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Managing food security risks and intra-regional trade in Africa

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The problem

The role of intra-regional trade in managing food price risks in Africa is being discussed in various *fora*. In response to high food prices, many countries adopted ad-hoc measures to restrict and/or prohibit trade with neighbouring countries. With policy makers, civil society organizations, development partners and other stakeholders as target audience, the brief shows that regional trade can reduce domestic food price volatility by shifting food staples from areas where local markets are unable to absorb surplus production to food deficit regions.

Key messages

- Increased intra-regional trade in food staples can play a significant role in reducing domestic food price volatility.
- Incentives to greater private sector investment in the market and value chain developments required to facilitate intra-regional trade have been depressed by a number of factors including significant increase in imports from extra-regional sources, and the use of ad hoc trade and market policy interventions in an attempt to manage food security risks
- Significant efforts need to be made to increase the confidence of governments to place greater reliance on market based instruments at the same time as ensuring that food security objectives are met, and to convince private sector stakeholders that such change is credible and will be sustained.
- Strengthening evidence on the merits of market based instruments, facilitating improved dialogue and supporting public-private partnerships for investment in transport and communication infrastructure to reduce transport costs and improve access to information, strengthening regulatory frameworks to promote competitiveness, and developing the capacity of involved stakeholders to advocate for policy interventions conducive to market and intra-regional trade development, are imperative.

1. Regional trade and price risk management

Regional trade can help to reduce domestic food price volatility by shifting food staples from areas where local markets are unable to absorb surplus production to food deficit regions. Regional trade effectively expands the size of the market, and where it is occurring, regional trade in SSA has contributed positively to the region's food security situation, with neighbouring countries essentially pooling production through trade to help to stabilize local markets. This is particularly important in regions reliant on rainfed food staples and which are susceptible to climate risk and associated production shortfalls or bumper harvests.

The fact that rainfall patterns differ within regions of the African continent means that trade between countries within these regions can adjust quantities available and thereby smooth prices, reducing the level of downside price risks faced by producers. Reduced price risk helps to sustain initiatives aimed at productivity increases by creating more stable producer incentives and strengthening the level of market integration of smallholder producers, including women farmers. This is critical in increasing smallholder participation in markets, a precondition for their adoption of productivity enhancing technology and related investments.[1]

2. Why is intra-regional trade in food staples limited?

The fact that formal intra-regional trade still accounts for less than 10% of total trade in food staples suggests that its contribution to mitigating price risks could be far greater.

A key determinant of increased intra-regional trade is sustained private sector engagement and associated investments in market development. However, levels of engagement and investment have been muted as a result of uncertain business environments. Although price variability is often driven by climatic events, a number of factors including the price depressions associated with rapid increases in import volumes, weak and often uncompetitive performance of market structures etc exacerbates the trade related risks that governments face. Such factors, and the ad hoc use of trade and market interventions in an attempt to manage national food availability and/or food prices in imperfectly functioning markets, has created significant uncertainty, suppressing private sector actors' investments in market development and reducing their engagement in formal cross border trade. In turn, this has exacerbated these price related shocks and further reduced private sector investment.

In many situations ad hoc interventions can be attributed to government concerns over the food security and nutrition related risks of increased trade, and the limited confidence that they have in the private sectors to operate in a way that mitigates trade related risks. For example, concerns about the food balance situation may result in government restricting exports at short notice.[2] However, if private sector exporters have already entered into contracts to supply a commodity to buyers in an importing country, these restrictions can result in significant losses (both financial and reputational) and reduce the willingness of the exporters to enter into such contracts in the future and therefore the likelihood that they will invest in market related infrastructure (including storage infrastructure) required to expand volumes of trade.

Many governments are concerned about their ability to source food staples regionally.

There is generally limited information as to the physical availability of staples at any given point

1 See, for example FAO (2013). *Smallholder Integration in Changing Food Markets.*

2 The primacy of national food security and longer term development objectives in influencing trade and related market policy interventions has been longstanding in many African countries and pre-dates the current global context of increased food price volatility (see for example, Sarris, A. and Morrison, J. (eds.). FAO and Elgar (2010). *Food Security in Africa* and Morrison J. and A. Sarris (2010). *Trade and market policy interventions: a synthesis of insights from research on Eastern and Southern African grain markets*. In Sarris, A. and Morrison, J. (eds.) (2010). *Food Security in Africa*. FAO and Edward Elgar). The current context has however re-ignited debate on the role of government interventions in reducing levels of food price volatility (see for example, Dawe, D. and Timmer, P. (2012). *Why stable food prices are a good thing: Lessons from stabilizing rice prices in Asia*, Global Food Security, Vol 1, Issue 2).

in time meaning that countries often do not know whether sufficient product will be available for importation when and where needed. Similarly, governments may be concerned about their ability to use regional trade to control upside price risk which can be to the detriment of domestic consumers of food staples, particularly in the current era of high and more volatile international prices. They may also be concerned about their inability to prevent rapid shifts of informally traded staples across borders and which might result in local food deficits.

Strategic grain reserves have received renewed attention in many countries as one of the public instruments that could assist in stabilizing prices . In Middle East and North African countries, the accumulation of stocks is considered as a more efficient strategy than the pursuit of self-sufficiency, mainly because most countries have limited potential for expanded agriculture.[3] National food security stocks are also attractive in landlocked countries where transport costs can be high and can also rise sharply in the event of an urgent requirement to transport large quantities over long distances. In general, humanitarian stocks with narrowly defined target groups and efficient management to minimize leakages can be justified, but the danger is that targeting is often imprecise or the target group is too wide and the risk of a leakage into local markets needs to be taken into account.[4]

In Africa, it is not just at the border that ad hoc policy intervention can create uncertainty. Where intervention in buying and selling does not adhere to announced prices or to announced purchase and selling patterns, it can create considerable uncertainty for private sector investors.[5] Intervention buying can also create difficulties in ensuring that stocks are held in the optimal location to allow redistribution to deficit areas in time of need. Given the increased attention that is being given to establishing national or regional food stocks, public sector intervention in domestic markets needs to be cognizant of these difficulties.[6]

Public sector interventions which seek to achieve legitimate food security objectives need not dampen incentives for private investment in precisely the types of institutional and infrastructural development that are required to allow governments to eventually reduce their levels of intervention. A public-private partnership approach can help to make sure that private sector investment in the food value chain is not hampered. In Asia, the use of light government interventions and procurement has resulted in efficient private sector participation in rice market and trade.[7]

3 Wright, B. and Cafiero, C. (2010). *Grain Reserves and Food Security in MENA Countries, AfDR.*

4 Gilbert, C.L (2011). *Food Reserves in Developing Countries: Trade Policy Options for Improved Food Security*, ICTSD, Issue No. 37, September.

5 This is often in sharp contrast to Asian governments' actions to stabilize prices (see for example Dawe and Timmer, (2012)).

6 See for example ICTSD & FAO (2013). *G-33 proposal: early agreement on elements of the draft Doha accord to address food security.*

7 Gilbert, C.L (2011). *Food Reserves in Developing Countries: Trade Policy Options for Improved Food Security*, ICTSD, Issue No. 37, September.

The unpredictable nature of international markets, trade flows and policy implementation has often prevented the private sector from taking forward positions, has reduced private sector willingness to invest in and use market institutions/infrastructure, and has suppressed incentives for storage, a precondition for price smoothing. Limited investments in market institutions and market infrastructure development is apparent in the fact that market based mechanisms such as Warehouse Receipt Systems, Commodity Exchanges and Market Information systems which could facilitate price discovery and thus reduce price volatility, have had limited success in the region. High costs of commerce, the difficulty in financing carryover of stocks and a lack of confidence in contract enforcement and delivery have all been cited as contributing factors to limited intra-regional trade.

3. Towards a solution

A shift to a more structured, market based approach to trade in food staples would, however, require a substantive change in the way in which many African governments currently use trade and market policy instruments to manage food staples availability and/or price stability. Many governments are well aware that their actions in pursuit of short term food security objectives are detrimental to longer term goals of market development, but they lack the confidence to rely upon markets and on trade based approaches in ensuring that these objectives are met.

In building the confidence of governments to place greater reliance on market based approaches and increased economic integration, enhanced dialogue, cooperation and coordination are essential, not only within different government ministries but with key stakeholders, including the private sector, civil society, regional organizations as well as other governments in the region. Such dialogue is important in moving towards agreement on regulations to ensure improved conduct of markets required for the effective use of market based instruments. Removing regulatory barriers to trade and competition along the value chain can significantly reduce asymmetries in market power, benefit farmers, enhance regional food trade and improve the management of food security risks.[8]

In turn, this requires a better understanding of the relative merits of trade and market interventions vis à vis approaches based on market based instruments (MBI) including for example, greater reliance on strengthened market information systems, warehouse receipt systems, commodity exchanges and other risk management institutions; improved monitoring of the actual implementation of trade policy interventions to increase transparency; and improved capacity of all stakeholders to engage in constructive debate.

Given the inadequate investment in such institutions and infrastructure, there is a limited pool of available evidence on the effectiveness of market based instruments, making it difficult to convince policy makers of their merits. Pilot projects across the region suggest that under certain conditions, the benefits are real.

8 Porto, G., Chauvin, D. N., and Olarreaga, M. (2012). *Supply Chains in Export Agriculture, Competition, and Poverty in SubSaharan Africa.* World Bank and CEPR; Engel, J and Jouanjean, M,A (2013). *Barriers to trade in food staples in West Africa: an analytical review.*- ODI Report, July.

For example, the nascent commodity exchanges such as the Agricultural Commodity Exchange for Africa, Zamace, and the Ethiopia Commodity Exchange have all demonstrated that with the appropriate support and policy environment, such instruments can function.

Increased reliance on market based instruments does not mean that there is no role for trade and market policy intervention. Governments in many developing countries have a role in managing increases in imports from extra-regional sources and in maintaining well-targeted and well-defined strategic reserves, in addition to implementing safety net programs to manage food security risks. However, governments are often constrained, both from a budgetary and administrative capacity perspective from designing and implementing effective and efficient consumer or producer safety nets or support packages that are adequately targeted to achieving their social objectives. Trade policy, although a blunter instrument, can however be more effective in meeting agriculture sector objectives and will continue to be an important risk management instrument both in ensuring food security and in facilitating longer term market development.

Trade policies have often been inappropriately used in attempting to achieve multiple objectives, often with significant conflicts between their use as short term responses to food shortages or high food prices, as opposed to their use in stimulating longer term development. Critical will be determining how trade policy can be better used in achieving the government's objectives without having detrimental effects on market development and, where necessary processes of market reform.

A short sharp shock that seeks to radically change a country's trade policy set is however, likely to induce backsliding. In shifting to a rules based approach to intervention that is supportive of the use of market based instruments, a number of aspects require consideration: (i) determining required changes in the structure and conduct of markets within which the private sector operates, (ii) determining the transition path to greater reliance on market based instruments in the context of more stable and transparent trade policy, and (iii) building the confidence of public and private sector stakeholders to make the transition to a credible policy environment.

A key difficulty in determining the appropriate set of rules for intervention during the transition is that the analysis of the impacts of different types of market interventions is problematic due to: (i) weak data, particularly on the level of informal trade and on actual policy implementation, and (ii) the difficulty of defining causal relationships between policy interventions and indicators of interest, such as levels of food insecurity.

A transition to a rules based approach, which essentially constrains the policy options available to governments, requires that they have increased confidence that they will be able to ensure food security related objectives through a more nuanced use of both public sector interventions and market based approaches. Increasing confidence requires strengthened evidence on the merits of alternative market based instruments and regulations in different contexts and at different stages of the transition path to a less discretionary policy environment, and on the appropriate blend of policy and market instruments during this transition, in addition to improved dialogue and capacity development to generate stakeholders' willingness to adopt these instruments.

Improved dialogue between the involved stakeholders will be critical.[9] Many actors have a stake in policy decisions and that many organizations are contributing to policy debates, but often this dialogue is insufficiently coordinated Key areas for further research and dialogue include evidence on the contribution of increased intraregional trade in reducing domestic market price volatility; the extent to which discretionary trade and market policy interventions undermine regional trade; the relative merits of different types of market based instruments in mitigating price volatility and in improving staples food availability; and the extent to which these instruments can be designed to adapt to discretionary policy interventions.

9 An example of such an initiative is the Agricultural Trade Policy Advisory Forum. Launched in Nairobi in May 2012, the ATPAF-ESA is an informal network of research institutes, international and regional organisations, and private sector and government institutions. The Forum provides a platform that builds on and strengthens existing initiatives aimed at improving the policy environment consistent with enhanced intra-regional trade in food staples.

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