social Rehabilitation Program, the government has itself recognized the importance of a functioning market system in providing incentives to produce. It also remains concerned about the potential impact of wrenching reforms in light of the nation's critical food insecurity and related social volatility. USAID support for the reforms discussed below, in combination with other food security related USAID activities, will encourage the government to implement reforms that will multiply the incentives to production already established under the ESRP.

B. The PSSP in Relation to Broader Reform Efforts

The process of economic policy reform undertaken by Mozambique is led by the Policy Framework Papers (PFP) negotiated each year between the government, the IMF, and the World Bank. Within this framework, USAID's policy dialogue and related support focus on food security issues in the broadest sense. Besides the production-oriented reforms of the PSSP, consumer-oriented reforms have been undertaken through P.L.480 Title II Section 206 agreements, which seek liberalization of consumer prices for food crops while maintaining and improving a targeted food safety net for poor urban households. As development and implementation of these reforms proceed in combination with those described below, both agricultural production patterns and consumer behavior should become increasingly market oriented, contributing over the longer term to a broad and productive agricultural base for Mozambique's economy.

USAID's approach to the process of policy reform in food and agriculture centers on an annually updated "Letter of Intent" from the government to USAID, which describes the government's priorities and objectives in the sector and specifies steps the government intends to take toward these objectives. The Letters of Intent are incorporated by reference into the PSSP Grant Agreement (and its amendments obligating incremental funding), and explicity provide the benchmarks for gauging progress on the policy reform agenda and workplan described in the PSS PAAD and as revised herein. The revised policy agenda is presented in the updated "Summary of Policy Objectives and Work Plan" matrix which follows (Figure 2).

The principal forum for monitoring progress on this agenda is the USAID - Government of Mozambique joint Working Group, established by the Minister of Finance, whose members include high level representatives from the Ministry of Agriculture, the Ministry of Commerce, the Ministry of Cooperation, the National Planning Commission, and the Ministry of Finance. The Working Group has met frequently since its inception to discuss progress on the policy agenda as well as constraints encountered and assistance needed to achieve the policy objectives.* In addition to the Working Group, direct dialogue with key Ministries continues, in particular with Finance on pricing questions and with Agriculture on state farm divestitures. The Minister of Finance, the key actor on all economic policies irrespective of the sector, continues to view USAID as a significant player in the formulation of food and agriculture policies. The evolution of this collaborative relationship on policy issues has contributed to an objective equal in importance to the policy reforms themselves -- namely, the full participation of Mozambican counterparts in the policy process and increased leadership on their part in directing further analysis and reform measures.

C. Specific Policy Agenda

Serious failures in the markets for agricultural production (inputs, outputs, and consumer goods) were the rationale for retaining and tightening a system of state-managed, state-controlled national distribution. Unfortunately, the very conditions which militated for retaining this system, i.e., the paucity of private traders and the rural insecurity which constrained their activities, in fact assured that the controlled system could not function as planned. The extensive array of restrictions on private marketing activities, some established under law and regulation since independence and others holdovers from the colonial period, have failed to prevent altogether the rebirth of private marketing agents and operations, yet have succeeded in effectively limiting their activities and institutionalizing the market imperfections the controls were created to address.

*The projectized portion of the PSSP (Private Sector Support Program Technical Assistance, 656-0218) contributes to the policy reform process through targeted applied research and related specialized assistance to inform the Working Group on the impact of planned policy reforms.

Figure 2

Mozambique Private Sector Support Program (656-0208)
Summary of Policy Objectives and Workplan
July 1990 Revision

POLICY AREAS	1989/90	1990/91	1991/92	POLICY INDICATORS	IMPACT INDICATORS	MEANS OF VERIFICATION
1. Agricultural Pricing Policy	OBJECTIVE: To maximize the liberalization of the agricultural pricing system and, for crops where full deregulation may not be presently feasible, institutionalize procedures for basing agricultural prices on world parity.			- Price changes and announcements.	- Production increases on family and commercial farms. - Farm income increases on family and commercial farms. - More consistent supply in markets throughout year.	- Production statistics by crop, province, farm type. - Estimated farm income calculated from production functions. - Selected market surveys.
a. Maize, beans, rice	- Establish parity producer prices; plan for floor price system. (Note: beans actually moved to floor price in 1989.)	- Move white maize and rice to parity-based producer floor price system; continue parity-based producer floor price for beans; assess impact and make recommendations.	- Adjust producer floor prices to maintain parity base.			
b. Cash crops	- Establish parity-based floor price system.	- Adjust floor prices to maintain parity base.	- Adjust floor prices to maintain parity base.			
c. Consumer prices		- Deregulate consumer price for white maize; assess impact; make recommendations re: beans and rice.	- Implement recommendations.			
Timing	- Before planting decisions.	- Before planting decisions.	- Before planting decisions.			
2. Divestiture of State Farms	OBJECTIVE: To develop and initiate the implementation of a divestiture program (including supporting policies for rational land redistribution, titling and registration) to redistribute state farms to commercial farmers.			- Declared policies on land redistribution including divestiture and titling procedures. - Development and promotion of divestiture program.	- Farms privatized. - Production increased on divested farms. - Farm income increased.	- Statistics on actual and planned divestitures. - Production statistics by crop in divestiture areas. - Estimates of farm income calculated from production functions and verified by sampling.
a. Planning and implementation	- Continue case-by-case divestitures of state farms. - Identify issues and policies to be addressed in divestiture program. - Complete terms of reference for additional tenure analyses and design of divestiture program.	- Implement analysis program on tenure issues. - Complete general divestiture program design. - Complete design of USAID-specific program for pilot divestitures.	- Implement USAID-specific pilot divestiture. - Continue divestitures in accordance with general program. - Refine divestiture policies, as needed, based on pilot divestiture.			
3. Private Ag. Sales and Service	OBJECTIVE: To demonstrate the effectiveness and viability of private sales and service networks for providing agricultural inputs to commercial and family farmers throughout the country.			- Percentage of private companies/traders participating in program. - Elimination of "credential system" for end users.	- Wider and better access to agricultural inputs. - Expansion of privatization.	- Statistics on numbers of private importers and dealers by input type and province. - Sampling of farmer attitudes toward supply networks. - Sampling of dealers to assess constraints to expansion.
a. For importers/distributors	- Continue private importation and distribution of all A.I.D. commodities; exemption for lubricants and limited spares.	- A.I.D. commodity imports fully private; plan to privatize ag-related public enterprises.	- Begin privatization plan.			
b. For end users	- Replace GRM administrative allocation system with direct private sales.	- Maintain.	- Maintain.			

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Figure 2

Mozambique Private Sector Support Program (656-0208)
Summary of Policy Objectives and Workplan
July 1990 Revision

POLICY AREAS	1989/90	1990/91	1991/92	POLICY INDICATORS	IMPACT INDICATORS	MEANS OF VERIFICATION
4. Access to Foreign Exchange	OBJECTIVE: To establish a process of testing foreign exchange allocation options that will increase the access of private entrepreneurs in the agricultural sector to foreign exchange and institutionalize market signals as an allocation mechanism.			- Implementation of FX allocation options agreed upon with donors.	- Increased access to foreign exchange at market-determined price.	- Survey of OGL users to determine private sector access.
a. Allocation mechanism	- Establish limited trial of OGL system.	- Evaluate effectiveness of OGL trial (with IBRD with USAID followup). - If trial is generally successful, modify and expand eligible sectors under OGL; otherwise formulate new options.	- Plan to extend OGL framework to larger portion of FX or test other allocation options.	- Range of eligible OGL sectors and volumes of FX increased.		- Trends in official and parallel exchange rates.
5. Private Marketing Channels	OBJECTIVE: To reduce restrictions on competitive private sector trade and transportation serving agricultural producers in Cabo Delgado, Nampula, and Zambezia provinces.			- Announcement and promotion of deregulations.	- Increased number of active traders and transporters.	- Sampling of traders/transporters/farmers.
a. Movement of commodities		- Rescind regulatory restrictions on inter-district and inter-provincial movement of agricultural commodities.	- Assess impact.		- More consistent supply of commodities in markets throughout the year.	- Market surveys.
b. Wholesaling		- Open district wholesaling opportunities to any licensed trader desiring to compete.	- Assess impact.		- Increased producer access to consumer goods and other "incentive" commodities.	- Sampling of farmers.
c. Licensing		- Analyze licensing requirements for private marketing agents at all levels to assess disincentive effects.	- Simplify licensing requirements based on analysis and encourage new competitors.		- Improved food balances between deficit and surplus production areas.	

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Government concerns over the pace and breadth of reform must be balanced against the cost and efficacy of government interventions. Attempts to "protect" farmers through the intervention of Agricom have generally had limited impact. Indeed, the Government has recognized Agricom's inability to operate effectively at a farmgate level, and has focused Agricom's function on wholesale trade, where it may prove an effective intermediary. On the other hand, regulations to control private trade due to concerns over monopsonistic markets may have only discouraged new participants that could promote competition. Many private wholesalers now benefit from state-enforced monopolies; although the prices at which such wholesalers trade are theoretically controlled, no government entity can monitor actual trade practices in rural areas. Conversely, producers and consumers must absorb the costs of inefficiencies and rents from lack of competition.

The reform program in this amendment to the Private Sector Support Program focuses on the policy constraints discussed in Section II-C. As discussed below, many options were considered to address these constraints. A key concern was to develop a reform package that minimized administrative demands on government, but instead allowed the market to set prices and determine production and marketing incentives to the extent practical.

The reforms are consolidated into two categories: pricing policies that determine financial incentives, and marketing regulations that affect the competitive environment. Pricing reforms will be implemented on a national basis, since it is clear that attempts to regulate prices have only spawned parallel markets with higher transaction costs that further restrict competition at a wholesale level. Marketing policy reforms focus on three provinces (Nampula, Cabo Delgado, and Zambezia) where production has significantly revived, trends suggest increased marketing activity, and current marketing policies will soon become binding constraints on trade unless they are changed. This phased approach on marketing reforms will permit the government, which is committed to additional market liberalizations under the PFP, to demonstrate the effectiveness of such incentives by focusing them on geographic areas where they are needed and can have a short-term impact.

1. Pricing Policy

a. Discussion

Government pricing policy has continued to be liberalized since the PSSP was developed. Additional changes in maize pricing were approved on May 30, 1990, and published in June. In keeping with agreements reached last year with USAID under the PSSP, the government has moved white maize to a parity-based producer floor price system, effective June 1990. The producer price for rice will continue to be fixed, but is to be revised based on import parity price considerations; this change is expected to be announced in September 1990, in time for planting decisions related to the 1991 harvest. Beans were moved to a parity-based producer floor price system in September 1989, a year before anticipated in the original PSS PAAD.

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Also in June 1990, the government fully deregulated the consumer price of white maize. This step had been under discussion with USAID in the course of negotiating the P.L.480 Title II Section 206 food aid program for 1990. (It is clear from qualifying statements in the PFP and from discussions that the government was reluctant to take this price reform step until it felt comfortable with the overall amount of food aid donated, a significant portion of which is to be provided under the 206 program.) For rice and for beans, consumer prices and, implicitly, marketing margins, remain fixed. However, the government sees the value in moving these prices to import parity, both to increase marketing incentives and to reduce subsidies that cannot be focused on the lowest income groups.

While there are strong arguments in favor of continuing the process of increasing price liberalization, there are reasons not to completely relax consumer price controls on all food commodities. Most importantly, subsidies on donated yellow maize continue to make significant quantities of a basic staple available to poor income groups, particularly in urban areas.* This subsidy has helped protect the food security of the urban poor, while at the same time enhancing the political viability of reforms that initially increase consumer prices during a transitional period intended to create a domestic supply response. With rice, the government's principal concern is that a few mills effectively control domestic supply. Full deregulation of consumer prices, they fear, would allow them to collect monopoly rents. The government's hesitance to deregulate the consumer price of beans is based on two concerns. First, it does not receive comparable quantities of beans as maize in food aid. Second, given the radical nature of its liberalization of domestically produced maize, it wishes to study the impact of this measure before deregulating the consumer price of beans. These are legitimate concerns, and have been incorporated into the proposed reform package.

The World Bank recently advanced other arguments against further liberalization of prices of staple crops beyond simply adjusting producer and consumer prices to international parity. At stake is whether the producer prices for maize and rice, the two staples remaining under the fixed price system, should be moved in 1990 to a producer floor price, with the government (through Agricom) acting as buyer of last resort. The Bank contends that unless minimum prices are established at a sufficiently high level, and unless there really is an active buyer of last resort, there will be disincentives to production; and if the minimum prices are set "high enough," they become effective fixed prices. They concluded that little would be gained by going to a minimum price system.

*This is true even though there appear to be leakages from designated commercial sales channels, conferring rents on individuals who participate in these leakages.

It is true, as the Bank argues, that minimum prices must be set appropriately, but the same is true for fixed prices. If prices remain fixed for staple crops, it is illegal for private traders to buy crops at any but the fixed price. However, if an appropriate minimum price is established, the problem of illegality is removed, and a private trader wishing to buy at a price exceeding the floor price may do so legally. If traders will not pay at least the floor price, then it is incumbent on the buyer of last resort to intervene. If Agricom cannot enforce floor prices, the resulting market clearing prices are not illegal, but a demonstration of financial constraints that keep the government from meeting price commitments. Indeed, field observations and surveys have indicated that producer prices are generally well below fixed prices in areas that are not easily accessible from towns or urban centers. A fixed price system for staples will not overcome this systemic problem.

A more exacting pricing policy question is whether the government should retain a producer floor price or a district-level wholesale floor price. The government could enforce minimum wholesale prices (generally paid at district centers) much more effectively than minimum producer prices. It has, however, opted to establish minimum producer prices in order to reduce the role of Agricom in the marketing chain. In practice, minimum producer prices will serve as reference points for farmers and traders to help compensative for limited market information in rural areas. With the government's decision to withdraw Agricom from primary-level buying, actual prices will be determined competitively. Should the government have established and announced minimum wholesale prices, it would have had to provide Agricom with the budget to enforce these prices in order to avoid destabilizing price signals to producers and traders. Recognizing that it does not have the budget to maintain a minimum wholesale price to do this on a national basis, and that Agricom does not have the administrative capacity to play this role, the government opted instead to limit its functions to announcing minimum producer prices.

Until minimum producer prices become the only administratively determined price in the production and marketing chain, attention must be given to (a) fixed transport tariffs and (b) the pan-territorial and pan-temporal nature of the still-fixed consumer prices for rice and beans, and the fixed producer price for rice. The government's options are two:

- implement an administratively complicated system whereby set tariffs and prices are location-specific and adjusted frequently enough to reflect changes in supply and demand according to season or economic distance from producer to consumer; or

- continue with the current simple administrative controls, despite their drawbacks, until it becomes viable to allow the market to determine wholesale and consumer prices.

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If prices remain controlled at more than one point in the marketing chain, the government will not be able to continue to ignore the problem of insufficient fixed (or indicative) margins between different levels of the controlled pricing system. Although transport tariffs were increased recently, indications are that these fixed margins are still insufficient, particularly for marketing agents to reach truly rural producers (See Section II-C). One option would be to move to a system of maximum transport tariffs, rather than fixed tariffs. To be implementable this would require state transport entities to be prepared to intervene if privately negotiated tariffs exceed a specified ceiling, particularly in areas where the security situation is problemmatic. It would also require building up the state transport sector, with detrimental long-term consequences that outweigh the short-term benefits.

Another approach to the problem of fixed but insufficient transport tariffs would be for the government to guarantee to cover extraordinary security-related costs of transport. Such a subsidy is compelling in principle, but difficult to implement. Ideally, it should not include the provision of direct tariff subsidies or supplements, but rather should be provided through the guarantee that the military will protect road traffic, either public or private; the subsidy would then be a component in the defense budget. Such a system would preclude the need for transporters and traders to negotiate with and reimburse the military for convoy protection; it would permit transport tariffs, and thus the handling margins, to be set or negotiated at more realistic, ordinary levels. Practically, it is unlikely that the government has the capacity to put such a system in place. Although budgeting procedures have improved, disbursement systems are imperfect, particularly the further one moves from Maputo. On the ground, there are not enough troops to perform designated functions, making it unlikely that traders would no longer have to negotiate with or subsidize the military.

Even if prices are controlled at only one point in the marketing system other than the producer level, the issue of transport tariffs (and other marketing costs) obviously is critical to any discussion of moving away from pan-territorial pricing. Any nationwide system of territorial differentials for margins based on transport cost disparities would clearly be difficult not only to enforce, but also to design. If controlled prices, even at one level of the marketing chain, were to continue into the future, the government would have to consider establishing a system of inter-territorial differentials based on realistic transport costs and other margin elements. This would be administratively complex and contrary to the end objectives of reducing the government's planning functions and increasing the role of the market in determining prices. Establishing a producer floor price system and allowing the market to determine all other trading prices is a more efficient approach to eliminating pan-territorial prices.

The issue of pan-temporal pricing is analogous to that of spatial pricing differentials. There are real costs in storing commodities that must be reflected in pricing policies in order to encourage the private sector to hold stocks and make investments that will preserve the quality of commodities. Again, the options to addressing this problem are to either establish differential seasonal prices or allow the market to reflect storage costs. As argued above, a market-based approach is obviously preferable.

The determination of when to allow consumer prices to reflect market forces, or indeed to reflect parity as closely as producer prices do already, is also an important food security issue. In moving toward more realistic margins in pricing policy over the past few years, the government has taken steps to move consumer prices closer to those implied by adjusted international parity prices. Currently, consumer prices remain fixed for inter alia yellow maize, rice, beans, and groundnuts. The eventual objective is to relax these controls for all products except yellow maize, which the donor community supplies explicitly for subsidized sales. With full consumer price deregulation, rice would de facto come out of the ration system (as did white maize in June 1990) and the basic food ration would consist of yellow maize alone. However, the government faces urban political and social forces which complicate the liberalization of the consumer price of rice; given the control held over supply by a few mills, there are also economic reasons to move cautiously on full deregulation.

In formulating the policy agenda proposed below, USAID has carefully considered the government's administrative capacity. The government has neither the information (on real production and marketing costs) nor the human resource capability to administratively determine prices, much less revise them in a timely way as circumstances change. Nor does it have, either centrally or provincially, the financial and institutional resources necessary to effectively enforce "last resort" approaches to controlled producer floor prices or transport tariff ceilings. Some of the policy alternatives (such as controlled but differential geographic or temporal pricing) would entail increased government analysis and intervention in establishing "appropriate" price components, neither of which the government has demonstrated a capacity to perform well. Given already strained government capacity in establishing and enforcing the existing, simple price controls (simple in that they are calculated and announced once a year, and apply for the whole country for the whole year), such additional burdens are clearly unrealistic. Although there are significant problems in the ways markets function at present in Mozambique, a more complex pricing policy which is badly administered certainly will act only to exacerbate them.

Our pricing reform approach is to combine the move to a producer-level floor price system for all food crops with complete liberalization (initially for white maize and later for beans and rice) of price controls at all subsequent transaction levels, including the consumer markets. Prices will vary at all marketing levels and across time and locations according to the real costs of production, transportation, and handling. The problem of what constitutes an adequate transport tariff will become a subject for negotiation between client and transporter, based on local conditions. Similarly, in situations of localized or seasonal glutand scarcity, market agents will be free to respond to the incentives and risks they face. This approach combines simplicity and ease of implementation with significant incentives to the agents linking agricultural producers and markets, and relieves the government of an onerous administrative burden.

b. Proposed reforms

Based on the foregoing discussion, the following benchmarks will indicate progress in support of expanded private sector marketing and will contribute to the PSSP's first policy objective, to maximize the liberalization of the agricultural pricing system:

- For white maize and rice, establish a parity-based producer floor price system and deregulate the consumer price of maize in 1990 (beans were moved to the producer floor price system in 1989);
- Assess the impact of pricing policy changes for all food crops; make recommendations for next steps in deregulating the consumer prices for rice and beans; and
- For cash crops, maintain parity-based producer floor price system as the only point of administrative price control.

c. Phasing

For 1990 the Government will establish IPP-based producer floor prices for rice, beans, white maize, and cash crops. All fixed producer prices will have been effectively eliminated. New floor prices will be announced before the end of September 1990, and widely promulgated in time for them to affect planting decisions for the 1990-91 agricultural cycle. (The liberalization of white maize at all other marketing levels, including the consumer price, was announced in June 1990.) Completion of the analysis of impact of the maize price changes, including recommendations for the timing and phasing of further price deregulation for beans and rice, will be a condition to disbursement of the third and final tranche of the Private Sector Support Program. The implementation of the recommendations for beans and rice will occur in 1991.

2. Private Marketing Channels

a. Discussion

Section II-C describes the key policy constraints hindering the emergence of strong competitive markets for both wholesale and retail trade of agricultural commodities. The reforms addressed under the PSSP focus on three policy areas central to creating a competitive environment that gives strong incentives to producers and traders and efficiently clears domestically produced goods: (i) free movement of commodities across geographic areas; (ii) unrestricted participation in wholesale trade; and (iii) efficient licensing of traders and transporters. Each of these policy issues is discussed further below.

As with the proposed pricing reforms, USAID has balanced the merits of eliminating some or all trade controls immediately, or phasing their removal over space and time. The difficulty with the former approach is that market conditions throughout the country vary vastly. In some areas where security conditions have improved, production and trade have picked up considerably; measures to encourage competition and increase incentives for private participation throughout the marketing chain are imperative to regenerating the economy. Economic activity continues to lag, however, in less secure areas; here, reform measures would have little impact on production and trade given that war conditions remain the binding constraint on production.

As was true with some elements of price controls, there are arguments for phased implementation of marketing reforms leading to nationwide implementation. Such a phased approach would have few negative drawbacks if key production areas are incorporated into the first phase of implementation. As indicated above, other factors will constrain production and marketing in insecure areas irrespective of the policy environment. Eventually, marketing reforms must be extended nationally to encourage economic growth as security conditions improve. For reasons discussed below, the areas selected to initiate marketing reforms under the PSSP are Cabo Delgado, Nampula, and Zambezia.

Restrictions on inter-provincial and inter-district trade were designed to allow authorities in a district or province to ensure availability of adequate food stocks for their constituencies (see Section II-C for a fuller discussion). Agricom was intended to control and release district-level stocks, particularly of maize. This policy was inadvertently reinforced by pan-temporal prices which eliminated the financial incentive to hold maize stocks, and by subsidies Agricom has paid to private transporters which made it preferable for wholesalers to sell their maize stocks to Agricom at the district level, allow Agricom to bear the cost of transport and deterioration, and then buy maize from Agricom at the provincial level at a low, subsidized price. Overall, the administrative and financial disincentives to trade reduced the likelihood that goods would move efficiently from surplus to deficit areas, while encouraging non-productive, rent-seeking behavior. The government eliminated these price distortions for maize in June 1990 when it made the producer floor price the only administratively determined price in the production and marketing chain. (Similar distortions did not exist for other commodities.)

With the removal of financial disincentives to holding private stocks and private trade of maize, it is essential to eliminate administrative restrictions on inter-provincial and inter-district trade. The government has controlled free movement of commodities through at least annual "Notices" in its national gazette, Boletim da Republica, which has binding regulatory status. The most recent such "Notice" was issued on April 4, 1990, officially announcing the current price controls in effect, and specifically reiterating that:

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(1) Surplus agricultural products can only be channeled to other provinces in accordance with targets established in the plan[*], and in unanticipated situations after the approval of the provincial governments; and

(2) There may be cases justifiably authorized, in which products from one province may be sold in another, principally to economize on transport, and for other reasons which justify [such sales].

The eventual objective is to withdraw these terms of the "Notices" entirely.

Concerns over open competition in wholesale trade stem from the previously described practice of designating a single wholesaler to supply key goods to each district, in effect giving this wholesaler preferential access to purchasing any commodities produced in the district. In some areas, local authorities reportedly have already begun to license more than one district wholesaler; this is certainly a positive development, and its expansion should be encouraged. Jettisoning the single-wholesaler rule for areas into which consumer goods are more readily delivered (given actual margins and security situation) will provide a fairly quick indication of the economic and social merits of such liberalization. The government's desire to guarantee at least one wholesaler carrying basic goods into more remote or less secure areas might be more effectively addressed through general incentives than through exclusive rights. Incentives to wholesalers to go into such areas should be designed in a manner that does not (i) discourage market entry of additional agents as they emerge, or (ii) in any way undermine the development of real competition at the lower levels of the marketing chain, or (iii) in general provide grounds for abusive rent-seeking activity.

On licensing policy, USAID seeks to ensure that controls do not unduly restrict entry into transport and trade activities. There exist good reasons for a government to establish licensing systems for many types of economic activity, at least above a certain level of value added; not least among these reasons is the government's legitimate desire to know whom to tax and by how much. In the case of primary retail trader licensing regulations, undue restrictions could lead to monopolistic and monopsonistic conditions and encourage rent-seeking activity. Based on interviews with wholesale traders and transporters, much of the restricting effect of the licensing procedures may be attributable to bureaucratic inefficiency, which of course is not likely to quickly change in response to a policy change. However, further analysis is required to confirm that the residual state-control orientation of administrators and bureaucrats does not exclude certain persons or enterprises from participating in marketing activities. Consideration must also be given to the need for policy changes which explicitly encourage new entrants and stronger competition.

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*This refers not to the "National Plan," but to a plan prepared annually by the Ministry of Commerce which still attempts to centrally determine domestic trade.

b. Proposed Reforms

The objective of the proposed marketing reforms is to reduce restrictions on competitive private sector trade and transportation serving agricultural producers in Cabo Delgado, Nampula, and Zambezia Provinces. Three elements are targeted:

Movement of Commodities:	Rescind regulatory restrictions on interdistrict and interprovincial movement of commodities by private sector traders and transporters in the three provinces.
Wholesaling:	Open district wholesale trade to any licensed trader desiring to compete.
Licensing:	Simplify licensing requirements to encourage participation in the market of any trader or transporter desiring to compete.

All of these changes will require substantial publicity at the provincial and district level to ensure fullest understanding of these new freedoms among government authorities, marketing agents, and producers.

c. Phasing

Analysis of available information on administrative restrictions to marketing suggests that the effects of these restrictions are impossible to separate; they compound each other as they contribute to impeding market development.* It appears most productive to consider geographically phased implementation of a set of reforms to lift key restrictions and encourage entry into the market of any trader or transporter desiring to compete.

The targeted reforms will be implemented, as indicated above, in Nampula, Cabo Delgado, and Zambezia provinces. In the first two provinces and in the northern parts of Zambezia, agricultural production is high and/or increasing rapidly, rural population density is high enough to entice trade and transport services, roads and bridges are in general adequate to make productive areas accessible (at least during key seasons), and private sector market activity has demonstrated potential for quick response to incentives.

*For example, a potential new trader who might be willing to meet all the licensing requirements may not be willing to absorb the rents involved in transporting commodities, and thus may decide to not enter the market at all; or a trader with one type of license might decide not to expand into other areas or other crops for the same reason.

For each of the proposed reforms, a two-step process is planned. I the case of inter-district and inter-provincial moving of commodities and expanding competition among wholesalers, announcement of the reforms will occur in 1990, and their implementation will be a condition to the disbursement of the final tranche of PSSP funding. The effects of these changes will be monitored and analyzed during the second year of the program, to inform government decisions on expanding these reforms to other provinces. In the case of the licensing requirements for traders and transporters, a rigorous analysis of the current regulations an their effects on competition in the targeted provinces will occur during the first year of the program, and specific reforms will be agreed upon and announced as a condition to disbursement of the second tranche of funding.

3. Expected Impact

The expected impact of these reforms is difficult to isolate from that of other reforms underway in Mozambique's quickly changing economy or from non-policy influences on production and trade, such as improved security or favorable weather. The general impact of both the pricing reforms and the lifting of restrictions on trade and transportation will be to amplify the opportunities for economic activity which are being created through major macroeconomic and political adjustments.

In addition, these reforms should lead to an absolute increase in the number of traders and transporters operating in the targeted provinces; an increased competitiveness among these traders and transporters to develop their markets, evidenced by new arrays of goods and more frequent, more client-oriented service; an extended reach of these operators into more remote areas, both to buy produce and to sell consumer goods and agricultural inputs; an increased range of marketing opportunities for producers as a result; an increase in household or privately held local stocks across the agricultural cycle, contributing to improved local food security; an improved food security balance among districts as surpluses find their way to deficit markets; and a decrease in the perceived need at district, provincial, or national level to maintain controls on marketing to protect either producers or consumers.

4. Conditionality

The $10 million of additional non-project assistance provided under this amendment will be obligated in a single amendment to the Grant Agreement in FY1990, which will incorporate an updated Letter of Intent, as described in Section II-B; this will set forth the government's objectives and specific intentions, including timing, to announce and otherwise implement the market-oriented policy reforms targeted in this amendment. The supplemental funding will be disbursed in two tranches in accordance with the conditions specified below.

a. First Tranche, Estimated September 1990, $4,000,000

i. Successful performance on FY1989/90 policy reform work plan under the PSSP. (Such performance is documented in Annex A.)

ii. Acceptance by USAID of a Letter of Intent which address the overall policy objectives and 1990/91 policy benchmarks described in this PAAD supplement. (This Letter of Intent has been submitted and is included as Annex F.)

b. Second Tranche, Estimated June 1991, $6,000,000

i. Successful performance on FY1990/91 policy reform work plan under the PSSP, including the market-oriented reforms specified in the Letter of Intent described above.

ii. Acceptance by USAID of an updated Letter of Intent summarizing reform progress to date, including the results of the analysis of trader and transporter licensing restrictions, and clearly stating the government's objectives and specific intentions, including timing, to announce and otherwise implement additional market-oriented policy reforms targeted in this amendment.

D. Monitoring and Evaluation

Monitoring of implementation and impact of the reforms targeted in this supplement will be incorporated into ongoing and planned monitoring and evaluation activities under the PSSP, which are described in the PAAD. These include: (i) CIP implementation and end-use monitoring; (ii) monitoring of progress on policy reform and the achievement of benchmarks, through continuing policy dialogue and activities of the joint Working Group as described in Section II-B; (iii) a PSSP mid-term evaluation, scheduled for March 1991, which will assess progress under the whole PSSP, including this supplement; (iv) regular monitoring of three private farms in each province participating in the PSSP, providing an indication of impact; and (v) applied research in direct support of the PSSP policy reform agenda, as described below.

It must be recognized that both the security situation and limited government statistical capacity severely constrain effective program evaluation. The GOM's data collection systems are weak or non-existent (for example, the Ministry of Agriculture does not collect information on production or on prices). The security situation and limited human and financial resources preclude systematic sampling; the result is little in-depth information or analysis of rural conditions, problems, and socio-economic patterns. Furthermore, what data are available are often gathered to satisfy a particular donor requirement. As a result, data are often not compatible and surveys are not repeated to allow time series analysis. There is also limited interchange of reports across and within ministries, so that information which exists is seldom widely available. Those who are in a position to make or influence policy decisions are not always cognizant of survey results. Thus, USAID's overall program monitoring strategy is to maximize the usefulness of data available from the government and other donors and facilitate limited sample surveys when appropriate.

Under the PSSP, USAID and the GOM are developing and implementing two applied research programs to provide information and analysis for the policy reform agenda. The first of these centers on food security issues facing rural households, and will be conducted collaboratively by Michigan State University and the Ministry of Agriculture. While necessarily limited in geographic scope, it will provide the first in-depth information on the food security status of rural households in Mozambique, farming and trade practices, responsiveness to policy changes, and constraints to agricultural development. The research will include targeted surveys of farmers and traders at key points in the agricultural cycle and production/marketing chain, analysis of the data gathered, and efforts to bring the results of the analysis to policy makers and others through seminars and working papers.

The second research program under the PSSP will be implemented by the Land Tenure Center at the University of Wisconsin, working collaboratively with the Ministry of Agriculture and other agencies concerned in issues of land tenure security. This research program has two principal elements: specific assistance in developing and implementing a pilot divestiture of state farm land to private and family farmers, and related guidance to the government based on experience in other countries; and more general assistance in identifying and addressing legal and other issues related to the availability and productive utilization of agricultural land, and land tenure security for farmers, particularly family or small private producers.

E. Disbursement Mechanism -- Commodity Import Program

As in the original PSSP, the supplemental non-project assistance provided through this amendment will be disbursed through a Commodity Import Program (CIP) mechanism. The supplemental resources will support agricultural transportation and marketing in the provinces of Zambezia, Nampula, and Cabo Delgado by providing trucks and related spare parts. Such assistance will directly address the "capital deficiencies" constraint discussed in Section II-C. Given the vast equipment requirements throughout the country, it was decided to focus assistance on specific geographic areas where it can have a significant and demonstrable impact. Importation and distribution will be strictly through the private sector.

1. Geographic Area

The provinces targeted for the commodities to be financed under this supplemental assistance are areas of signficant potential; all three have demonstrated increases in private sector participation in trade and marketing and together they make up the most agriculturally productive (historically, and again recently) part of the country. (See statistics in Annex D.) Some areas in these provinces, particularly in Nampula, have surplus production both in food and in cash crops, waiting to be transported to markets in high demand areas and to processing or export facilities. The brief description of each province provided below includes an estimate of its share of the supplemental $10 million. These relative shares may change in the course of program implementation, depending on an early 1991 demand assessment update.

a. Zambezia Province - $2,524,938

The main agricultural crops produced in this province are copra, vegetables, cashews, sunflowers, beans, rice, and maize. A marked increase in production during the 1989/90 production period was noted in the province due to the improved security situation. (The rapidity and extent of this recovery once security improved surprised all observers.) Output is marketed locally as well as in Quelimane (the provincial capital) and, when transport is available in the surplus-producing districts bordering Nampula province, in Nampula town. Cashew, a smallholder cash crop, has demonstrated particularly active production and marketing recovery as private traders move it to the processing plant at Angoche in Nampula province, immediately north of the producing districts in Zambezia. Financing under this amendment will provide trucks of 8- to 12-ton capacity.

b. Nampula Province - $5,209,875

The main agricultural crops produced in this province are maize, rice, sorghum, beans, groundnuts, sunflowers, cashews, cotton, and vegetables. Production during the 1989/90 cycle showed a sizeable surplus for many of these commodities. Output is marketed locally as well as in Nampula town and to other provinces through the major port in Nacala. Financing under the supplement will provide trucks of 8- to 25-ton capacity.

c. Cabo Delgado Province - $2,268,432

Cabo Delgado's main agricultural crops are maize, rice, sorghum, beans, groundnuts, sunflowers, cotton, and vegetables. Output is marketed locally as well as in Pemba (the provincial capital and a major port) and to other provinces through Pemba's port. This supplemental financing will provide trucks of 8- to 25- ton capacity.

2. Commodities to be Financed

a. Demand

As in the PSSP, the demand analysis summarized in Annex E, relies on the judgments of private sector importers and distributors, assuming prevailing exchange rates. Importers and distributors interested in participating in the program were asked to provide an indication of the demand for transport equipment in each of the participating provinces. The analyses received from the major importers indicate that immediate demand for the proposed commodities far exceeds the funding level of this supplement. The information provided in the importer/distributor demand assessments was augmented through discussions with private transporters and traders in these provinces as well as discussions with government officials (agriculture and commerce) at central and provincial levels.

b. Proposed Commodities

Table 4 provides the proposed breakdown for commodities financed under this supplement. This breakdown is subject to revision shoulc circumstances change over the course of CIP implementation. Each truck unit financed will include spare parts and accessories; costs for these are included in the following estimates.

Table 4
Commodity Import List

Type of Truck	Estimated No. of Units	Estimated Cost CIF	Probable Source/Origin
8 Ton	59	$ 3,227,300	AID Code 935
9 Ton	38	$ 2,302,800	AID Code 935
10 Ton	21	$ 1,814,400	AID Code 935
12 Ton	20	$ 1,980,000	AID Code 935
20 Ton	5	$ 378,000	AID Code 935
25 Ton	3	$ 300,600	AID Code 935
Total	146	$10,000,000	

c. DFA Procurement Plan

The following information is provided in accordance with the Special Procurement Policy Rules Governing the Development Fund for Africa, dated April 1, 1988 (Rules). Administrative Recommendation No. 2 of the Rules requires that DFA-financed procurement occur in the United States to the maximum extent practicable. However, past experience under the PSSP and predecessor CIPs, which financed 3-ton and 8-ton trucks for farmers, has demonstrated the need to procure the trucks and spare parts to be financed under this supplement from Code 935 countries. In Mozambique traffic moves on the left. At present, no U.S.-manufactured vehicles are marketed or serviced in Mozambique, as no U.S. firm produces trucks with steering wheels on the right side of the cabin. Spare parts and maintenance facilities for U.S. vehicles of any size or type are nonexistent in Mozambique. Thus,

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it is not appropriate to finance U.S.-manufactured trucks under this program, as they could not be adequately maintained.

As stated in Operational Recommendation No. 1 of the Rules, A.I.D.'s normal cargo preference requirements and procedures apply to this program as a matter of law. However, provided that cargo preference requirements are complied with, that Recommendation authorizes A.I.D. financing of delivery services on Code 935-flag ocean vessels.

In accordance with Operational Recommendation No. 2 of the Rules, air travel and transportation to and from the United Stated will be on U.S. certified carriers unless exceptions are made by USAID Mission Director. Little or no financing of air travel and transportation is foreseen for this supplement.

3. CIP Implementation Procedures

a. Allocation

Financing available under this supplement will be shared among private sector importers of trucks who are operating in the provinces of Cabo Delgado, Nampula, and Zambezia. Initial allocations of financing will take into consideration: (i) the importers' market analyses; (ii) the distributors' repair and after-sales service capabilities (financing will not be accorded to importers/distributors who do not have adequate after-sales service capabilities in the provinces to ensure maintenance and repair support for the equipment); and (iii) the number of importers participating in each province (when similar trucks can be provided by more than one importer/distributor in a province, USAID will encourage competition between brands as long as adequate after-sales service exists for each of the competing brands). Initial allocations will be reassessed after six months, and again every six months thereafter, and adjusted as necessary based on CIP implementation progress.

b. Procurement

All commodities financed will be procured under the terms of A.I.D. Regulation 1, "Rules and Procedures Applicable to Commodity Transactions" (A.I.D. Handbook 15, Appendix A), Section 201.23(e), governing procurement under special supplier-importer relationships. This section permits solicitation from only one supplier if the importer is the supplier's authorized dealer/distributor. As in the PSSP, equipment will be procured by eligible authorized dealer-distributors, so as to strengthen private sector dealers, encourage market competition, and allow the end-user to express brand preference. It is anticipated that proposed commodities will be procured by at least two different dealers.

c. Distribution

As in the PSSP, distribution will be based on market forces in that real private sector investment decisions will determine the resource allocations. Importers/dealers will sell these trucks and spare parts on an ordinary commercial basis to private sector transporters and traders in the target provinces. In order to permit access to the equipment for as many eligible clients as possible, a ceiling on the number of USAID-financed units a single enterprise can buy is desirable; initially, sales will be limited to three of any one type of truck per individual or enterprise, although USAID may lower this ceiling based on implementation progress and changes in demand.

d. Disbursement

Commodity imports will be financed by A.I.D. direct letters of commitment issued by the USAID/Mozambique Controller's Office following procedures utilized under the PSSP. Once a contract is approved by A.I.D. and the appropriate GOM Ministries, USAID prepares a "Concurrence of Award" letter for the Bank of Mozambique. The importer submits to the Bank of Mozambique an import license, approval of freight rate from MOCARGO (the GOM freight agent), and a letter advising the Bank of what financial arrangements have been made to guarantee the payment of the local currency equivalent of the transaction. The Bank confirms the importers financial arrangements, indicates the transaction number on A.I.D.'s letter of concurrence, and returns a copy to USAID's Commodity Management Office (CMO). The CMO then requests the Controller to issue the direct letter of commitment.

4. CIP Implementation Schedule

USAID expects to obligate these supplemental funds in July 1990 through an amendment to the Private Sector Support Program Grant Agreement with the GOM, to be based on this amendment to the PSS PAAD. In the meantime, the CMO is working with potential importers and distributors to prepare equipment specifications and quantities for each province. The tentative implementation plan is as follows:

As soon as the agreement amendment is signed USAID will issue allocation letters to the importers for the first disbursement of supplemental funds ($4 million of the $10 million total).

Four to six weeks later, proforma invoices should be submitted by the importers and dealers to USAID for review.

After USAID review and GOM concurrence, A.I.D. direct letters of commitment will be issued by the Controller (approximately the beginning of November 1990).

Depending on the commodity source, some imports will be arriving at the ports of entry beginning May 1991.

Six months after the initial allocations, the CMO will review progress on importer allocations and any unused funds will be re-allocated using the procedures stated above. This sequence will be repeated for any re-allocated funds as well as for disbursements in FY1991 of the remaining $6 million of supplemental funds (disbursement of these funds is dependent upon the conditionality described in Section III-C).

5. CIP Implementation Management and Monitoring

The Mission Commodity Management Office will manage the implementation of this supplement to the PSSP CIP. The CMO is directed by a Commodity Management Officer who is assisted by a CIP Monitor, a CIP End-Use/Field Monitor, an agricultural economist (part time), and a secretary. During implementation, the CMO performs on-going assessment of program-financed commodity use and demand. This assessment process is the basis for changes in the allocation of CIP resources among importers, types of commodities, and provinces, as described above and in the PSS PAAD.

The CIP Monitor is responsible for all aspects of financial accounting and reporting and assists with the allocation of funds and approval of transactions. In addition, the CIP Monitor oversees the importation, customs clearance, and distribution of the imports through constant communication with the importers, including periodic visits to verify that distribution has taken place in accordance with agreed-to procedures and that the commodities are being utilized by the intended clients. Due to the GOM's staffing constraints, the CIP Monitor also tracks and reports compliance with A.I.D. Cargo Preference requirements, normally a host country function.

The CIP End-Use/Field Monitor assesses the impact of CIP-financed commodities on agricultural production in target areas. With approval of this supplement, this responsibility will expand to include assessment of the impact of commodities on agricultural production and marketing. The End-Use/Field Monitor travels extensively to (i) monitor the extent to which A.I.D.-financed commodities are visible and properly utilized; (ii) monitor the extent to which participating importers and distributors are complying with CIP procedures; and (iii) monitor the extent to which program commodities are meeting demand.

F. Financial Plan

Supplemental resources provided through this amendment will be disbursed through non-project commodity import assistance under the Private Sector Support Program (656-0208). Funds will be obligated in a single amendment to the PSSP grant agreement, and disbursed in two tranches in accordance with the conditionality and procedures described in Section III-C. Table 5 updates the financial plan for the PSSP, including the resources to be provided under this supplement and, for illustrative purposes, a planned addition of $500,000 for technical assistance in FY1991.

Table 5
Revised Summary Financial Plan

Element	FY1989	FY1990	FY1991	Total
Non-Project Assistance				
Commodity Import Assistance				
- Original PSSP	13,550	12,500	13,000	39,050
- This Amendment	0	10,000	0	10,000
OGL Financing (Subject to AID/W Concurrence)	0	0	5,000	5,000
Subtotal	13,550	22,500	18,000	54,050
Project Assistance				
Technical Assistance and Research				
- Original PSSP	0	400	300	700
- Planned FY1991 Amendment	0	0	400	400
Implementation and Monitoring				
- Original PSSP	0	200	200	400
- Planned FY1991 Amendment	0	0	100	100
Evaluation and Audit	0	0	400	400
Subtotal		600	1,400	2,000
Total	13,550	23,100	19,400	56,050

G. Local Currency Use

Priorities, procedures and controls for the use of local currency generated by the commodity imports financed under this supplemental assistance are as described in the PSS PAAD. In connection with road rehabilitation efforts in support of rural marketing, the government is attempting to establish a special road maintenance fund; if this fund materializes, USAID may adjust the categories identified above to give a higher priority to road rehabilitation.

Annex A

Progress Report on Policy Reforms

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UNCLAS SECTION 01 OF * MAPUTO 01336

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AID/W FOR AFR/PD/SA AND AFR/SA
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E.O 12356: N/A
TAGS: ---
SUBJECT: MOZAMBIQUE PRIVATE SECTOR SUPPORT PROGRAM (656-0208/18): PROGRESS REPORT ON POLICY REFORM AGENDA

REF: (A) 89 STATE 216487; (B) MAPUTO 1159

1. THIS CABLE SUMMARIZES PROGRESS IN ACHIEVING THE 1989/90 POLICY BENCHMARKS UNDER THE MOZAMBIQUE PRIVATE SECTOR SUPPORT PROGRAM (PSSP). BASED ON THE GOM'S COMPLIANCE WITH THE BENCHMARKS, USAID IS PREPARED TO PROCEED WITH AUTHORIZATION AND OBLIGATION OF FY90 FUNDING INCREMENT FOR THE PSSP IN ACCORDANCE WITH THE AUGUST 1989 AA/AFR APPROVAL MEMORANDUM AND DELEGATION OF AUTHORITY. SEPTEL REQUESTS BUDGET ALLOWANCE AND PAAD AMENDMENT NUMBER IN ACCORDANCE WITH REF A GUIDANCE FOR NON-PROJECT ASSISTANCE UNDER THE DFA.

SUMMARY

2. USAID IS SATISFIED THAT SIGNIFICANT PROGRESS HAS BEEN MADE TOWARD ACHIEVING THE POLICY OBJECTIVES SET OUT IN THE PRIVATE SECTOR SUPPORT PAAD AND IN THE GOM'S LETTER OF INTENT, WHICH WAS INCORPORATED INTO THE PSSP GRANT AGREEMENT OF AUGUST 30, 1989. THE PAAD AND THE LETTER OF INTENT OUTLINED FOUR POLICY OBJECTIVES TO BE ACHIEVED UNDER THE PSSP WHICH RELATED TO LIBERALIZATION OF PRODUCER PRICES, STATE FARM DIVESTITURES, STRENGTHENING OF PRIVATE SALES AND SERVICE NETWORKS FOR AGRICULTURAL INPUTS, AND TESTING MARKET-BASED OPTIONS FOR FOREIGN EXCHANGE ALLOCATION. THE GOM'S LETTER OF INTENT DESCRIBES A WORK PLAN FOR 1989/90 THAT CONTRIBUTES TO ACHIEVING THESE OBJECTIVES. THIS WORK PLAN HAS BEEN COMPLETED AND SATISFIES THE BENCHMARKS SET FORTH IN THE PAAD FOR 1989/90. FURTHERMORE, POLICY DIALOGUE IN THE FOOD AND AGRICULTURE SECTOR HAS CONTINUED TO IMPROVE IN THE COURSE OF PURSUING THIS POLICY AGENDA. THE GOM HAS SUCCESSFULLY COMPLETED ITS 1987-1990 ECONOMIC REHABILITATION PROGRAM WITH THE WORLD BANK AND THE IMF.

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NEGOTIATIONS ARE IN PROCESS FOR A MORE EXACTING PROGRAM UNDER THE IMF'S ENHANCED STRUCTURAL ADJUSTMENT FACILITY. A PROCESS OF POLITICAL LIBERALIZATION INCLUDING CONSTITUTIONAL REFORM AND PLANNING FOR ELECTIONS IN 1991 IS PROCEEDING CONCURRENTLY.

BACKGROUND

3. THE PSSP WAS APPROVED AS A MULTIYEAR, DOLS 45.5 MILLION PROGRAM IN AUGUST 1989. AT THAT TIME THE FIRST TRANCHE OF NON-PROJECT ASSISTANCE (DOLS 13.55 MILLION) AND THE FULL TECHNICAL ASSISTANCE BUDGET (DOLS 1.5 MILLION) WERE AUTHORIZED. AUTHORITY WAS DELEGATED TO THE USAID/MOZAMBIQUE MISSION DIRECTOR TO AUTHORIZE INCREMENTAL OBLIGATIONS (EXCEPT FOR DISBURSEMENTS THROUGH AN OPEN GENERAL LICENSE SYSTEM). IN THE PAAD, USAID INDICATED THAT IT WOULD REPORT ON POLICY PROGRESS TO AID/W BEFORE AUTHORIZING INCREMENTAL TRANCHES OF ASSISTANCE. THIS CABLE CONSTITUTES THE MISSION'S PROGRESS REPORT.

4. THE PSSP'S PURPOSE IS TO IMPROVE INCENTIVES FOR PRIVATE SECTOR AGRICULTURAL PRODUCTION IN ORDER TO ENHANCE THE PRIVATE AGRICULTURAL SECTOR'S PRODUCTION AND INCOME. SPECIFIC POLICY OBJECTIVES OF THE PROGRAM, AS STATED IN THE PAAD'S "SUMMARY OF POLICY OBJECTIVES AND WORKPLAN" MATRIX, ARE:

- A. TO MAXIMIZE THE LIBERALIZATION OF THE PRODUCER PRICING SYSTEM AND, FOR CROPS WHERE FULL DEREGULATION MAY NOT BE PRESENTLY FEASIBLE, INSTITUTIONALIZE PROCEDURES FOR BASING AGRICULTURAL PRICES ON IMPORT/EXPORT PARITY;

- B. TO DEVELOP AND INITIATE THE IMPLEMENTATION OF AN ACTION PLAN (INCLUDING SUPPORTING POLICIES FOR RATIONAL LAND REDISTRIBUTION, TITLING, AND REGISTRATION) TO REDISTRIBUTE STATE FARMS TO COMMERCIAL AND FAMILY FARMERS;

- C. TO DEMONSTRATE THE EFFECTIVENESS AND VIABILITY OF PRIVATE SALES AND SERVICE NETWORKS FOR PROVIDING AGRICULTURAL INPUTS TO COMMERCIAL AND FAMILY FARMERS THROUGHOUT THE COUNTRY; AND

- D. TO ESTABLISH A PROCESS OF TESTING FOREIGN EXCHANGE ALLOCATION OPTIONS THAT WILL INCREASE THE ACCESS OF PRIVATE ENTREPRENEURS IN THE AGRICULTURAL SECTOR TO FOREIGN EXCHANGE AND INSTITUTIONALIZE MARKET SIGNALS AS AN ALLOCATION MECHANISM.

5. THE PSSP GRANT AGREEMENT INCORPORATED A LETTER OF INTENT FROM THE GOM STATING ITS OWN COMMITMENT TO THESE POLICY OBJECTIVES OVER THE COURSE OF THE PSSP AND DETAILING THE BENCHMARKS EXPECTED TO BE ACHIEVED DURING 1989/90. FOR REPORTING PURPOSES, THIS CABLE STATES, UNDER EACH OF THE FOUR POLICY AREAS, THE BENCHMARKS OUTLINED IN THE PAAD AND THE GOVERNMENT'S POLICY AS DESCRIBED IN THE LETTER OF INTENT. A DISCUSSION THEN FOLLOWS ON ACTUAL POLICY PERFORMANCE.

POLICY DIALOGUE

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6. USAID AND THE GOM ESTABLISHED A JOINT WORKING GROUP TO CONSIDER BOTH THE CONSUMER AND PRODUCER DIMENSIONS OF FOOD SECURITY AND TO MONITOR PROGRESS ON POLICY REFORMS AGREED TO UNDER BOTH THE PSSP AND THE MULTI-YEAR PL480 TITLE II SECTION 206 COMMERCIAL FOOD AID PROGRAM. THE WORKING GROUP REPORTS TO THE MINISTER OF FINANCE. IT IS CHAIRED BY THE NATIONAL DIRECTOR FOR AGRICULTURAL ECONOMICS, AND ITS MEMBERS ARE SENIOR OFFICIALS FROM THE MINISTRIES OF AGRICULTURE, COMMERCE, FINANCE, PLANNING, AND COOPERATION. A REPRESENTATIVE FROM THE UNIVERSITY OF EDUARDO MONDLANE ALSO PARTICIPATES. THE FIRST MEETING OF THE WORKING GROUP OCCURRED IN OCTOBER 1989, AND THE GROUP CONTINUES TO MEET REGULARLY. WORKING GROUP MEMBERS HAVE DISCUSSED PROGRESS ON THE POLICY AGENDA AS WELL AS CONSTRAINTS ENCOUNTERED AND ASSISTANCE NEEDED TO ACHIEVE THE POLICY OBJECTIVES. FROM AN INITIALLY RESERVED AND FORMAL FORUM, THE WORKING GROUP HAS EVOLVED INTO ONE WHICH PERMITS INCREASINGLY OPEN EXCHANGES OF INFORMATION AND OPINIONS.

7. IN ADDITION TO THE WORKING GROUP, DIRECT DIALOGUE WITH KEY MINISTRIES CONTINUES, IN PARTICULAR WITH FINANCE ON PRICING QUESTIONS AND WITH AGRICULTURE ON STATE FARM DIVESTITURES. THE MINISTER OF FINANCE, THE KEY ACTOR ON ALL ECONOMIC POLICIES IRRESPECTIVE OF THE SECTOR, CONTINUES TO VIEW USAID AS THE GOVERNMENT'S PRINCIPAL COUNTERPART IN THE FORMULATION OF FOOD AND AGRICULTURE POLICIES. HE HAS ALSO ASKED USAID TO PLAY A COORDINATING ROLE AMONG DONORS AND GOVERNMENT TO DEVELOP A COMMON STRATEGY FOR THE GENERATION, PROGRAMMING AND MANAGEMENT OF COUNTERPART FUNDS, IN EFFECT SEEKING USAID ASSISTANCE TO RATIONALIZE A PORTION OF THE BUDGET EQUAL TO TOTAL TAX REVENUES. THE EVOLUTION OF THIS COLLABORATIVE RELATIONSHIP ON POLICY ISSUES HAS CONTRIBUTED TO AN OBJECTIVE EQUAL IN IMPORTANCE TO THE POLICY REFORMS THEMSELVES -- NAMELY, THE FULL PARTICIPATION OF MOZAMBICAN COUNTERPARTS IN THE POLICY PROCESS AND INCREASED LEADERSHIP ON THEIR PART IN DIRECTING FURTHER

ANALYSIS AND REFORM MEASURES.

AGRICULTURAL PRODUCER PRICES

8. PAAD BENCHMARKS FOR 1989/90: (A) ESTABLISH PARITY-BASED PRODUCER PRICES FOR MAIZE, BEANS, AND RICE, AND PLAN FOR MOVING THESE TO A FLOOR PRICE SYSTEM IN 1990/91; AND (B) ESTABLISH A PARITY-BASED FLOOR PRICE SYSTEM FOR CASH CROPS.

9. THE GOM LETTER OF INTENT STATES: "...OUR STRATEGY IS TO UTILIZE FLOOR PRICES WITH EXCEPTIONS ON MAIZE, RICE AND SUGAR THAT GUARANTEE PRODUCERS A FAIR RETURN IN CASES WHERE THERE MAY BE ONLY ONE BUYER WHILE ENCOURAGING PRICE DIFFERENTIATION BASED ON QUALITY. WHEN CONDITIONS ARE CREATED THAT ALLOW A COMPETITIVE MARKET TO EXIST FLOOR PRICES MAY BE RECONSIDERED AND WHENEVER POSSIBLE (THE) MARKET SHOULD DETERMINE PRODUCER PRICES. ... FOR 1989/90, A FLOOR PRICE SYSTEM WILL BE MAINTAINED FOR CASH

CROPS (CASHEWS, COTTON, COPRA, SUNFLOWER, CASTOR BEANS AND GROUNDNUTS) AND FOR BEANS IN WHICH FLOOR PRICES ARE RELATED TO INTERNATIONAL BORDER PRICES. DUE TO THE LIMITED INFORMATION CURRENTLY AVAILABLE ON RURAL MARKETING OPTIONS AND TO ADDRESS FOOD SECURITY CONCERNS, MAIZE AND RICE WILL CONTINUE TO BE SOLD AT A FIXED PRODUCER PRICE RELATED TO INTERNATIONAL BORDER PRICES. ALL OF THE ABOVE PRICES WILL BE ANNOUNCED IN SEPTEMBER, 1989..." IN FACT, THE GOM MOVED BEANS FROM THE FIXED PRICE CATEGORY TO THE FLOOR PRICE SYSTEM IMMEDIATELY, RETAINING FIXED PRICES ONLY ON MAIZE AND RICE.

10. DISCUSSION OF PERFORMANCE: ON SEPTEMBER 18, 1989, THE NATIONAL COMMISSION FOR SALARIES AND PRICES ANNOUNCED NEW AGRICULTURAL PRODUCER PRICES IN ACCORDANCE WITH THE INTENTIONS OUTLINED ABOVE. AS PROMISED IN THE LETTER OF INTENT, FIXED PRODUCER PRICES WERE ANNOUNCED FOR MAIZE AND RICE, AND FLOOR PRICES WERE ESTABLISHED FOR THE REMAINING COMMODITIES CITED ABOVE. THE WORLD BANK ESTIMATED THE NEW PRICES FOR MAIZE AND RICE AT 10 PERCENT ABOVE IMPORT PARITY AT THE OFFICIAL EXCHANGE RATE. THE PREMIUM ON BORDER PARITY REFLECTS THE GOM'S DESIRE TO ACHIEVE GREATER SELF-SUFFICIENCY IN BASIC GRAINS. THE FLOOR PRICES ANNOUNCED FOR OTHER CROPS RANGED, ACCORDING TO THE WORLD BANK'S CALCULATIONS, FROM AN ESTIMATED 50 PERCENT OF BORDER PARITY FOR CASHEWS AND COPRA TO 80 PERCENT OF BORDER PARITY FOR BEANS.

11. AT PRESENT WE HAVE NO MEANS TO DISTINGUISH THE IMPACT OF THE NEW PRICES FROM THAT OF OTHER FACTORS (E.G. IMPROVED SECURITY IN SOME RURAL ZONES) WHICH HAVE AFFECTED PLANTING DECISIONS. NONETHELESS, SIGNIFICANT INCREASES IN PRODUCTION OF BOTH FOOD CROPS AND CASH CROPS ARE BEING REPORTED IN MANY AREAS WHERE HARVEST AND MARKETING ARE NOW UNDERWAY, AND WE BELIEVE THAT THE PRICE ANNOUNCEMENTS HAVE MADE A POSITIVE CONTRIBUTION TO THESE INCREASES. IN THE CONTEXT OF RESEARCH TO BE CONDUCTED WITH THE ASSISTANCE OF MICHIGAN STATE UNIVERSITY OVER THE NEXT 18 MONTHS, USAID AND THE GOM WILL MORE CLOSELY EVALUATE THE IMPACT OF THE PRICE POLICY CHANGES.

12. IT IS OF IMPORTANCE TO THE PRICE LIBERALIZATION PROCESS THAT THE GOVERNMENT HAS STATED ITS INTENTION TO PROCEED IMMEDIATELY WITH COMPLEMENTARY CONSUMER PRICE POLICY CHANGES WHICH ARE LIKELY TO HAVE A BIG IMPACT ON MARKETING INCENTIVES FOR MAIZE, THE PRINCIPAL CEREAL STAPLE FOR MOST MOZAMBICANS. IN MAY 1990 THE GOVERNMENT INTENDS TO INCREASE THE CONSUMER PRICE FOR DOMESTICALLY PRODUCED WHITE MAIZE TO IMPORT PARITY, THEREBY INCREASING MARKETING MARGINS BETWEEN THE FIXED PRODUCER PRICE AND THE END PRICE TO CONSUMERS. FOR THE 1990/91 AGRICULTURAL SEASON, THE GOVERNMENT INTENDS TO ESTABLISH A FLOOR PRICE FOR WHITE MAIZE AND ALLOW THE MARKET TO DETERMINE THE CONSUMER PRICE AS WELL AS THE MARGINS FOR TRANSPORTERS AND TRADERS. U.S. DONATED YELLOW MAIZE WILL CONTINUE TO BE SOLD AT A SUBSIDIZED PRICE (ESTIMATED AT 20 PERCENT BELOW IMPORT PARITY) AS A SAFETY NET MEASURE FOR LOW INCOME GROUPS DURING THE COURSE OF LIBERALIZATION AND

MARKET ADJUSTMENTS.

STATE FARM DIVESTITURES

13. PAAD BENCHMARKS FOR 1989/90: COMPLETE A NATIONAL STATE FARM DIVESTITURE PLAN AND A USAID-SPECIFIC IMPLEMENTATION SCHEDULE.

14. THE GOM LETTER OF INTENT STATES: "...OUR FEBRUARY 1989 PFP (POLICY FRAMEWORK PAPER) SPECIFIED THAT THE GOVERNMENT WILL PREPARE AN ACTION PLAN FOR EACH (STATE FARM) ENTERPRISE, SPELLING OUT FURTHER CHANGES OR REFORMS NECESSARY FOR FINANCIAL VIABILITY OR THE STEPS THAT WILL BE TAKEN TO REDISTRIBUTE THE LAND TO MORE EFFICIENT PRODUCERS. IN 1989/90, THE GOVERNMENT WILL COMPLETE THE ACTION PLAN SPECIFIED IN THE FEBRUARY 1989 PFP, INCLUDING DETAILS ON DIVESTITURE PROCEDURE, BENEFICIARY SELECTION AND TENURE SECURITY. DURING THE COURSE OF THE 1989/90 AGRICULTURAL YEAR, THE GOVERNMENT WILL ALSO DEVELOP WITH USAID A SCHEDULE FOR 1990/91 AND 1991/92 TO REDISTRIBUTE

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LANDS PREVIOUSLY USED BY SPECIFIC STATE FARMS IDENTIFIED IN THE PFP ACTION PLAN TO COMMERCIAL AND FAMILY FARMERS."

15. DISCUSSION OF PERFORMANCE: PROGRESS TOWARD THE DIVESTITURE BENCHMARK HAS OCCURRED, ALTHOUGH AN ACTION PLAN HAS NOT YET BEEN COMPLETED. PLANNING FOR STATE FARM RESTRUCTURING AND DIVESTITURE WAS UNDERTAKEN BY THE MINISTRY OF AGRICULTURE IN 1989, RESULTING IN PREPARATION OF A DRAFT ACTION PLAN FOR INTER-MINISTERIAL DISCUSSION, APPROVAL, AND IMPLEMENTATION. THE DRAFT PLAN WAS NOT APPROVED, BUT ITS PREPARATION FOCUSED ATTENTION ON THE LACK OF CLEAR POLICY IN REGARD TO AGRICULTURAL LAND USE IN GENERAL AND DIVESTITURES IN PARTICULAR. THE DEBATE RESULTED IN A REFERRAL OF THE ISSUE TO PRESIDENT CHISSANO FOR GUIDANCE, WHO RECONFIRMED THE OBJECTIVE OF DIVESTING OR RESTRUCTURING STATE FARMS, AND INSTRUCTED THE MINISTRY OF AGRICULTURE TO TAKE THE LEAD ROLE IN RESOLVING TECHNICAL PROBLEMS. THIS RESULTED IN THE MINISTRY OF AGRICULTURE DRAFTING GUIDANCE ON LAND USE AND DIVESTITURE PROCEDURES. WE HAVE BEEN INFORMED THAT AN INTER-MINISTERIAL APPROVAL OF SUCH A POLICY (BEING PREPARED BY THE MINISTRY OF AGRICULTURE) IS EXPECTED IN MAY.

16. FOR A NUMBER OF REASONS, FORMULATION OF A GENERAL POLICY ON LAND USE AND DIVESTITURE MAY, AT THIS STAGE IN THE EVOLUTION OF MOZAMBIQUE'S LAND LAWS, PROVE MORE PRACTICAL AND USEFUL THAN THE ORIGINALLY ANTICIPATED DIVESTITURE PLAN. FIRST, THE DIVESTITURE PLANNING PROCESS IS COMPLICATED BY THE FACT THAT BY LAW DIVESTITURE AUTHORITIES ARE DECENTRALIZED. GRANTS OF LONG-TERM LEASEHOLDS FOR AREAS UP TO 250HA ARE WITHIN THE DISCRETION OF PROVINCIAL GOVERNORS; LARGER TRACTS CAN BE GRANTED BY THE MINISTRY OF AGRICULTURE, AND AREAS OVER 500HA BY THE COUNCIL OF MINISTERS; AND CERTAIN SPECIALIZED GOVERNMENT OFFICES, SUCH AS THE SECRETARY OF STATE FOR COTTON, ALSO HAVE SOME AUTHORITIES. IT IS ALSO IMPORTANT TO NOTE THAT PLANNING AND SCHEDULING THE DIVESTITURE OF STATE FARM ASSETS IS DIFFICULT WHEN BUYERS MUST BE SOUGHT AND DEALS NEGOTIATED, WHICH IS THE SITUATION FOR MANY OF THESE ENTERPRISES. PRIVATE OPERATORS ARE UNDERSTANDABLY RELUCTANT TO ABSORB THE SUBSTANTIAL DEBTS AND BLOATED EMPLOYMENT ROLLS OF THE STATE FARM ENTERPRISES, FURTHER COMPLICATING SOME DIVESTITURE NEGOTIATIONS. IN ADDITION, THE NATIONAL DIRECTORATE OF GEOGRAPHY AND CADASTRE, WHICH IS REQUIRED BY LAW TO REGISTER LAND HOLDINGS, HAS BEEN SO FUNDAMENTALLY NEGLECTED SINCE INDEPENDENCE THAT IT CANNOT KEEP UP WITH THE SYSTEMATIC REGISTRATION RESPONSIBILITIES NECESSARY TO ORDERLY DIVESTITURES, PARTICULARLY THOSE WHICH WILL REDISTRIBUTE LARGE HOLDINGS TO SMALL FARMERS. FINALLY, NEW CONSTITUTIONAL PROVISIONS EXPECTED TO BE ENACTED THIS CALENDAR YEAR ARE CERTAIN TO RESULT IN SUBSTANTIAL OVERHAUL OF THE LAND LAW AND REGULATIONS UNDER WHICH DIVESTITURES OCCUR. (SEE REF B RE: GOM PROGRESS ON PRIVATE PROPERTY RIGHTS IN LAND.)

17. MANY OF THE COMPLICATIONS THAT COULD ARISE IN

DEVELOPING AND IMPLEMENTING A DIVESTITURE PLAN WERE RAISED BY AID/W DURING THE PAAD REVIEW AND LED TO MODIFICATION OF USAID'S OBJECTIVES IN THE PAAD TO FOCUS ON PLANNING AND POLICY DEVELOPMENT RATHER THAN THE ACTUAL DIVESTITURE OF STATE FARM LANDS. THE PROCESS OF DEVELOPING AN APPROPRIATE POLICY FRAMEWORK IS STILL ON TRACK. WHEN ONE TAKES INTO CONSIDERATION THE NEW CONSTITUTIONAL PROPOSALS FOR PRIVATE LAND OWNERSHIP, THE GOVERNMENT MAY IN FACT BE FURTHER AHEAD ON THE CREATION OF LAND MARKETS THAN COULD HAVE BEEN ANTICIPATED. WHILE IT REMAINS DIFFICULT TO EXTRACT DETAILS ON DIVESTITURE PLANNING AND IMPLEMENTATION, WE ARE SATISFIED WITH PROGRESS TO DATE FOR THREE REASONS:

- A. FIRST, IT IS CLEAR THAT THE GOM'S INTENTION TO RESTRUCTURE AND DIVEST STATE FARM HOLDINGS IS A SERIOUS ONE. DIVESTITURES OF STATE FARMS ARE OCCURRING TO PRIVATE AND MIXED (PRIVATE-GOM) VENTURES. SINCE 1987, THE NUMBER OF STATE FARMS HAS BEEN OFFICIALLY REDUCED FROM 150 TO 109, EITHER THROUGH PRIVATIZATION OR CLOSURE, REDUCING THE AREA UNDER STATE FARM CONTROL FROM 150,000HA TO 90,000HA. (WE BELIEVE THE ACTUAL NUMBER OF STATE FARMS IS, IN FACT, LOWER THAN THE OFFICIAL 109, WHICH

BEST AVAILABLE DOCUMENT

SUFFERS FROM DELAYS IN RECORDING PROVINCIAL LEVEL DIVESTITURES.) IN SOME CASES, WHAT IS BEING DIVESTED IS THE ENTERPRISE, INCLUDING EXCLUSIVE RIGHTS TO PURCHASE AND PROCESS CERTAIN CROPS IN A "CONCESSION" AREA, RATHER THAN THE AGRICULTURAL LAND, WHICH CONTINUES TO BE USED BY PRIVATE AND FAMILY FARMERS; THESE CASES INCLUDE PLANS FOR THE NEW VENTURES TO PROVIDE IMPROVED INPUTS, EXTENSION, AND MARKET SERVICES TO FARMERS IN THE AREA. IN OTHER CASES, PRIVATE APPLICANTS WHO EXPRESS INTEREST ARE BEING GRANTED LONG-TERM LEASEHOLDS TO PORTIONS OF STATE FARMS, USUALLY IN RETURN FOR PAYMENT OF LAND TAXES DUE. THERE ARE MANY ASPECTS OF THIS AD HOC APPROACH WHICH TROUBLE US. THERE ARE ALSO ELEMENTS OF THE DECENTRALIZED APPROACH WHICH ARE ATTRACTIVE AND SHOULD BE RETAINED. BUT THE FACT OF DIVESTITURE IS NOT IN DOUBT.

- B. SECOND, THE TECHNICAL STAFF OF THE MINISTRY OF AGRICULTURE ARE CLEARLY SEIZED WITH THE URGENCY OF CAREFULLY ADDRESSING THE COMPLEX QUESTIONS OF TENURE SECURITY WHICH HAVE BEEN RAISED IN CONNECTION WITH STATE FARM DIVESTITURE PLANNING, ESPECIALLY FOR FAMILY FARMERS WHO HAVE NEVER HAD ANY SECURITY THROUGH THE LAW. IN THIS CONNECTION, AN INITIAL REPORT ON TENURE SECURITY ISSUES AND OPTIONS, PREPARED BY THE LAND TENURE CENTER (LTC) AT THE UNIVERSITY OF WISCONSIN-MADISON, HAS RECEIVED WIDER THAN EXPECTED CIRCULATION. THE ISSUES THEREIN IDENTIFIED HAVE BEEN BROUGHT INTO SHARP FOCUS BY THE GOM'S SUBSEQUENT ANNOUNCEMENT OF DRAFT LANGUAGE FOR THE NEW NATIONAL CONSTITUTION, WHICH INCLUDES PROVISION FOR PRIVATE OWNERSHIP OF PRODUCTIVE ASSETS, SPECIFICALLY INCLUDING LAND.

- C. THE WORKING GROUP DESCRIBED ABOVE, AND OTHER GOM TECHNICAL STAFF INVOLVED IN DIVESTITURE PLANNING, HAVE SPECIFICALLY REQUESTED ADDITIONAL ASSISTANCE FROM LTC ON LAND AND DIVESTITURE ISSUES, WHICH WE ARE MOVING TO PROVIDE. USAID AND THE GOM ENVISAGE A TWO TRACK POLICY ANALYSIS AND IMPLEMENTATION PROGRAM WITH LTC. AT A BROAD POLICY LEVEL, USAID WILL FINANCE A SERIES OF SHORT-TERM CONSULTANCIES AND IN-COUNTRY SEMINARS BY LTC TO ADVISE THE GOVERNMENT ON TENURE SECURITY, DIVESTITURE AND A BROAD ARRAY OF LAND POLICY ISSUES THAT WILL FACTOR INTO THE CONSTITUTIONAL REVISION PROCESS, AS WELL AS ENHANCE THE VIABILITY OF INDIVIDUAL DIVESTITURES. TO HELP EFFECTUATE AND MONITOR THESE POLICIES, A LONG-TERM LTC ADVISOR WILL WORK WITH THE MINISTRY OF AGRICULTURE TO IMPLEMENT PILOT DIVESTITURE(S) AND FEED BACK LESSONS LEARNED INTO THE BROADER POLICY FRAMEWORK. BY THE END OF THE PROGRAM BEING FORMULATED WITH LTC, USAID ENVISAGES THAT THE GOM WILL HAVE DEVELOPED AN APPROPRIATE POLICY FRAMEWORK AND ACTION PLAN, AND HAVE EXPERIENCE IN TAKING SUCH POLICIES THROUGH TO IMPLEMENTATION.

18. IN SUM, THE GOM HAS UNDERTAKEN SERIOUS DIVESTITURE PLANNING, TREATING SUCH ISSUES AS LAND POLICY, TITLING AND REGISTRATION, AND BENEFICIARY SELECTION, AND USAID AND LTC ARE ASSISTING THE PROCESS. WHILE AN ACTION PLAN AND SCHEDULE FOR DIVESTITURES HAVE NOT BEEN APPROVED, WE

BELIEVE THAT A STATEMENT OF DIVESTITURE OBJECTIVES AND GUIDELINES, INCLUDING A PRIORITIZATION OF WHICH PROPERTIES ARE DIVESTED FIRST, WILL BE ISSUED TO PERMIT DECENTRALIZED DIVESTITURE TO PROCEED IN A MORE ORDERLY AND EQUITABLE FASHION GIVEN THE CONSTRAINTS NOTED.

PRIVATE NETWORKS FOR AGRICULTURAL INPUTS

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19. PAAD BENCHMARKS FOR 1989/90: (A) CONTINUE PRIVATE IMPORTATION AND DISTRIBUTION OF ALL A.I.D.-FINANCED COMMODITY IMPORTS (WITH EXEMPTION FOR LUBRICANTS AND LIMITED SPARES INTENDED TO MAINTAIN EQUIPMENT PROVIDED TO PARASTATALS UNDER PREDECESSOR CIPS); AND (B) REPLACE THE GOM'S SYSTEM OF ADMINISTRATIVE ALLOCATION OF A.I.D. COMMODITIES TO END-USE CLIENTS WITH SYSTEMATIZED DEMAND-DRIVEN DIRECT SALES TO PRIVATE DISTRIBUTORS FOR ON-SELLING TO THEIR CLIENTS.

20. THE GOM LETTER OF INTENT STATES: "THE GOVERNMENT WILL CONTINUE TO USE PRIVATE CHANNELS FOR IMPORTATION AND DISTRIBUTION OF USAID-FINANCED COMMODITIES IN ORDER TO

ASSURE MORE EFFICIENT ALLOCATION MECHANISMS, WITH ONE EXCEPTION IN 1989/90. WE REQUEST THAT FUNDS BE MADE AVAILABLE FOR SPARE PARTS FOR ITEMS FINANCED DURING THE INITIAL YEARS OF USAID'S COMMODITY IMPORT SUPPORT WHICH ARE HANDLED SOLELY BY PUBLIC ENTERPRISES." THE LETTER CONTINUES: "AS OF 1989/90 THE GOVERNMENT WILL NO LONGER MAKE ALLOCATIONS TO END USERS FOR USAID-FINANCED COMMODITIES. INSTEAD, IMPORTERS AND DISTRIBUTORS WITHIN EACH PROVINCE WILL BE FREE TO SELL AGRICULTURAL INPUTS IMPORTED UNDER THE PROGRAM WITHIN THE PROVINCE TO THOSE FARMERS WITH AN ESTABLISHED FARMING HISTORY WHO HAVE THE CAPACITY TO EARN AND PAY THE LOCAL CURRENCY COST OF THE INPUTS. ... THIS MEASURE, IN EFFECT, REPLACES THE ADMINISTRATIVE ALLOCATION TO END USERS...WITH A MARKET-BASED ALLOCATION SYSTEM."

21. DISCUSSION OF PROGRESS: PROGRESS ON THESE BENCHMARKS IS FULLY SATISFACTORY. AT PRESENT 99 PERCENT OF THE CIP IS BEING IMPLEMENTED THROUGH PRIVATE IMPORTERS AND DISTIBUTORS. MOREOVER, THE GOM'S LETTER OF INTENT DID INDEED MARK THE TERMINATION OF THE ADMINISTRATIVE ALLOCATION SYSTEM TO END USERS IN WHICH ONLY FARMERS WHO RECEIVED A "CREDENTIAL" FROM THE MINISTRY OF AGRICULTURE WERE AUTHORIZED TO PURCHASE CIP COMMODITIES. PIL NUMBER 3 DATED NOVEMBER 15, 1989, FORMALLY ESTABLISHED PROCEDURES TO PHASE OUT ADMINISTRATIVE ALLOCATIONS IN FAVOR OF A MARKET-BASED ALLOCATION SYSTEM. ELIGIBLE CLIENTS WERE LIMITED TO ESTABLISHED PRIVATE SECTOR FARMERS AND PRIVATE TRANSPORTERS INVOLVED IN AGRICULTURE-RELATED ACTIVITIES. USAID SUBSEQUENTLY EXECUTED A MEMORANDUM OF UNDERSTANDING WITH EACH PARTICIPATING DEALER/DISTRIBUTOR SPECIFYING REQUIREMENTS FOR ADVERTISING AND RECORD KEEPING.

22. THE GOM OPTED TO BEGIN IMPLEMENTING THE NEW MARKET-BASED SYSTEM IMMEDIATELY, APPLYING IT TO A SMALL BALANCE OF THE FY88 CIP AND TO THE FULL FY89 PROGRAM. A SMALL SHARE OF FY88 COMMODITIES WHICH DEALERS COULD NOT MANAGE TO SELL TO "CREDENTIALED" FARMERS MOVED IMMEDIATELY WHEN SALES WERE OPENED TO ALL PRIVATE FARMERS. DEALERS AND DISTRIBUTORS HAVE VOICED GREATER ENTHUSIASM ABOUT THE PROGRAM AND CITE REDUCED ADMINISTRATIVE BOTTLENECKS AND IMPROVED RELATIONS WITH POTENTIAL CLIENTS AS A RESULT OF BEING ABLE TO DEAL WITH ANY PROSPECTIVE BUYER WITH AVAILABLE FINANCING AND NOT JUST ADMINISTRATIVELY DESIGNATED FARMERS. WITH ALLOCATION DECISIONS BEING MADE IN THE MARKET PLACE, THE MINISTRY OF AGRICULTURE ITSELF ENCOUNTERS FEWER CONFLICTS WITH FARMERS, WHO PREVIOUSLY COMPLAINED ABOUT NOT RECEIVING CREDENTIALS. OVERALL, THE REFORM HAS BEEN AN IMPORTANT DEMONSTRATION OF HOW A COMPETITIVE MARKET CAN MAKE MORE EFFICIENT AND LESS COSTLY ALLOCATIONS OF RESOURCES THAN GOVERNMENT ADMINISTRATORS.

23. A STRENGTHENING OF THE PRIVATE SECTOR DISTRIBUTION NETWORK HAS ALSO BEEN NOTED. ESTABLISHED DEALERS AND DISTRIBUTORS ARE BECOMING MORE ACTIVE AND VISIBLE IN THE PROVINCES, OFFERING IMPROVED SERVICES AS THEY COMPETE FOR

CLIENTS. THIS HAS BEEN REINFORCED BY THE GOM'S INCREASED READINESS TO GRANT IMPORT LICENSES TO PRIVATE ENTERPRISES SEEKING TO IMPORT AND DISTRIBUTE AGRICULTURAL INPUTS. FOR EXAMPLE, THE NETWORK FOR SEED DISTRIBUTION IN THE PROVINCES, WHICH TO DATE HAS CONSISTED OF BASICALLY TWO OPERATORS (ONE PARASTATAL, ONE PRIVATE), IS BECOMING MORE DENSE -- ONE NEW ENTRANT INTO THE SECTOR, AND REPORTS OF OTHER NEW ENTERPRISES BEING ORGANIZED. WITH COMPETITION INCREASING, IMPROVEMENTS IN CHOICE, SERVICE, AND PRICE TO THE FARMERS SHOULD RESULT. IN ANOTHER INSTANCE, REPRESENTATIVES OF AN ASSOCIATION OF PRIVATE COOPERATIVES ARE INTERESTED IN ASSESSING DEMAND AMONG MEMBERS FOR SOME OF THE ELIGIBLE COMMODITIES, AND IMPORTING DIRECTLY FOR SALE TO THESE MEMBERS. ONE EFFECT SHOULD BE CONTINUING IMPROVEMENT IN THE REACH OF INPUT DISTRIBUTION NETWORKS TO SMALLER SCALE FARMERS WHO DID NOT BENEFIT UNDER THE SYSTEM OF RESTRICTED IMPORT LICENSES AND CREDENTIALS.

ACCESS TO FOREIGN EXCHANGE

24. PAAD BENCHMARK FOR 1989/90: ESTABLISH A LIMITED

TRIAL WITH AN OPEN GENERAL LICENSE SYSTEM.

25. THE GOM LETTER OF INTENT STATES: "...PRODUCTIVE ENTERPRISES MUST HAVE MORE DIRECT ACCESS TO FOREIGN EXCHANGE IN ORDER TO SATISFY DEMAND FOR PRODUCTION INPUTS. THE SUBSTANTIAL REALIGNMENT OF THE EXCHANGE RATE DURING 1987 AND 1988 NOW PROVIDES SCOPE FOR A SHIFT TOWARDS A MORE OPEN TRADE REGIME. THE GOVERNMENT THEREFORE INTRODUCED IN APRIL 1989 A MECHANISM FOR THE NON-ADMINISTRATIVE ALLOCATION OF FOREIGN EXCHANGE, USING FUNDS TO BE MADE AVAILABLE UNDER THE WORLD BANK THIRD REHABILITATION CREDIT.... THE SYSTEM WAS INITIATED BY DEFINING A NARROW RANGE OF IMPORTED INPUTS...FOR WHICH FOREIGN EXCHANGE AND IMPORT LICENSES WILL BE AUTOMATICALLY AVAILABLE ON REQUEST. THE PRODUCT RANGE WILL BE EXPANDED, DURING 1990, TO ENCOMPASS A GREATER SHARE OF AVAILABLE EXCHANGE AS MORE FLEXIBILITY IN THE SUPPLY OF EXTERNAL ASSISTANCE IS ATTAINED. ALL PRODUCTIVE ENTERPRISES WILL BE ELIGIBLE FOR THE SYSTEM AND WILL BE ABLE TO IMPORT ANY ELIGIBLE PRODUCTS THAT ARE INPUTS TO THE PRODUCTIVE PROCESS IN WHICH THEY ARE REGISTERED TO OPERATE."

26. DISCUSSION OF PERFORMANCE: AS INDICATED IN THE LETTER OF INTENT, THE GOVERNMENT ESTABLISHED AN OPEN GENERAL LICENSE SYSTEM (LOCALLY CALLED THE SNAAD) IN APRIL 1989. THE SNAAD BECAME OPERATIONAL ONLY IN NOVEMBER 1989 DUE TO DELAYS IN DISBURSEMENTS FROM THE WORLD BANK THIRD REHABILITATION CREDIT. EXPERIENCE WITH THE SNAAD IS STILL LIMITED, AND IT WILL TAKE TIME UNTIL THE SYSTEM IS KNOWN AND EXTENSIVELY UTILIZED THROUGHOUT THE COUNTRY. HOWEVER, IN THE SNAAD'S SHORT PERIOD OF OPERATION THE GOVERNMENT HAS APPEARED RESPONSIVE TO PRIVATE SECTOR INPUT AND HAS ATTEMPTED TO ATTRACT A GREATER SHARE OF DONOR IMPORT PROGRAMS INTO THE SNAAD IN ORDER TO PHASE DOWN ADMINISTRATIVE FOREIGN EXCHANGE ALLOCATIONS.

27. IMPORTERS WHO HAVE UTILIZED THE SNAAD HAVE INDICATED THAT THEY HAVE INDEED HAD AUTOMATIC ACCESS TO IMPORT LICENSES AND FOREIGN EXCHANGE. IMPORTERS INITIALLY COMPLAINED OF A DOLS 250,000 CEILING PER QUARTER THAT WAS ESTABLISHED TO REGULATE DEMAND. THIS CEILING PRECLUDED THEM FROM MAKING BULK PURCHASES AT PREFERENTIAL RATES AND RESULTED IN HIGHER OVERALL TRANSPORT COSTS. IN RESPONSE TO SUCH COMPLAINTS AND TO ACCELERATE USE OF SNAAD FUNDS, THE GOVERNMENT REMOVED THE QUARTERLY CEILING IN FEBRUARY 1990. IMPORTERS IN ELIGIBLE SECTORS NOW HAVE FREE ACCESS TO FOREIGN EXCHANGE PROVIDED THEY CAN RAISE LOCAL CURRENCY COUNTERPART FUNDS. THE ONLY REGULATORY PROVISION IS THAT IMPORTERS COMPLY WITH WORLD BANK COMPETITION REQUIREMENTS. THE GOM IS PRESENTLY PREPARING FOR USAID A REPORT ON THE USE OF SNAAD FUNDS THROUGH MARCH 31, 1990. THE GOVERNMENT HAS VERBALLY INDICATED THAT PRIVATE FIRMS HAVE BEEN THE PRINCIPAL BENEFICIARIES.

28. THE FIRST YEAR OPERATIONAL TARGET IS THAT THE SNAAD

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WILL FINANCE, BY DECEMBER 1990, DOLS 25 MILLION IN IMPORTS, EQUIVALENT TO ABOUT 20 PERCENT OF MOZAMBIQUE'S UNTIED EXTERNAL AID. INFORMALLY, THE GOVERNMENT HAS ADVISED USAID THAT IT WILL EXPAND THE SNAAD TO MOST AGRICULTURAL INPUTS (INCLUDING SPARE PARTS, IMPLEMENTS, TOOLS, SEEDS, AND POSSIBLY TRACTORS) IN MAY 1990. OTHER NEW SECTORS MAY BE ANNOUNCED AT THAT TIME. THE WORLD BANK AND THE GOVERNMENT PLAN TO EVALUATE THE SNAAD IN JUNE 1990. THIS MAY LEAD TO ADDITIONAL FINE TUNING THAT WILL MOVE THE SNAAD MORE AND MORE TOWARD A MARKET-BASED ALLOCATION MECHANISM.

THE 1990/91 PROGRAM

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29. BASED ON THE GOVERNMENT'S FULLY SATISFACTORY PERFORMANCE ON THE 1989 BENCHMARKS, USAID WILL BEGIN TO NEGOTIATE A FOLLOW-UP LETTER OF INTENT WHICH WILL LAY OUT A DETAILED WORK PLAN FOR 1990/91. USAID ANTICIPATES THAT THIS LETTER OF INTENT WILL COMPLY WITH THE 1990/91 BENCHMARKS PROPOSED IN THE PAAD.

30. ON AGRICULTURAL PRODUCER PRICES, THE GOVERNMENT HAS ALREADY ESTABLISHED A FLOOR PRICE SYSTEM FOR BEANS AND HAS EXPRESSED ITS INTENT TO DO SO FOR MAIZE AND RICE. THE KEY ISSUE ON CASH CROPS WILL BE TO ENSURE A MARKET-DETERMINED PRICE. IN 1989/90 CASH CROPS TRADED AT PRICES ABOVE THE GOVERNMENT'S FLOOR PRICES. SUBSTANTIVELY, USAID FEELS THE OBJECTIVE OF MARKET-DETERMINED PRICES CAN BE ACHIEVED EITHER BY ELIMINATING THE FLOOR PRICES COMPLETELY OR MAINTAINING THE FLOOR PRICES AT A LEVEL THAT ALLOWS THE MARKET TO FUNCTION, AS WAS DONE IN 1989. IN THE LATTER CASE, FLOOR PRICES SERVE AS A SAFETY NET MEASURE FOR FARMERS IN AREAS WHERE MARKETS STILL REMAIN THIN.

31. ON STATE FARM DIVESTITURES, THE GOVERNMENT HAS AGREED TO THE FRAMEWORK FOR FURTHER ANALYSIS AND IMPLEMENTATION OF DIVESTITURE POLICIES IN CONJUNCTION WITH USAID AND THE LAND TENURE CENTER AS DISCUSSED IN PARA 17C. THE DIALOGUE ON LAND ISSUES IS, FURTHERMORE, EXPECTED TO CONTRIBUTE SIGNIFICANTLY TO THE DEVELOPMENT OF CONSTITUTIONAL PROVISIONS ON PRIVATE LAND OWNERSHIP. USAID'S STRATEGY FOR 1990/91 IS TO: (A) COMPLETE THE STATEMENT OF GUIDELINES AND POLICIES FOR DIVESTITURE AND LAND USE; (B) DESIGN AND INITIATE THE IMPLEMENTATION TRIALS WITH THE GOVERNMENT AND LTC; AND (C) HELP THE GOVERNMENT MAKE UNEQUIVOCAL PROVISIONS FOR PRIVATE LAND OWNERSHIP IN ITS DRAFT CONSTITUTION.

32. IN SUPPORT OF PRIVATE SALES AND SERVICE NETWORKS FOR AGRICULTURAL INPUTS, USAID WILL CONTINUE THE PRIVATE SECTOR FOCUS OF THE CIP. COMMODITY SALES TO END USERS WILL CONTINUE TO BE MARKET DRIVEN RATHER THAN BASED ON ADMINISTRATIVE ALLOCATIONS. LETTER OF INTENT NEGOTIATIONS WILL ENCOMPASS EXTENDING MARKET-DRIVEN SALES TO OTHER IMPORT SUPPORT PROGRAMS IMPLEMENTED BY THE GOVERNMENT AND THE IDENTIFICATION OF AGRICULTURE-RELATED PARASTATALS FOR DIVESTITURE.

33. LASTLY, USAID WILL CONTINUE TO SUPPORT THE WORLD BANK'S LEAD ROLE IN TESTING AND INSTITUTIONALIZING A MARKET-BASED FOREIGN EXCHANGE ALLOCATION SYSTEM. THE KEY ISSUES IN 1990 WILL BE A THOROUGH EVALUATION OF THE SNAAD AND ITS EXPANSION TO ENCOMPASS A LARGER SHARE OF UNTIED FOREIGN EXCHANGE. EVALUATION QUESTIONS ON WHICH USAID WILL FOCUS ARE: CONFIRMING PRIVATE SECTOR ACCESS TO THE SNAAD, ENSURING THAT PARASTATALS DO NOT FINANCE TRANSACTIONS THROUGH SUBSIDIES AND PREFERENTIAL CREDIT, REVIEWING WHETHER EXCHANGE RATE MANAGEMENT REFLECTS INCREASED DEMAND ON THE OFFICIAL FOREIGN EXCHANGE MARKET, AND THE ESTABLISHMENT OF ADEQUATE ACCOUNTING AND MONITORING SYSTEMS. USAID PARTICIPATION IN THE SNAAD WILL DEPEND ON THE EVALUATION FINDINGS.

34. SEPTEL HAS BEEN SENT CONCURRENTLY WITH THIS CABLE REQUESTING BUDGET ALLOWANCE AND PAAD AMENDMENT NUMBER. AN EXPANDED VERSION OF BENCHMARKS FOR THE OVERALL USAID PROGRAM IN MOZAMBIQUE, AS REQUESTED AT THE USAID CONCEPTS

PAPER/COUNTRY PROGRAM STRATEGIC PLAN REVIEW, FOLLOWS
SHORTLY BY COURIER. METELITS

BT
#1336

NNNN

Annex B

AID/W Design Guidance

8.2

ACTION: AID-3 INFO: AMB DCM

VZCZCT00279
PP RUEHTO
DE RUEHC #1281/01 0882343
ZNR UUUUU ZZH
P 292340Z MAR 90
FM SECSTATE WASHDC
TO RUEHTO/AMEMBASSY MAPUTO PRIORITY 3465
INFO RUEHNR/AMEMBASSY NAIROBI PRIORITY 7668
BT
UNCLAS SECTION 01 OF 03 STATE 101281

LOC: 106
30 MAR 90
CN:
CHRG: FAA
DIST: AID

AIDAC NAIROBI FOR REDSO/ESA

E.O. 12356: N/A
TAGS:
SUBJECT: MOZAMBIQUE FY-1990 AGRICULTURAL MARKETING CONCEPT PAPER

REF: MAPUTO 0135

1. AN INFORMAL REVIEW, CHAIRED BY DAA/AFR ELSAIERS, AND ATTENDED BY REPRESENTATIVES FROM AFR/SA, AFR/PD/SA, PPC/PB, AFR/DP/PAB AND AFR/DP/PPE WAS HELD ON MARCH 1, 1990 TO CONSIDER THE CONCEPT PAPER, REFTEL, SUBMITTED BY USAID/MOZAMBIQUE. THE BUREAU FOR AFRICA APPROVES FOR FURTHER DEVELOPMENT AN AGRICULTURAL MARKETING ACTIVITY TO BE ADDED TO THE EXISTING PRIVATE SECTOR SUPPORT PROGRAM (656-0208), SUBJECT TO THE GUIDANCE CONTAINED HEREIN. AN INFORMAL AGENDA, PREPARED BY AFR/PD/SA (FYI: THIS PAPER HAS BEEN PROVIDED TO MISSION DIRECTOR WHILE IN AID/W ON CONSULTATION. END FYI) GUIDED THE DISCUSSION AT THE MEETING. THIS CABLE FOLLOWS THE FORMAT OF THAT PAPER.

2. PRIOR TO ENTERTAINING THE SPECIFIC AGENDA QUESTIONS, DISCUSSIONS CENTERED ON THE APPROPRIATENESS OF THE SUB-SECTOR, AG MARKETING, AS (A) A POLICY AREA IN WHICH A.I.D. SHOULD BE INVOLVED AND (B) A CONSTRAINT TO GROWTH IN THE AG SECTOR CONDUCIVE TO BEING RESOLVED THROUGH THE PSSP APPROACH. IT WAS THE GENERAL CONSENSUS THAT THIS WAS AN APPROPRIATE AREA FOR A.I.D. INVOLVEMENT, AND THAT AN ADD-ON TO THE PSSP WAS AN APPROPRIATE VEHICLE FOR PROVIDING THIS ASSISTANCE. IN RESPONSE TO WHETHER THIS ADD-ON SHOULD BE QUOTE AEPRP UNQUOTE, THE CHAIR DEFERRED A DECISION TO MOZAMBIQUE PROGRAM WEEK. WHAT WAS DECIDED WAS THAT THE PROPOSAL WAS WORTHY OF EXTRA-OYB FINANCING AT THE PROPOSED LEVEL OF DOLS 10 MILLION DURING FY 1990.

3. WITH THAT DETERMINATION MADE, THE REVIEW PROCEEDED TO EXAMINE SOME OF THE SPECIFIC AGENDA ITEMS RELATED TO THE PROPOSAL. THE FIRST ITEM RELATED TO THE DEVELOPMENT OBJECTIVE TO BE ACHIEVED IN THE AG MARKETING AREA OVER THE LOP. THE MISSION HAS AN APPROVED STRATEGY FOR PROVIDING FLEXIBLE ASSISTANCE IN THE POLICY AREA THAT IS

PREDICATED ON THE ARTICULATION OF CLEAR OBJECTIVES FOR THAT ASSISTANCE. YET A PICTURE OF WHAT THE MARKETING SYSTEM WILL LOOK LIKE AT THE END OF THIS ACTIVITY IS NOT PRESENTED N THE CONCEPT PAPER. TO BE CONSISTENT WITH THE APPROACH TO POLICY-BASED ASSISTANCE ADOPTED IN MOZAMBIQUE, THE AG MARKETING COMPONENT NEEDS TO BE MORE FULLY INCORPORATED INTO THE PSSP PROGRAM MATRIX.

THIS INCLUDES A CLEAR STATEMENT OF THE OBJECTIVE AND REFORMS TO BE ADOPTED (FIXED FOR THE FIRST YEAR; LESS FIXED FOR THE OUT-YEARS), THE PROGRESS INDICATORS THE MISSION WILL USE TO TRACK ACHIEVEMENT OF THE OBJECTIVE, AND THE PROGRAM'S IMPLEMENTATION BENCHMARKS. ALL THIS NEEDS TO BE DONE PRIOR TO AUTHORIZATION OF THE AMENDMENT.

4. ANOTHER AGENDA ITEM TREATED THE QUESTION OF TIMING OF THE PROPOSED REFORMS. SPECIFICALLY, VIS-A-VIS EXCHANGE RATE REFORM, WE DISCUSSED WHETHER THE PROPOSED PROGRAM IN AGRICULTURAL MARKETING WAS PREMATURE. AS STATED IN REFTEL, TWO MAIN PROBLEMS ASSOCIATED WITH IMPROVING THE MARKETING SYSTEM ARE THE SECURITY SITUATION AND THE FOREIGN EXCHANGE ALLOCATION SYSTEM. THE FIRST CANNOT BE DEALT WITH BY A.I.D., AND REFORM OF THE FX ALLOCATION SYSTEM IS INCLUDED IN THE CURRENT PSSP AND PFP. HAS PROGRESS ON THE EXCHANGE FRONT BEEN SUFFICIENT TO WARRANT COMPLEMENTARY INTERVENTIONS IN THE AGRICULTURAL MARKETING AREA AT THIS TIME?

THE PSSP SUPPORTS MOVEMENT TOWARD A MARKET-BASED FX

A LOCATION SYSTEM AS A MEANS TO INCREASE THE ACCESS OF PRIVATE ENTREPRENEURS IN THE AGRICULTURAL SECTOR TO FX. AS AN INTERIM STEP, THE PSSP WILL SEEK TO EXTEND THE OGL TO AG INPUTS. IN INCORPORATING THE AG MARKETING COMPONENT WE WOULD EXPECT THE MISSION TO SEEK LIKEWISE TO EXTEND THAT COVERAGE TO TRANSPORT AND OTHER MARKETING-RELATED EQUIPMENT TO BE INITIALLY BROUGHT IN VIA CIP UNDER THE MARKETING COMPONENT.

AS PART OF THE ANNUAL PROGRESS REVIEW OF THE PSSP AS CURRENTLY APPROVED WE EXPECT MISSION WILL PROVIDE A THOROUGH UP-DATE ON STATUS OF THE OGL. WE NOTED THAT MISSION HAS STEPPED BACK FROM THE ORIGINAL PROPOSAL TO DISBURSE A.I.D. FUNDS THROUGH THE OGL BEGINNING IN 199). IN SHORT, WE HAVE LOTS OF QUESTIONS ABOUT THE OGL SYSTEM, ITS STATE OF DEVELOPMENT AND ITS FUNCTIONING. THE ISSUE IS SCHEDULED FOR DISCUSSION DURING PROGRAM WEEK, BUT PRIOR TO THE AUTHORIZATION OF ANY FY 1990 FUNDS, WE EXPECT TO SEE THE PROGRESS REPORT ON THE CURRENT PSSP WHICH WILL INCLUDE THE OGL DISCUSSION.

5. MANY OF THE CONSTRAINTS TO SECTOR GROWTH IDENTIFIED

IN THE CONCEPT PAPER RELATE TO THE EFFICIENCY OF AG MARKETING AND TRANSPORT SYSTEMS (I.E., COSTS ARE HIGH, SERVICE IS POOR TO NON-EXISTENT ETC.). BY IMPLICATION, ONE OF THE OBJECTIVES OF THE PROPOSED PROGRAM IN AG MARKETING WILL BE TO IMPROVE EFFICIENCY OF THE SUBSECTOR BY INTRODUCING/STIMULATING COMPETITION; I.E., INCREASED AVAILABILITY OF SERVICE WILL REDUCE COSTS AND IMPROVE SERVICE. TO DO THIS, THE MISSION NEEDS TO EXAMINE CLOSE(Y THE CONSTRAINTS TO INCREASING COMPETITION. FOR EXAMPLE THE MISSION WILL NEED TO LOOK AT THE PRESENT OWNERSHIP OF TRUCK TRANSPORT, AND TO WHOM ANY NEW TRUCKS ARE GOING SINCE THERE ARE LOTS OF VESTED INTERESTS (PUB(IC AND PRIVATE, WE ~~PRE~~SUME) IN THE MOZAMBICAN-TRANSPORT SECTOR WHICH MAY NOT WELCOME INCREASED COMPETITION. WHAT OTHER MEASURES MIGHT BE NEEDED TO ENSURE THAT COMPETITION IS INCREASED? ARE ADEQUATE CREDIT MEASURES IN PLACE TO BROADEN THE NUMBER OF BUSINESS PEOPLE WHO CAN EFFICIENTLY ENTER THE SECTOR? WILL PARASTATALS CONTINUE TO PROVIDE TRANSPORT SERVICES THAT ARE HEAVILY SUBSIDIZED? HOW WILL THAT AFFECT COMPETITION?

AS FOR THE COMMODITY DEMAND ASSESSMENT, PARA 19 OF REFTEL, WE SUGGEST THAT A BROAD RANGE OF EQUIPMENT BE

OFFERED, SINCE THAT TOO MIGHT AFFECT A BUSINESS PERSON'S DECISION TO ENTER THE SECTOR. FOR EXAMPLE, IF ONLY VERY LARGE TRUCKS WERE OFFERED AND NO CREDIT COULD BE HAD PURCHASERS OF CIP EQUIPMENT WOULD BE LIMITED TO FEW, LARGE BUSINESSES WITH ACCESS TO LARGE AMOUNTS OF CASH. THIS, TOO, COULD WORK AGAINST AN OBJECTIVE THAT INCLUDED INCREASING COMPETITION. THERE IS ALSO AN EQUITY ISSUE HERE. SOME MECHANISM BY WHICH THE BROADEST PARTICIPATION CAN BE ENCOURAGED (E.G., PREFERENTIAL TREATMENT FOR FIRST TIME PURCHASERS OF CIP COMMODITIES) SHOULD BE CONSIDERED. THE COMMODITY LIST ITSELF SHOULD REFLECT A DESIRE FOR BROAD PARTICIPATION (E.G., FEWER LARGE TRUCKS, MORE SMALLER ONES).

6. THE MEETING ALSO CONSIDERED WHETHER THE PROPOSED CONDITIONALITY AREAS ARE SUFFICIENTLY BROAD TO ADDRESS THE FULL GAMUT OF CONSTRAINTS TO IMPROVING THE MARKETING SYSTEM. SPECIFICALLY, ROAD AND BRIDGE INFRASTRUCTURE WAS MENTIONED AS A CONSTRAINT TO PERFORMANCE OF THE AG MARKETING SYSTEM IN MISSION'S CABLE. IT WAS DETERMINED THAT THIS, LIKE THE SECURITY PROBLEM, IS NOT AN ISSUE THAT WE CAN DO ANYTHING ABOUT. AT THE SAME TIME, NOT ADDRESSING THAT CONSTRAINT DOES NOT NEGATE THE NEED FOR THE PROGRAM. IN BRIEF, WE UNDERSTAND THAT A.I.D. CANNOT RESOLVE THE NATIONAL TRANSPORT PROBLEM. WHAT WE ARE CONCERNED ABOUT IS WHETHER A COMPETITIVE SYSTEM OF ACCESS TO AG MARKET TRANSPORT CAN WORK IN SOME AREAS. AS THE SECURITY SITUATION EASES OVER THE LONGER RUN, INFRASTRUCTIVE INVESTMENTS TO SUPPORT SECTORS OF A.I.D. INVESTMENT WILL UNDOUBTEDLY BE CONSIDERED AS PART OF NATIONAL RECONSTRUCTION. DEPENDING ON HOW THE GPRM, A.I.D. AND OTHER DONORS REVISE THEIR STRATEGIES. THIS MAY OR MAY NOT BE APPROPRIATE FOR USG FINANCING, BUT THE

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CONCERN SHOULD BE ADDRESSED AT SOME FUTURE DATE.

7. DISBURSEMENT STRATEGY: PARA 11 OF REFTEL PROPOSES THAT UP TO 60 PERCENT OF THE ADDITIONAL AUTHORIZED PROGRAM LEVEL BE DISBURSED UPON RECEIPT OF A LETTER OF INTENT FROM THE GPRM AND 40 PERCENT REMAIN FOR DISBURSEMENT AGAINST PROGRESS ON REFORMS. WHILE WE HAVE YET TO SEE THE SPECIFIC REFORMS, ADDRESSING THE POLICY PROBLEMS IDENTIFIED IN REFTEL PLUS THOSE DISCUSSED IN THIS CABLE COULD RESULT IN A RATHER LARGE PACKAGE OF REFORMS TO BE IMPLEMENTED. ALSO, GIVEN THE PERCEIVED NEED TO STIMULATE AS WELL AS TO ENSURE COMPETITION IN THE SECTOR, DOES IT MAKE SENSE TO DISBURSE UP TO 60 PERCENT OF THE RESOURCES BEFORE ANY OF THE BARRIERS TO ENTRY HAVE BEEN ADDRESSED? THE LETTER OF INTENT, SINCE IT CONFIRMS AND RECORDS A.I.D. AND GPRM UNDERSTANDINGS ON THE OBJECTIVES OF THE PROGRAM SHOULD BE REQUIRED PRIOR TO PROGRAM OBLIGATION. THE REMAINDER OF THE CONDITIONALITY SHOULD BE INCORPORATED INTO A REVISED REFORM PROGRESS AND DISBURSEMENT STRATEGY FOR THE WHOLE PSSP. IN THIS WAY, THE MISSION AND GPRM WILL BE ABLE TO ADDRESS THE ISSUE OF REFORM PHASING MORE COMPREHENSIVELY.

8. DESIGN STRATEGY AND AUTHORIZATION VENUE: PRIOR TO THE AUTHORIZATION OF EITHER THE PAAD AMENDMENT FOR THIS YEAR'S ON-GOING COMMITMENT TO THE PSSP AS CURRENTLY APPROVED, THE REVIEW ON PROGRESS OF THE CURRENT REFORM PACKAGE NEEDS TO BE CARRIED OUT. AID/W WILL WISH TO REVIEW THAT PROGRESS PRIOR TO THE INCREMENTAL AUTHORIZATION/OBLIGATION OF FY 1990 FUNDS. ONCE COMPLETE, MISSION SHOULD PROCEED TO OBLIGATE CURRENTLY APPROVED FY 1990 FUNDS (DOLS 12.5 MILLION CIP AND DOLS 620,000 PROJECT). THE MARKETING AMENDMENT WILL REQUIRE A SEPARATE DESIGN, APPROVAL AND AUTHORIZATION TRACK. SEPARATING THESE ACTIONS WILL ALLOW ADEQUATE TIME FOR FULL DEVELOPMENT OF THE MARKETING ACTIVITY. IN THE

COURSE OF PROGRAM WEEK DISCUSSIONS IN AID/W, MISSION AND BUREAU PERSONNEL WILL ADDRESS THE ISSUE OF WHAT AID/W WILL WANT TO APPROVE AND AUTHORIZE IN CONJUNCTION WITH THE MARKETING ACTIVITY; I.E., WHETHER THE WHOLE AMENDMENT PACKAGE OR SOMETHING LESS SHOULD BE REVIEWED IN AID/W. SEPTEL WILL PROVIDE FINAL GUIDANCE ON THIS POINT. BAKER
BT
#1281

NNNN

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ACTION: AID-3 INFO: AMB DCM

VZCZCT00777
OO RUEHTO
DE RUEHC #5374/01 1992342
ZNR UUUUU ZZH
O P 182337Z JUL 90
FM SECSTATE WASHDC
TO RUEHTO/AMEMBASSY MAPUTO IMMEDIATE 4155
INFO RUEHNR/AMEMBASSY NAIROBI PRIORITY 1718
RUEHMB/AMEMBASSY MBABANE 9727
BT
UNCLAS SECTION 01 OF 04 STATE 235374

LOC: 219 656
19 JUL 90 0550
CN: 04848
CHRG: FAAS
DIST: AID

ACTION
20 JUL 1990
ACTION OFFICER
INFO:
ACTION TAKEN:

AIDAC NAIROBI FOR REDSO/ESA; MBABANE FOR RLA

E.O. 12356: N/A
TAGS:
SUBJECT: MOZAMBIQUE PRIVATE SECTOR SUPPORT PROGRAM (656-0208)

REFS: A) STATE 101281 (NOTAL); B) MAPUTO 1336 (NOTAL)

1. AN AFRICA BUREAU PROJECT COMMITTEE MEETING WAS HELD ON MAY 22, 1990 TO REVIEW THE PROGRESS REPORT SUBMITTED BY USAID/MOZAMBIQUE (REF B) FOR THE SUBJECT PROGRAM. THOSE PRESENT REPRESENTED AFR/PD/SA, AFR/DP/PPE, AFR/DP/PAR, AFR/TR/ANR AND GC/AFR. WHILE AFR/SA WAS NOT PRESENT AT THE MEETING, THAT OFFICE HAS CONCURRED IN THE CONTENTS OF THIS CABLE. THIS CABLE PROVIDES USAID/MOZAMBIQUE WITH AN AD HOC DOA TO AMEND THE PSSP PAAD TO ADD THE AEPRP-FINANCED AGRICULTURAL MARKETING COMPONENT, SUBJECT TO THE GUIDANCE CONTAINED HEREIN AND IN CONJUNCTION WITH GUIDANCE CONTAINED IN REF A (THE AEPRP GUIDANCE CABLE).

2. GENERAL COMMENTS. IN ITS REVIEW, THE PROJECT COMMITTEE FOCUSSED MOST OF ITS ATTENTION ON COMPARING THE MISSION'S PROPOSAL FOR FY 1990-91 CONDITIONALITY WITH THE QUOTE TERMS FOR DISBURSEMENT IN EXCESS OF DOLS 13,550,000 UNQUOTE, AS CURRENTLY CONTAINED IN THE PAAD AUTHORIZATION. THE COMMITTEE WAS PLEASED WITH THE CLEAR PROGRESS MADE IN EACH OF THE AREAS COVERED BY THE CURRENT PROGRAM, AND WE COMMEND THE MISSION FOR A REPORT THAT WELL DOCUMENTS BOTH PROGRESS AND OUTSTANDING ISSUES. THE REPORT ALSO INDICATES THAT THE MEANS OF ACHIEVING SOME OF THE OBJECTIVES HAVE VARIED FROM WHAT WAS ORIGINALLY ENVISAGED. AS A RESULT THE ACTIONS TAKEN OVER THE PAST YEAR DO NOT IN EVERY INSTANCE CORRESPOND WITH THE WORKPLAN SET OUT IN THE 1989 LETTER OF INTENT (LOI). IN OUR VIEW, THE INTENT OF THE FIRST YEAR CONDITIONALITY WAS MET CLEARLY, BUT COMPLIANCE WITH THE STRICT LETTER OF THE CONDITIONALITY (I.E., THE WORKPLAN IN THE LOI) HAS NOT IN ALL INSTANCES PROVEN PRACTICAL. BOTH AID/W AND THE MISSION RECOGNIZED THAT THIS MIGHT HAPPEN WHEN THE PROGRAM WAS DESIGNED AND APPROVED, AND

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WE BELIEVE THAT SUFFICIENT FLEXIBILITY TO ADDRESS THE SITUATION IS DESIGNED INTO THE PROGRAM. IT IS NECESSARY PRIOR TO AUTHORIZATION AND OBLIGATION OF FY 1990 FUNDS, TO MODIFY AND DOCUMENT CHANGES IN THE POLICY MEASURES WHICH CONSTITUTE THE CONDITIONALITY. THIS INVOLVES TWO THINGS. (1) SINCE ONE CP TO DISBURSEMENT OF THE FY 90 TRANCHE IS COMPLIANCE WITH THE FY 89 WORKPLAN, TO THE EXTENT THAT IT WAS NOT TECHNICALLY COMPLIED WITH, EITHER THE PLAN IN THE LOI (AND PAAD MATRIX) NEED TO BE RETROACTIVELY MODIFIED TO REFLECT WHAT OCCURRED, OR THE FY 90 CP NEEDS TO BE MODIFIED DIRECTLY TO REFLECT WHAT ACTUALLY OCCURRED. (2) TO THE EXTENT THAT THE POLICY MEASURES TO BE ACCOMPLISHED IN FY 90 WILL DIFFER FROM THOSE IN THE PAAD MATRIX AND LOI, THOSE DOCUMENTS NEED TO BE REVISED. THE DISCUSSION BELOW WILL SUGGEST SPECIFIC MODIFICATIONS WHICH THE MISSION SHOULD CONSIDER IN ITS NEGOTIATIONS WITH THE GOVERNMENT OF MOZAMBIQUE (GOM).

3. AGRICULTURAL PRODUCER PRICES.

A. DISCUSSION. IN 1989/90, THE GOM MOVED CASH CROPS AND BEANS TO A FLOOR PRICE SYSTEM IN WHICH FLOOR PRICES ARE RELATED TO INTERNATIONAL BORDER PRICES. MAIZE AND RICE CONTINUED TO BE SOLD AT FIXED PRICES ALSO RELATED TO IMPORT PARITY. THE TRANSFER OF BEAN PRICING TO THE FLOOR PRICE SYSTEM WAS DONE A YEAR EARLIER THAN ORIGINALLY INTENDED, AND THE GOM CLEARLY SURPASSED FIRST YEAR CONDITIONALITY IN THIS RESPECT. FOR 1990/91, THE MISSION PROPOSES THAT THE GOM WILL MOVE MAIZE AND RICE

TO THE FLOOR PRICE SYSTEM. IN ADDITION, THE MISSION BELIEVES THAT THE KEY ISSUE FOR THE 1990/91 PERIOD WILL BE TO ENSURE A QUOTE MARKET-DETERMINED PRICE UNQUOTE FOR CASH CROPS. WE AGREE THAT THIS WILL BE THE MAIN ISSUE, BUT WE ARE CONCERNED WITH THE MISSION'S PROPOSAL TO ALLOW THE FLOOR PRICE SYSTEM TO OPERATE FOR ALL CROPS. AS STATED IN THE PROGRESS REPORT, THE MISSION BELIEVES THAT QUOTE THE OBJECTIVE OF MARKET-DETERMINED PRICES CAN BE ACHIEVED EITHER BY ELIMINATING THE FLOOR PRICE SYSTEM ALTOGETHER OR BY MAINTAINING THE FLOOR PRICES AT A LEVEL THAT ALLOWS THE MARKET TO FUNCTION, AS WAS DONE IN 1989. UNQUOTE. IN 1989, THE FIXED PRICE ESTABLISHED FOR MAIZE AND RICE WAS APPROXIMATELY IMPORT PARITY PLUS TEN PERCENT AND FLOOR PRICES RANGED FROM 50 PERCENT OF IMPORT PARITY TO 80 PERCENT OF IMPORT PARITY FOR CASH CROPS. IMPORT PARITY WAS CALCULATED AT THE OFFICIAL EXCHANGE RATE FOR BOTH FIXED AND FLOOR PRICES. GIVEN THE DISPARITY BETWEEN THE OFFICIAL AND PARALLEL MARKET VALUE OF THE METICAL, THE COMMITTEE QUESTIONED WHETHER THE CALCULATION WAS WORTHWHILE. ON THE SURFACE, IMPORT PARITY PLUS TEN PERCENT APPEARS TO BE A PRICE DESIGNED

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TO STIMULATE PRODUCTION, BUT IN REALITY THE CALCULATION PROBABLY RESULTS IN A DOMESTIC PRICE THAT BEARS NO RESEMBLANCE TO ITS OPPORTUNITY COST (I.E. A COST CALCULATED AT AN EXCHANGE RATE REFLECTIVE OF THE SHADOW PRICE OF THE METICAL) OR IMPORTING THE SAME COMMODITY. IT SHOULD, IN FACT, RESULT IN A PRICE THAT IS SO LOW AS TO BE MEANINGLESS, AND WE ASSUME THAT THAT IS WHAT THE MISSION MEANT REGARDING THE CONTINUATION OF FLOOR PRICES THAT ARE ESTABLISHED SO THAT THE MARKET FUNCTIONS WELL ABOVE THEM. BUT WHAT IS THE PURPOSE IN MAINTAINING A FLOOR PRICE SYSTEM THAT IS MEANINGLESS OTHER THAN FOR INCOME SECURITY REASONS, DISCUSSED BELOW? SINCE THERE IS CLEARLY COST TO THE GOM BUDGET ASSOCIATED WITH ADMINISTERING THE FLOOR PRICE SYSTEM, WOULDN'T IT BE A NET BENEFIT TO ELIMINATE THE SYSTEM? SINCE THE MOVE TO MARKET BASED PRICING FOR 1990/91 WAS ORIGINALLY PLANNED FOR ALL CROPS EXCEPT MAIZE, RICE AND BEANS, WHAT IS THE RATIONALE AT THIS TIME FOR NOT MOVING FORWARD? WE WOULD ALSO EXPECT THAT SINCE THE GOM MOVED BEANS TO THE FLOOR PRICE SYSTEM LAST YEAR, THEY TOO WOULD MOVE TO A MARKET PRICING SYSTEM FOR 1990/91.

SINCE THE MISSION POSED TTE QUESTION OF TWO MODALITIES FOR ACHIEVING MARKET PRICES, WE EXPECT THAT THE MISSION WILL THOROUGHLY EXPLORE THE ADVANTAGES OF EACH

ALTERNATIVE WITH THE GOM AS PART OF THE LOI NEGOTIATIONS. AID/W PREFERENCE IS FOR LESS INTERFERENCE IN THE MARKET AT THE EARLIEST FEASIBLE TIME. IF THERE IS NO ECONOMIC RATIONALE FOR MAINTAINING THE FLOOR PRICE SYSTEM FOR CASH CROPS AND BEANS IN 1990/91, THEN THE GOVERNMENT SHOULD BE ENCOURAGED TO DISMANTLE THE SYSTEM SOONER RATHER THAN LATER.

ANOTHER PROBLEM WITH CALCULATING FLOOR PRICES BASED ON IMPORT PARITY AT THE OFFICIAL EXCHANGE RATE HAS TO DO WITH EQUITY CONSIDERATIONS. ONE TYPICAL RATIONALE FOR A FLOOR PRICE SYSTEM IS TO ENSURE A BASE OR MINIMUM PRICE TO PRODUCERS. HOW DOES IMPORT PARITY CALCULATED AT THE OFFICIAL EXCHANGE RATE AFFECT FAMILY INCOME? ARE FLOOR PRICES FOR CASH CROPS SO LOW AS TO RESULT IN TOTAL INCOME BELOW THE POVERTY LINE? IF SO, THE SYSTEM WOULD APPEAR TO BE MEANINGLESS AS A MINIMUM GUARANTEE FOR FARMER INCOME AS WELL. FROM OUR PERSPECTIVE, IT SEEMS THAT THE MISSION'S CHOICE FOR 1990/91 SHOULD BE TO ENSURE THAT A REALISTIC EXCHANGE RATE IS USED FOR PARITY CALCULATIONS AND, IF NECESSARY, MAINTAIN THE FLOOR PRICE FOR INCOME SECURITY. TOGETHER, THEY SHOULD PROMOTE MOVEMENT TOWARDS MARKET DETERMINED PRICES AND MINIMIZE RISK VIA THE FLOOR PRICE.

B. GUIDANCE. THE 1990/91 BENCHMARK FOR MAIZE. BEANS' AND RICE WILL NEED TO BE REVISED TO REFLECT REAL GOM INTENT. WE EXPECT THAT THE CONDITIONALITY BENCHMARK FOR 1990/91 AS STATED IN THE PAAD POLICY MATRIX WOULD BE ACHIEVED AT A MINIMUM. GIVEN EARLIER THAN ANTICIPATED MOVEMENT ON BEAN PRICES, WE WOULD EXPECT BEANS TO BE TREATED AS CASH CROPS FOR CONDITIONALITY PURPOSES FOR

1990/91. MOVING RICE AND MAIZE TO A FLOOR PRICE SYSTEM SHOULD ALSO BE REGARDED AS MINIMUM CONDITIONALITY FOR 1990/91. SINCE THE FIXED PRICES HAVE BEEN SO LOW FOR THESE COMMODITIES THAT THE MARKET HAS FUNCTIONED FREELY WELL ABOVE THEM, WE WOULD ENCOURAGE THE MISSION TO URGE THE GOM TO MOVE TO A MARKET BASED SYSTEM DIRECTLY. WE ALSO ENCOURAGE THE MISSION TO SORT THROUGH THE ISSUES RELATED TO AN IMPORT PARITY-BASED FLOOR PRICE SYSTEM CALCULATED AT DISTORTED EXCHANGE RATES.

4. DIVESTITURE OF STATE FARMS.

A. DISCUSSION. FROM THE MISSION REPORT, CONSIDERABLE PROGRESS IN THIS AREA HAS BEEN ACHIEVED. THE FACT THAT

IN BEGINNING TO DEVELOP ITS DIVESTITURE PLAN FOR EACH FARM, THE GOM NEEDED TO REASSESS AND REDRESS THE POLICY ENVIRONMENT IS NOT SURPRISING TO THE AID/W COMMITTEE. THE FACT THAT THE GOM IS MOVING SO SWIFTLY TO BOTH CLARIFY ITS POLICY AT THE CONSTITUTIONAL LEVEL AND TO PROMULGATE AND ACT UPON THAT POLICY INDICATES BOTH A CLEAR COMMITMENT TO THE PRIVATE OWNERSHIP OF LAND, AS WELL AS ACTUAL PROGRESS MADE OVER THE PAST YEAR.

WE ENCOURAGE THE MISSION IN DEALING WITH THE GOM ON THIS ISSUE TO DEEMPHASIZE RACKING UP SPECIFIC NUMBERS OF DIVESTITURES AND TO FOCUS EFFORTS ON ESTABLISHING AND IMPLEMENTING THE POLICY AND LEGAL FRAMEWORK TO ENSURE ORDERLY DIVESTITURE, FINANCING, TRANSFER, AND TENURE SECURITY FOR NEW HOLDERS. IN THIS REGARD, WE ARE CONCERNED THAT THE MOST RECENT PFP CONTINUES TO PLACE PRIMARY EMPHASIS ON NUMBERS OF ENTERPRISES DIVESTED AND HECTARES TRANSFERRED TO PRIVATE CONTROL.

FINALLY, THE COMMITTEE DISCUSSED THE APPARENTLY LITTLE EMPHASIS BEING PLACED ON DISPOSITION OF CAPITAL

INVESTMENT ON DIVESTED FARMS. WHILE SMALL AND FAMILY FARMERS MAY BE RECEIVING THE LAND DE FACTO AT PRESENT, WHO IS RECEIVING THE CAPITAL EQUIPMENT? WE DISCUSSED WHETHER THE MISSION MIGHT CONSIDER ENCOURAGING THE GOM TO DEVELOP A COHERENT/CONSISTENT STRATEGY TO DIVEST ITSELF OF THE CAPITAL IMPROVEMENTS. HAS THIS BEEN DONE

B. GUIDANCE. GOM AND MISSION CLEARLY NEED TO REVISE THE WORKPLAN FOR THIS OBJECTIVE. 1989/90 ACTIONS TAKEN NEED TO BE RECORDED SINCE THEY DIFFER SUBSTANTIVELY FROM LOI AND WORKPLAN. MISSION PROPOSED BENCHMARKS FOR 1990/91 (PARA. 31, REF B), APPEAR REASONABLE FROM AID/W BUT OUR IMPRESSION IS THAT A LOT OF A.I.D. EFFORT AND ASSISTANCE MAY BE REQUIRED TO ACCOMPLISH THE THREE TASKS IDENTIFIED. WE UNDERSTAND MISSION IS PREPARED TO PROVIDE THIS ASSISTANCE ON A CONTRACT BASIS AND THAT IS APPROPRIATE. AT THE SAME TIME WE ENCOURAGE THE MISSION TO TAKE APPROPRIATE MEASURES TO ENSURE THAT CONTRACTORS RECEIVE SUFFICIENT A.I.D. OVERSIGHT SO THAT THEY REMAIN WITHIN THE PARAMETERS OF MISSION OBJECTIVES.

FINALLY, WE BELIEVE THAT THE MISSION'S STATEMENT OF OBJECTIVE IN THIS AREA NEEDS SOME REVISION. IT SEEMS THAT AT A MINIMUM THE CONCEPT OF THE QUOTE ACTION PLAN UNQUOTE HAS ALTERED CONSIDERABLY. MISSION AND GOM

SHOULD CAREFULLY ASSESS THE OBJECTIVE STATEMENT, DOCUMENT RATIONALE AND ANY CHANGE, AND MAKE APPROPRIATE REVISIONS PRIOR TO OBLIGATING FY 1990 FUNDS.

5. PRIVATE NETWORKS FOR AGRICULTURAL INPUTS.

A. DISCUSSION. THE MISSION REPORT DOCUMENTED MORE THAN SATISFACTORY PROGRESS IN THIS AREA. THE COMMITTEE WAS PARTICULARLY APPRECIATIVE OF MISSION'S INSIGHTS INTO SPIN-OFF EFFECTS THAT LIBERALIZATION OF INPUT SALES/SERVICE IS HAVING IN RURAL AREAS. SPECIFIC REFERENCES TO INCREASED ENTRANTS INTO THE SECTOR AS WELL AS INCREASED ACCESS TO AND USE OF AGRICULTURAL INPUTS BY FARMERS WERE MOST INFORMATIVE. FURTHERMORE, WE WERE PLEASED TO NOTE THAT FOR 1990/91 MISSION AND GOM ARE PREPARING TO ENTER INTO DISCUSSION ON DIVESTITURE OF SPECIFIC PUBLIC ENTERPRISES WHICH PROVIDE AGRICULTURAL INPUTS. HOWEVER, GIVEN THE EVIDENCE THAT EXISTS WHICH IMPLIES THAT THE PRIVATE SECTOR WILL MOVE INTO THE SECTOR AS PARASTATALS CLOSE DOWN, WE WONDER WHY THE MISSION ISN'T LOOKING FOR MORE FROM THE GOM OVER 1990/91 THAN TO SIMPLY IDENTIFY PARASTATALS FOR DIVESTITURE. IS IT UNREASONABLE TO REQUEST THAT IN ADDITION TO IDENTIFICATION OF SPECIFIC ENTERPRISES, THE GOM ALSO DEVELOP A PRIORITIZED ACTION PLAN? GIVEN GOOD WILL AND THE EXPERIENCE TO DATE, IT WOULD SEEM APPROPRIATE TO THE PROCESS OF DIVESTITURE TO ACTUALLY BEGIN SUCH A PLAN, IF NOT AS PART OF THIS COMPONENT, PERHAPS AS PART OF THE MARKETING COMPONENT TO BE ADDED.

B. GUIDANCE. MISSION SHOULD CONSIDER ADVANCING THE WORK PLAN FOR THIS COMPONENT, PER DISCUSSION ABOVE.

6. ACCESS TO FOREIGN EXCHANGE.

A. DISCUSSION. THE COMMITTEE BELIEVES THAT MISSION.S DECISION TO APPROACH SUPPORT OF THE OGL WITH CAUTION IS VALID. THE PROPOSED EVALUATION OF THE OGL IS CLEARLY NECESSARY PRIOR TO INCREASED DONOR FINANCIAL SUPPORT FOR THE MECHANISM. WE WONDER, HOWEVER, WHAT RELATIONSHIP THERE IS BETWEEN THE EXCELLENT QUESTIONS POSED BY THE MISSION IN PARA. 33 OF THE PROGRESS REPORT AND THE EVALUATION THAT THE WORLD BANK IS CONDUCTING IN JUNE/JULY. WILL THAT EVALUATION ADDRESS MISSION'S CONCERNS? IF NOT, WHAT ACTION DOES THE MISSION PROPOSE TO TAKE? GIVEN THE TENOR OF MISSION CONCERNS AND

INFORMATION PROVIDED BY THE MISSION INFORMALLY, WE ASSUME THAT THE MISSION WILL WISH TO INDEPENDENTLY VERIFY THE EFFECTIVENESS OF THE LIMITED OGL AND ITS PROSPECTS FOR SUCCESS AS A MEANS OF ALLOCATING AND DETERMINING THE PRICE OF FOREIGN EXCHANGE IN MOZAMBIQUE. WHILE WE SUPPORT SUCH INDEPENDENT VERIFICATION, WE ALSO WISH TO EMPHASIZE THAT PROGRESS TOWARD LIBERALIZING THE FOREIGN EXCHANGE REGIME IS A CRUCIAL PART OF THIS PROGRAM. WITHOUT IT, MOST OF THE OTHER POLICY REFORMS WILL HAVE LITTLE SUSTAINABLE IMPACT ON PRODUCTION AND INCOMES. PROGRESS TOWARD FREEING THE ALLOCATION MECHANISM NEEDS TO CONTINUE OVER THIS NEXT YEAR, AND IT SHOULD BE TREATED AS PART OF THE AGENDA FOR 1990/91.

B. GUIDANCE. IF SUFFICIENT INFORMATION IS AVAILABLE TO THE MISSION PRIOR TO OBLIGATING FY 1990 FUNDS, THE MISSION AND THE GOM SHOULD ARRIVE AT A DECISION ON THE OGL AND REFLECT IT IN THE AGENDA FOR 1990/91 E.G., EXPAND THE OGL, EXPAND THE TRIAL, ETC. IF THE MISSION BELIEVES THAT INFORMATION AVAILABLE PRIOR TO NEGOTIATING

THE LOI IS INSUFFICIENT TO ARRIVE AT ANY STATEMENT OF OGL EXPANSION OVER THE NEXT YEAR, WE ENCOURAGE THE MISSION TO WORK OUT A STRATEGY WITH THE GOM THAT SPECIFIES A SCHEDULE FOR REACHING SOME CONCLUSIONS ON THE OGL. THE 1990/91 WORKPLAN FOR THE PSSP SHOULD NOT REMAIN SILENT ON THE ISSUE OF LIBERALIZING THE FOREIGN EXCHANGE REGIME. ACTIONS TOWARD THE OBJECTIVE SHOULD BE EXPLICITLY LAID OUT FOR THE 1990/91 PERIOD, EVEN IF THEY LARGELY CONSIST OF STEPS TO REVIEW, EVALUATE AND DECIDE A COURSE OF ACTION ON THE OGL. AID/W UNDERSTANDS THAT MISSION IS NOT REQUESTING AID/W CONCURRENCE, REQUIRED IN ORIGINAL PAAD, TO DISBURSE FY 90 AID FUNDS INTO THE OGL.

7. AEPRP FINANCED ACTIVITY. REP A PROVIDED GUIDANCE ON THE AEPRP FINANCED AGRICULTURAL MARKETING COMPONENT. PURSUANT TO THE DELEGATION OF AUTHORITY IN PARA. 8, BELOW, MISSION MAY PROCEED TO APPROVE PAAD AMENDMENT. WE DO REQUEST, HOWEVER, THAT PRIOR TO OBLIGATING THE AEPRP FUNDS, MISSION SUBMIT TO AID/W FOR INFORMAL COMMENT THE FOLLOWING RE THE NEW COMPONENT: (A) THE POLICY MATRIX; (B) THE DRAFT LOI; AND (C) A REVISED LOCAL CURRENCY USE PLAN IF SUBSTANTIVE CHANGES IN USES ARE CONTEMPLATED.

8. DELEGATION OF AUTHORITY. THE ACTING AA/AFR HEREBY

DELEGATES AUTHORITY TO THE MISSION DIRECTOR, USAID/MOZAMBIQUE, TO AMEND THE PRIVATE SECTOR SUPPORT PROGRAM (656-0208) TO ADD AN AGRICULTURAL MARKETING COMPONENT, RESULTING IN A NEW TOTAL APPROVED LOP NOT TO EXCEED DOLS 55.55 MILLION. FUNDING WILL BE INCREMENTALLY AUTHORIZED AND OBLIGATED AS DELEGATED IN THE ORIGINAL PROGRAM APPROVAL AND SUBJECT TO THE SAME TERMS AND CONDITIONS. THIS AD HOC DOA IS SUBJECT TO THE GUIDANCE CONTAINED HEREIN AND IN STATE 101281, DATED MARCH 29, 1990, AND TO ALL THE TERMS AND CONDITIONS OF DOA 551, EXCEPT FOR THE DOLLAR AMOUNT LIMITATION.
BAKER
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Economic Analysis Update

The Original PSSP Analysis

The economic analysis section of the PSS PAAD, prepared in 1989, employed a producers' surplus technique to assess the likely impact of reformed producer prices on the welfare of producers of a range of price-controlled staple and cash crops. The analysis was somewhat unusual and innovative in that it incorporated benefit-cost assessment techniques, techniques that are usually applied only to project assistance, to justify the expenditure of non-project assistance funds. The conclusions of the analysis were that in addition to the program benefits derived by the private sector from the commodity imports, there were additional "producers' surplus" benefits.

To carry out that analysis, the Mission calculated the value of the producers' surplus triangle at varying price elasticities of supply, and using varying percentage changes in prices resulting from the desired reform package. The period selected for the analysis was 1986-89, during which the Government began to reform its agricultural policies. The elasticity estimate finally chosen was at the low, but not improbable, end of the posited elasticity set range, suggesting relative conservatism in its contribution to the predicted program benefits. The low end of posited price increases was based upon an increase from 1986 agricultural prices to floor prices prevailing in 1989. The high end of the price increases assumed that free trade of commodities would raise 1989 producer prices to international parity parices (IPPs) from their 1986 levels. Implicitly, this band of price increases assumed that if the reforms were to be halted producer prices would return to their pre-reform (i.e., 1986) levels with respect to IPPs. It was not possible to calculate the impact of moving prices from a 1989 base below adjusted IPPs to actual IPP levels because six of the nine commodity prices were actually floor prices (rather than fixed prices) and, more importantly, the remaining three producer prices were calculated to be above adjusted IPP producer prices. Thus, a straightforward approach of comparing the divergence of 1989 pre-program official prices from adjusted IPP-related prices was not practicable.

Some Modification to the Original Analysis

When the original analysis was carried out, there were a number of economists in A.I.D. who objected to the analysis in principle. Their primary objection was that the comparison of producers' surplus benefits to costs, with costs defined as the amount of program assistance provided, was misleading, because the amount of program assistance provided was not an accurate measure of costs of the reforms. Some argued this on the basis that there are really no "costs" to a government's making the paper changes that are the policy reform measures. Others argued that although there are (perhaps calculable) costs of reform that might involve compensating those who lose (including those who indulge in abusive rent-seeking activity) when resource allocations shift as a result of policy reform, A.I.D.'s program assistance inputs are never derived on the basis of these costs. In any event, where there are no well-defined costs, benefit-cost analysis is not relevant.

Although there is a certain merit in these objections, insofar as they go, the methodology employed in the original analysis is clearly productive and useful. The important aspect of the original analysis is that it is a valid and useful impact analysis, even if it does not provide straightforward benefit-cost answers. Equally, however, it is important to follow up any such impact analysis with an evaluation to check the validity of the assumptions.

There appear to be some significant differences between the PAAD analysis of producer/IPP price divergence ratios and the IBRD's most recent analyses of these ratios, contained in the 1989 food security study and the 1990 country economic memorandum. At the same time, it is important to note that the analysis of price divergence for 1988 and 1989 in the PAAD is taken directly from the Bank's May 1988 agriculture sector review. The differences between USAID's earlier analysis and the current IBRD analysis appear to stem from two elements. First, the more recent IBRD analyses use international prices that are more current, while the USAID (and May 1988 IBRD) analysis uses international prices for 1989 projected in the IBRD's 1987 biannual price projection paper. Second, the market exchange rate used by USAID for 1989 appears to be too low. In any event, the price divergence ratios currently in use by the Bank are no longer those used in the PAAD, suggesting that at least from the Bank's standpoint the price analysis in the PAAD is no longer correct. In the interests of solidarity (and in the absence of more appropriate prices and exchange rates), it appears preferable at this juncture to use the most recent IBRD price analyses.

Table C-1 contains estimates for an alternative economic impact analysis to that used in the original PAAD. First, more realistic 1989 international prices are used to determine the border prices for the nini products in question. Second, an exchange rate of 960 (meticais per dollar) for 1989 is used, rather than the 750 used in the PAAD. The price relatives (1989 official producer price in relation to adjusted parity prices) for all products show that official prices were below parity prices. Thus, it is possible to employ an approach using a move from pre-program (i.e., 1988/89 crop year) divergence from parity to full parity as the measure of the percentage change in prices likely to occur as a result of the program. In another departure from the analysis in the original PAAD, Table C-1 estimates 1989 production, rather than using the 1986 production estimates included in the PAAD.

The Table suggests that, using a reasonable 0.2 elasticity estimate, a ten percent discount rate, and the 1989 divergence from parity, one can derive potential impacts that are somewhat higher than those in the original PAAD analysis. The potential impact of the program as described in the original PAAD was on the order of $120 million, consisting of $50 million in commodities and $70 million in producers' surplus, over a 20-year period. The revised analysis suggests that the latter figure is perhaps closer to $100 million, bringing the total impact to about $150 million.

An Amended Analysis for this Supplemental Assistance

In the analysis, the Mission explicitly stated that price elasticities of supply on the lower end of the tested range were more likely to obtain because of non-price supply constraints. For example, in discussing the elasticity issue, page 93 of the PAAD states that "(g)iven the transportation difficulties and the general insecurity throughout the country which impede both marketing and input supply, it seems likely that the supply elasticity would be rather low." Thus, one would suppose that the price elasticity of supply would increase if one were to improve marketing conditions, and such improvements are precisely the purpose of this proposed amendment to the program.

The original analysis concluded that a reasonable first approximation of the increase in consumer surplus, discounted over a 20-year period, would be about $70 million ($100 million with our new price assumptions), taking a low price elasticity of supply of 0.2. The currently proposed additon of $10 million to the program would generate an additional $10 million in discounted producer surplus if the elasticity of supply were to be improved slightly from 0.20 to 0.21. This minor increase in elasticity seems plausible as a result of the proposed market liberalizations.

Thus, rather than actually positing an increase in the price elasticity accruing to the marketing reforms we wish to see, we opt to turn the analysis around and state what improvement would be required to justify the expenditure. There are two reasons to use this approach. First, the original analysis did not actually assert an elasticity, but selected one from a range of possibilities. This could be repeated, but it would not tell us anything new regarding this proposed amendment. Second, this is an amendment to an approved program concept, focusing resources on an important element (the marketing element) of a system that is generally considered to need many improvements. It therefore makes sense to consider the minimal extent of marketing improvement required, as reflected in increased price elasticity of supply, to justify the proposed funding increment. As stated above, this required improvement is both modest and realistic.

In addition to the impacts (benefits) discussed in the original PAAD, it is important to mention another (if probably unquantifiable) impact. The program is designed to encourage policy reforms by providing foreign exchange for private sector imports into Mozambique. That benefit was captured in the original analysis by including as benefits to the economy the value of the equipment so imported. In addition, however, the local currency generated under this program (although not a net economic additions) represents a resource made available to the government. If programmed as intended, it will obviate the need for an equivalent amount of government borrowing from the banking system. The effect of this on reducing inflationary pressures in Mozambique is not easy to quantify, but the additional funds available under this program are equivalent to about 15-plus percent of total external grant revenues received in 1989, and are the equivalent of one-third of total additions to the stock of the banking system's lending to the government in 1989. This program is thus serving a useful role in enabling the government budget to relax its claims on the domestic banking system for financing the government deficit.

Table C-1
Summary Economic Analysis

1989 Shortfall from Parity

.Commodity	1989 Prod. Value	Actual Price/ Parity	Percent Increase Needed	-----Range of Elasticities---- 1.0	0.5	0.2	0.1
Maize	74334.1	87.0	15.0	837	418	167	84
Rice	17641.4	90.6	10.3	94	47	19	9
Sorghum	33095.8	88.8	12.6	264	132	53	26
Beans #1	49403.9	57.5	73.8	13445	6722	2689	1344
Groundnut	50066.4	60.3	65.7	10811	5406	2162	1081
Sunflower	476.6	51.5	94.0	211	105	42	21
Copra	3788.2	46.1	117.0	2594	1297	519	259
Cashew	19229.9	36.3	175.2	29500	14750	5900	2950
Cotton	3177.4	69.9	43.1	295	148	59	30
ANNUAL VALUE IN METICAIS				58051	29025	11610	5805
ANNUAL VALUE IN DOLLARS				60.47	30.23	12.09	6.05
20-YEAR NPV AT 10 PERCENT				514.8	257.4	103.0	51.5

Commodity	1986 PROD (PAAD)	-OFFICIAL-- 1986 MKTD	1989 MKTD	1989 EST'D PROD&&	1989 PARITY P.P.***	1989 VAL PROD	1989 ACTUAL PRICES
Maize	460.0	21.5	80.1	587.6	126.51	74.3	110
Rice	93.0	19.0	22.3	110.3	160.00	17.6	145
Sorghum	267.0	0.7	2.9	309.3	106.99	33.1	95
Beans #1	97.0	2.8	14.9	123.6	399.68	49.4	230
Groundnut	102.0	0.9	2.1	118.5	422.58	50.1	255
Sunflower	1.0	1.0	1.6	1.8	267.73	0.5	138
Copra	29.0	28.4	12.5	17.5	217.03	3.8	100
Cashew	40.0	40.2	50.1	55.9	343.95	19.2	125
Cotton	11.0	10.8	10.8	12.7	250.43	3.2	175

*At a market exchange rate of 960 meticais per dollar.
**1986 production increased by 15 percent plus the difference between marketed production in these two years.
***These prices are calculated elsewhere, and are 1989 producer prices derived using a market exchange rate of 960 meticais per dollar, estimated border prices, and an adjustment factor between border and producing areas.

Marketed Production by Provinces
1981/1989

(Metric Tons)

Commodity	Year	Cabo Delgado (a)	Nampula (b)	Zambezia (c)	Total (a+b+c)	Niassa (d)	Tete (e)	Manica (f)	Sofala (g)	Inhambane (i)	Gaza (j)	Maputo (l)	National (a...l)
Maize	1981	3,541	4,639	25,647	33,827	7,068	21,494	8,294	1,129	523	4,103	1,884	78,322
	1982	8,036	6,546	20,539	35,121	17,468	25,623	6,957	145	60	1,258	2,519	89,151
	1983	5,026	5,951	17,725	28,702	15,700	6,221	3,017	109	105	1,619	130	55,803
	1984	11,151	13,263	27,146	51,560	15,470	12,990	1,062	112	805	582		82,561
	1985	9,534	9,821	14,150	33,505	7,798	4,466	5,698	1,390	555	2,939	2,230	58,581
	1986	5,878	3,979	2,413	12,270	1,160	1,436	4,535	306	171	1,154	442	21,474
	1987	7,769	7,368	582	15,717	1,858	268	6,105	686	322	1,726	529	27,331
	1988	8,633	7,981	2,189	18,803	4,138	1,854	10,496	2,512	126	2,516	4,132	44,579
	1989	18,363	17,600	6,630	42,593	6,427	4,007	15,769	1,651	1,166	1,358	6,774	79,767
	Prev 1990	20,000	20,000	9,500	49,500	6,580	7,000	10,000	2,000	1,200	2,000	5,000	91,290
Rice	1981	377	645	1,650	2,672	91			281		25,124	692	28,860
	1982	527	976	658	2,161	82			85		38,614	600	41,542
	1983	1,139	1,736	201	3,076	41			25		14,126		17,268
	1984	1,064	2,295	1,346	4,705	54			36	19	14,272		19,088
	1985	640	1,269	1,904	3,813	34	1	2	407	20	13,567	50	17,894
	1986	512	908	868	2,288	17	3	6	232	3	16,465	2	19,016
	1987	258	3,099	372	3,729	9		1	121	9	27,000	718	31,587
	1988	96	1,277	328	1,701	36		19	304	4	28,049	1,612	31,725
	1989	420	4,000	2,660	7,080	348		23	280	2	12,866	1,728	22,327
	Prev 1990	600	4,500	3,000	8,100	250			300	10	12,500	1,800	22,960
Sorghum	1981	216	167	205	588	18	205	57	56			53	977
	1982	630	516	43	1,189	72	165	47	44			44	1,561
	1983	675	510	52	1,237	17	7	38	15				1,314
	1984	546	1,203	223	1,972	7	98	5	67				2,141
	1985	695	777	75	1,547	8	173	14	57	10	3		1,812
	1986	273	238	3	514	6	111	13	22	2	4		672
	1987	272	195	11	478	6	1	22	5				512
	1988	345	292	62	699	81	34	43	23				880
	1989	1,614	800	105	2,519	39	197	69	123				2,947
	Prev 1990	1,300	900	100	2,300	20	150	100	150				2,720
Cassava (Dry)	1981	1,058	2,603	6,444	10,105	85				639			10,909
	1982	2,160	2,738	3,873	8,771	495		1			239		9,506
	1983	2,022	3,445	2,625	8,092	428	4			18			8,542
	1984	485	1,690	1,226	3,401	57		3		50	1		3,512
	1985	450	4,295	1,294	6,039	94	8	5	59	145	17		6,367
	1986	485	3,806	1,285	5,576	171		17	12	210	20		6,006
	1987	1,637	4,971	345	6,953	113		100		104			7,270
	1988	4,910	7,080	244	12,234	68			2				12,304
	1989	420	4,100	1,500	6,020	76	45						6,141
	Prev 1990	4,500	8,000	2,000	14,500	200	50						14,750

Marketed Production by Provinces
1981/1989

(Metric Tons)

Commodity	Year	Cabo Delgado (a)	Nampula (b)	Zambezia (c)	Total (a+b+c)	Niassa (d)	Tete (e)	Manica (f)	Sofala (g)	Inhambane (i)	Gaza (j)	Maputo (l)	National (a...l)
Beans	1981	139	405	10,448	10,992	2,195	1,463	106	62		52	9	14,879
	1982	230	756	1,406	2,392	3,636	707	16			119	3	6,873
	1983	451	902	843	2,196	2,185	208	128			7		4,724
	1984	251	1,028	1,007	2,286	815	255	1		59	133		3,549
	1985	458	1,359	561	2,378	564	140	10		80	440		3,612
	1986	512	1,330	138	1,980	321	77	15		126	294	8	2,821
	1987	1,588	6,141	80	7,809	1,129	12	17	3	33	151	51	9,205
	1988	522	2,090	769	3,381	773	935	9	7	1,646	240	155	. 7,146
	1989	4,335	7,000	655	11,990	1,764	733	60	2	13	307	10	14,879
	Prev 1990	4,500	7,500	1,000	13,000	1,050	800	80		30	500	100	16,160
Groundnuts	1981	250	4,506	106	4,862		3	72	15				4,952
	1982	15	1,393	26	1,434		1	7		1		10	1,453
	1983	61	592	12	665	1	2						668
	1984	84	1,919	26	2,029	11	3				1		2,044
	1985	393	1,606	9	2,008	1	3			2	5		2,019
	1986	231	624	1	856	1	2	2		8	9	5	883
	1987	150	1,961	1	2,112		1			13		4	2,130
	1988	73	1,634		1,707					2	1	95	1,805
	1989	10	2,050		2,060							1	2,061
	Prev 1990	365	2,400		2,765							10	2,775
Sunflower	1981	934	4,707	1,501	7,142	2,593	316	1,141	640	46	18	184	12,080
	1982	577	5,930	586	7,093	2,879	178	329	297	4	5	15	10,800
	1983	383	3,147	791	4,321	2,675	89	109	55	14	6		7,269
	1984	220	2,499	272	2,991	1,803	116	18	60	26	4		5,018
	1985	84	4,178	95	4,357	971	60	40	18	2	1		5,449
	1986	66	568	120	754	81	10	157	12				1,014
	1987	65	833		898	35		124	5				1,062
	1988	16	452	112	580	52		308	7	75			1,022
	1989	19	1,100	8	1,127	87		252	1	177			1,644
	Prev 1990	50	1,200		1,250	100		300		200			1,850
Copra	1981			50,375	50,375					4,024			54,399
	1982			34,972	34,972					1,645			36,617
	1983			29,085	29,085					1,133			30,218
	1984			23,410	23,410					1,426			24,836
	1985			22,234	22,234					1,180			23,414
	1986			27,434	27,434					966			28,400
	1987			23,919	23,919					1,614			25,533
	1988			19,277	19,277					3,537			22,814
	1989			11,187	11,187					1,318			12,505
	Prev 1990			20,000	20,000					2,000			22,000

Marketed Production by Provinces
1981/1989

(Metric Tons)

Commodity	Year	Cabo Delgado (a)	Nampula (b)	Zambezia (c)	Total (a+b+c)	Niassa (d)	Tete (e)	Manica (f)	Sofala (g)	Inhambane (i)	Gaza (j)	Maputo (l)	National (a...l)
Cashews	1981	2,300	66,500	11,400	80,200				1,500	7,900	2,400		92,000
	1982	700	46,200	8,300	55,200				100	500	800		56,600
	1983	300	13,700	1,700	15,700				100	100	900		16,800
	1984	600	17,100	1,600	19,300					1,300	4,600		25,200
	1985	600	20,200	3,700	24,500				500	1,900	2,200		29,100
	1986	1,068	21,996	2,966	26,030			9	94	6,474	6,852	710	40,169
	1987	742	23,400	1,141	25,283				297	5,170	6,480	305	37,535
	1988	745	23,700	1,840	26,285				256	7,700	9,100	300	43,641
	1989	2,971	30,500	2,015	35,486				74	2,300	4,170	48	42,078
	Prev 1990	500	20,000	2,000	22,500				50	3,000	2,500	50	28,100

SOURCE: AGRICOM - Alguns Extractos sobre a Comercializacao Agricola entre 1981 e 1988

CIP Demand Analysis

Total demand for transportation equipment and other commodities is difficult to obtain due to the security situation. However, recent surveys of farmer and transporter needs by Entreposto. the Mercedes dealer, and Tecnica Industrial, the Mitsubishi dealer, indicate that the demand for transport equipment in the three northern provinces (Zambezia, Nampula and Cabo Delgado) significantly exceeds available program funding. Although transport availability continues to be a major constraint to production and marketing in these provinces, the demand for commodities reflected here probably has been dampened by the security situation.

Table E1
Demand For Transport Equipment

Commodity	Estimated Demand	Dealer Value	Province			
TRANSPORT EQUIPMENT			Total	Zambezia	Nampula	Cabo Del
8 Ton Trucks	$8,916,100	$54,700	163	50	95	18
9 Ton Trucks	$4,605,600	$60,600	76	8	40	28
10 Ton Trucks	$1,900,800	$86,400	22	8	10	4
12 Ton Trucks	$6,930,000	$99,000	70	6	39	25
20 Ton Trucks	$378,000	$75,600	5		4	1
25 Ton Trucks	$300,600	$100,200	3		2	1
Boat Motors						
15 Hp	$48,000	$600	80		55	25
25 Hp	$80,000	$1,000	80		55	25
50 Hp	$20,000	$2,500	8		6	2
Marine Eng. Spares Caterpillar	$800,000			$200,000	$400,000	$200,000
T O T A L	$23,979,100					

In addition to considering the data provided by the two major importer-distributors, Mission staff have interviewed farmers, transporters and traders, Ministry of Agricultural officials, and other provincial officials regarding the transport needs of the private sector transporters, traders, and farmers in each of the provinces. These interviews indicated a greater demand for some items, such as the 20- and 25- ton trucks, than is indicated in the surveys from the dealers. However, since the equipment dealers will be importing the commodities and will assume the risk for their sale, their demand projections are given greater weight.

Annex F

Letter of Intent

República Popular de Moçambique
Ministério da Cooperação

Maputo, July 3, 1990

Mr. Julius Schlotthauer
Director
USAID Mozambique
Maputo

Dear Mr. Schlotthauer:

The Government of the People's Republic of Mozambique greatly appreciates the continuing assistance of the United States, particularly your support for the development of Mozambique's food and agriculture sector. The purpose of this letter is to update the Government's policies and objectives in the food and agriculture sector, in order to ensure the continuing timely and effective integration of USAID's economic assistance with the Government's Economic and Social Rehabilitation Program.

This letter builds upon its forerunner of August 31, 1989, and upon the agreements reached between USAID and the Government of the People's Republic of Mozambique on the P.L. 480 Title II Section 206 Programs for 1989 and 1990. All measures of those agreements remain in full force and, together with this letter, constitute the full range of policy issues agreed upon by USAID and the Government in the food and agriculture sector. The joint Government of Mozambique - USAID Working Group on Food and Agriculture Policy which was established pursuant to those agreements continues to provide a forum for coordination and regular review of progress toward achieving the Government's objectives in this sector.

The Government's Economic and Social Rehabilitation Program (ESRP), as described in the Policy Framework Paper for 1990-92, sets forth the Government's development strategy for the next three years. The strategy focuses on the recovery of the agricultural sector, particularly the family sector where poverty is severe and the potential for growth is high. Key elements of the strategy are continued improvement of price incentives to producers, improved agricultural support services and markets for their products, and efficient marketing of consumer goods in rural areas. To achieve these objectives, the Government will seek to revitalize the commercial distribution system, particularly private trade networks, and to rehabilitate transport infrastructure. Overall, the Government is working to create an economic environment that favors an increased role for the private sector, imposes financial discipline on public enterprises, and gives the exchange rate, prices, and interest rates the central role in resource allocation.

A.V.

This letter focuses on four areas of agricultural policy that support the overall ESRP framework, and which were established as a basis for USAID cooperation with the GPRM in the Government's letter of August 31, 1989. These areas are: marketing and pricing policy, restructuring of state farms, private sector networks for agricultural inputs sales and services, and foreign exchange allocation mechanisms. Following is a summary of progress made in these areas in the past year, and of intended policy measures for 1990 and 1991.

In the area of agricultural marketing and pricing policy, our objectives remain to increase agricultural productivity and strengthen competitive markets. Policy changes in 1989/90 significantly increased the role of the market in sending price signals to producers. Nearly all agricultural products have moved from fixed producer prices to a producer floor price system, retaining fixed prices only for maize, rice, and sugar. Both floor prices and the remaining fixed prices reflect import/export parity, and were announced in advance of the planting season. The impact of these measures is being reflected in reports of good harvests in secure zones throughout the country, although erratic rains have caused disappointing crops in some areas, particularly for rice.

During 1989/90, the Government and USAID had jointly undertaken to conduct a comprehensive analysis of production factors in the agricultural sector. Through extensive discussions in our joint Working Group, it was agreed that the most useful approach to completing such an analysis would be in the context of a longer-term research effort. A detailed analytic program has now been defined with Michigan State University. Research work is expected to begin by October 1990. The Government will nominate at least three counterparts to participate in each stage of the research and analysis program.

In 1990/91, the Government intends to proceed with phased price deregulations. Domestically produced maize was moved in June 1990 from a fixed producer price to a producer floor price. In September 1990 the Government will also introduce a minimum producer price for rice. All other producer floor prices will be readjusted based on import/export parity. The new agricultural price regime will be announced in September 1990, so farmers can make planting decisions which take price incentives into account.

A.V.

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To reinforce improved production incentives, the Government will emphasize complementary changes in marketing policy in 1990/91. A key measure announced in June 1990 is the liberalization of the consumer price of domestically produced maize, leaving the producer floor price as the only administratively determined price in the production and marketing chain for maize. This policy change effectively eliminates financial disincentives under the earlier fixed price regime to private participation in maize marketing, and will encourage competition among traders to the benefit of producers and consumers. The Government, with USAID support, will evaluate by June 1991 the impact of deregulated domestic maize prices, taking into consideration: the effect on prices throughout the production and marketing chain, incentives provided for private commercial trade, the extent of reduced budgetary burden on AGRICOM, and, to the extent that they can be obtained, indicators of quantities marketed. Should the results prove positive, the GPRM plans to extend its experience with maize liberalization to beans and eventually rice.

Planned relaxation of administrative restrictions on agricultural trade will further encourage marketing of agricultural commodities and help revitalize private trade networks. The Government will, by September 1990, eliminate administrative regulations hindering free inter-district and inter-provincial movement of agricultural commodities, and will open district-level wholesaling opportunities to any licensed trader desiring to compete. These measures, to be enacted and announced through the appropriate Government legal channels, will facilitate the flow of commodities from surplus to deficit areas, allow new entrants to compete in supplying consumer goods to the rural population, and improve the competitive environment for rural trade. In addition, the Government will analyze licensing requirements for private marketing agents (transporters, wholesalers and retailers) to assess potential barriers to entry. The Government will review this analysis with USAID by February 1991, allowing agreed upon recommendations to simplify licensing requirements to be implemented later that year.

Government policies in land distribution and tenure security have undergone rapid evolution during the past year, and continue to develop. Our objective is to increase the economic use and productivity of agricultural lands by developing land use policies and constitutional reforms which will enhance land tenure security overall and encourage investment in agriculture. In the context of this objective, the Government reaffirms its intent to restructure state farms where appropriate and to divest other state farm holdings to family and commercial operators.

A.V.

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In 1989/90, work on an Action Plan for state farms restructuring and divestiture advanced. On a case-by-case basis, many divestitures of state farms were authorized and have been implemented. At present, the total number of state farms is just 72, having been reduced from a total of 150 in 1987. In 1990/91, the Government, with USAID assistance, will deepen the analysis of divestiture issues through further study of land tenure security in general, and through the detailed planning and implementation of at least one pilot divestiture of state farm land to family farmers. Through the joint GPRM - USAID Working Group, a research and analysis plan has been developed for the Land Tenure Center at the University of Wisconsin. Field work is expected to begin in October 1990. Also in 1990/91, the Government intends to complete a statement of policies and guidelines for encouraging land use in support of increased agricultural productivity, as guidance for the various authorities involved in land allocations and particularly divestitures.

Another objective of the Government's agricultural development strategy is to enhance the reach, competitiveness, and viability of networks providing agricultural inputs and services to farmers nationwide. The Government recognizes that implementation of the USAID Commodity Import Program through private importers and distributors has effectively supported this objective. In 1989/90, the Government ceased to administratively allocate USAID-financed imports to end users, allowing participating importers and distributors to determine the types and quantities of various commodities needed by their eligible clients. To ensure wider distribution of the program's benefits a limit was retained of one tractor and truck per client. In 1990/91, the Government intends that private import and distribution channels will handle all USAID-financed commodity imports, again retaining the annual limit per client. As a step in further encouraging the development of effective agricultural support services, the Government also intends in 1990/91 to identify and analyze a number of agriculture-related parastatal enterprises for possible divestiture to private operators. Depending on the technical requirements for the analysis, the Government may request USAID support for technical assistance.

A.V.

It should, finally, be noted that foreign exchange allocation policy has evolved to complement and reinforce the emergence of productive private enterprises and trade networks. Our principal objective in this area continues to be to expand and ease access to foreign exchange for necessary imports for productive enterprises and activities. The mechanism for pursuing this objective is a market-based system under which foreign exchange and import licenses are automatically available to any enterprise working in eligible sectors. In this way, the demand for foreign exchange will be increasingly influenced through adjustments in the exchange rate, tariffs, and taxes, including customs duties, eliminating the need for administrative restrictions.

Experience under the system for non-administrative allocation of foreign exchange (SNAAD) established by the Government in 1989 has been generally positive. The enterprises utilizing the SNAAD to date have been overwhelmingly private sector ones. Sales to end users are market driven rather than administratively determined. Some adjustments in the program have already been made based on early applications, such as the discontinuation of the dollar ceiling per client. The Government is seeking additional donor resources to permit the planned expansion of this system to additional productive sectors. In May 1990, the Government announced the expansion of the SNAAD to include agricultural inputs such as selected parts and spare parts as described in the Ministerial Decree dated May 14, 1990. Further expansion to include other agriculture inputs and other sectors will depend on the level of donor resources mobilized for the SNAAD and on a rigorous evaluation of the SNAAD's performance to be conducted in June-August 1990.

In conclusion, the Government confirms its intention to pursue the food and agriculture sector policy objectives identified in the PFP and in the specific USAID agreements cited above. We intend to take significant steps in 1990/91 toward achievement of these objectives. These actions will in large part depend on USAID's continuing support, both financial and technical, in this sector. We look forward to continuing our close and productive collaboration.

Sincerely,

Jacinto Veloso

Jacinto Soares Veloso
Minister of Cooperation