

FAO Briefs on Import Surges

- Countries

No. 7
Kenya: dry
milk powder,
sugar,
maize¹



February 2007

SUMMARY

- Import surges of three agricultural commodities – dry milk powder, sugar and maize – were raised as a serious issue by stakeholders after the mid-1990s. The surges coincided with liberalization of trade policies in Kenya.
- While surges occurred for all three commodities, it is difficult to conclude that liberalization was the primary cause of the surges. Rather, internal factors in Kenya contributed significantly to the rises in imports, including lack of capacity to cope with seasonal supply shortages caused by weather conditions, lack of smooth transition to market liberalization and administrative difficulties in handling imports.
- The analytical capacity to monitor and respond to import surges is restricted by deficiencies in trade surveillance, in particular access to accurate trade and price statistics. Kenya's increasing participation in regional agreements suggests that this could be a priority area for future trade policy analysis and capacity building.

Introduction

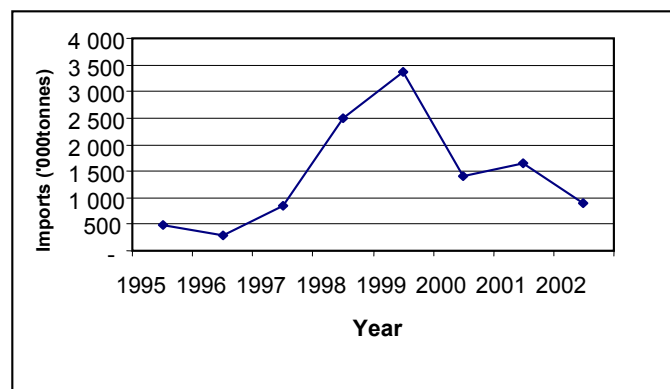
Kenya's crop and livestock sectors are very important in the country's economy, accounting for about 25 percent of the GDP and supporting about 80 percent of the country's population. Powdered milk, sugar and maize are key commodities contributing to the food security of the nation and to the livelihoods of the people; and therefore, an increase in imports of these commodities needs to be carefully analyzed and well understood.

This brief summarizes the key findings of analysis of import surges of these three commodities in Kenya. It aims to document the surges, to identify the reasons for the surges, to assess the injury impact of the surges, and to determine their causality.

Identification of import surges

There are two categories of **dry milk powders**: dry whole milk powder and dry skim milk powder. Dry milk powder in general accounts for 44 percent of Kenya's total volume and value of milk imports, which include also milk cream, infant milk, butter and raw milk. Dry milk powder is a substitute product to raw liquid milk produced and marketed domestically. Figure 1 shows imports of dry milk powder from 1990 to 2002. Notable increases occurred in the mid 1990s and from 1998 to 2001. Between 1995 and 2002, imports exceeded the previous three-year moving average by at least 30 percent in 1995, 1998, 1999 and 2000.

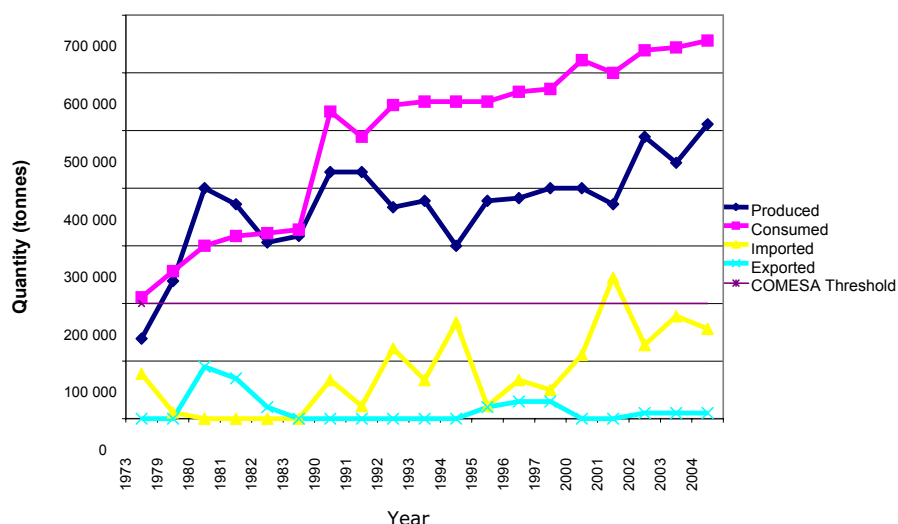
Figure 1. Kenya - imports of dry milk powder (skim and cream)
1995 – 2002



Source: Mbwika, *et al* (2005) and Kenya Dairy Board (KDB)/
Kenya Revenue Authority (KRA) Records

¹ Case studies prepared by national experts.

Figure 2. Trends in Kenya's sugar production, consumption and external trade, 1973-2004



Source: KSB Yearbook, 2005

According to the Kenya Sugar Board, nearly 6 million people derive their livelihoods from the **sugar** industry, either directly through sugarcane production, sugar manufacturing and distributive activities, or indirectly through the allied economic activities. The provision of social infrastructure by the sugar industry is a key component of the corporate responsibility of the sugar millers in Kenya. The sugar milling factories and the sugarcane plantations owned by the factories have employed between 43 000 and 75 000 people in Kenya over the last ten years. The sugarcane industry also contributes significantly to the revenue of both the local authorities and the central government in the form of the value-added tax, sugar development levy and local authority levies.

The production of sugar in Kenya does not meet the domestic demand. Kenya produces about 450 000 tonnes of sugar annually, and the demand for sugar is around 620 000 tonnes. Therefore, the shortfall must be met by imports. Since domestic sugar milling factories produce only raw sugar, industrial users of refined sugar always depend on imports for their manufacturing requirements. The government policy is to meet the shortfall of sugar through imports from COMESA. Currently Kenya allocates a sugar industry safeguard quota of 200 000 tonnes of sugar imports from COMESA, which will expire in 2008. This quota allocation is shared between white raw sugar and white refined sugar.

Sugar imports in Kenya increased from about 65 000 tonnes in 1996 to about 170 000 tonnes in 1998 and to around 250 000 tonnes in 2001 (Figure 2). Kenya appears to have experienced significant increases in sugar imports after the liberalization of sugar trade and the removal of price controls in the country in the 1990s.

Significant surges took place in 2001, 2003 and 2004, possibly coinciding also with increased unrecorded cross-border imports

In recent years, a deficit in the domestic supply of **maize** has been recorded. The deficit has been between 180 000 and 540 000 tonnes annually. The shortfall of maize supply in the country has been met through both recorded and unrecorded cross border trade.

Officially reported maize imports have been increasing from an annual low of 3 percent to an annual high of 12 percent of domestic consumption, reflecting levels of domestic production. Kenya experienced particularly serious surges in 1994, 1997, 2001 and 2004 when imports exceeded the previous three-year moving average by at least 30 percent.

Reasons for the surges

Seasonal milk supply shortages occur during and shortly after the dry periods. Such shortages force local processors to obtain and use **dry milk powders** to meet demand. In the absence of domestic stocks of dry milk powders, imports are required to meet domestic requirements during and after the dry periods.

However, there is some evidence that increased levels of dry milk imports since 1995 were also attributable to other causes. Until 1992, the (old) Kenya Cooperative Creameries Limited (KCC), a semi-private milk processor and seller, benefited from monopoly status. It was the only dairy processing firm in Kenya that had processing facilities to convert raw liquid milk into dry milk powder. In 1992, the Kenyan dairy industry was liberalized, and the old KCC, with no preparation for competition, collapsed in 1997. Soon, new competitors entered the market, and the old KCC lost most of its share in the liquid milk market. At the same time, the old

KCC still owned the infrastructure that the competitors did not have for the collection and cooling of raw milk before processing. Therefore, the old KCC was the only supplier of dry milk powder. Under these circumstances, Kenya experienced rising imports in dairy products, particularly milk powder from the late 1990s to 2002. In 2003, the old KCC was revived by the government and handed over to farmers as a dairy cooperative organization under the name of New KCC, with a new management team. Since then, the amounts of locally produced and processed dairy products have increased substantially, reducing the need for imports. Regional trade agreements, particularly COMESA, could also be a factor facilitating imports of powdered milk.

Increases in imports of **sugar** did not arise directly from price competition. Based on 2004 prices, imported sugar landed in Mombasa at 23.30KSh per kg c.i.f. Importers paid relevant duties and sold the sugar to wholesalers at 48KSh per kg, and consumers pay between 63 and 76KSh per kg, which is in the same price range as sugar produced domestically. Rather, the incidence of sugar import surges in Kenya has been attributed to difficulties in the administration of the duty-free quota allocations. These difficulties cause delays in the timely importation of sugar. Consequently, sugar arrivals and distribution occur when product may no longer be needed. The adverse market impact of official sugar imports is additionally aggravated by unrecorded cross-border sugar imports. Domestic production shortfalls due to periodic drought also prompt sugar imports. Similarly, serious drought conditions were also one of the main reasons for periodic import surges of **maize**. While the increases helped meet domestic market needs, the timing of imports, as for sugar, sometimes had disruptive

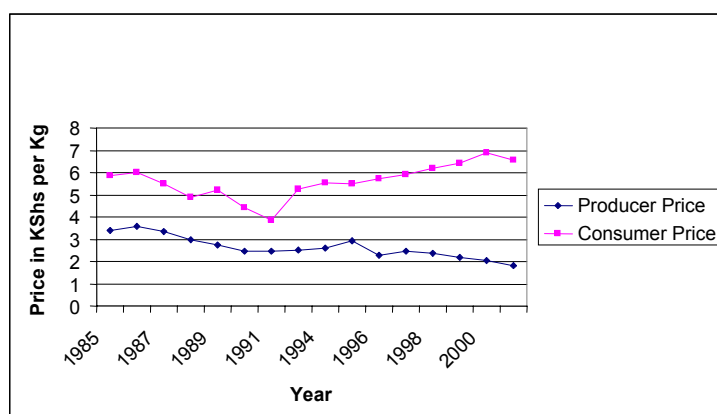
effects on domestic production. Difficulties related to the approval and sanctioning of maize imports on concessionary terms by the government for food security purposes sometimes resulted in delays in the placing and processing of orders. Thus, the imported product entered the country when underlying market conditions had changed.

Evidence of injury

Because **dry milk powder** is a substitute product for raw milk, it can be used in the processing of many other products that are normally processed with raw milk. Thus, the import surges of powdered product in the context of rising domestic demand can have a direct impact on local milk production as well as the demand for fresh, locally produced milk for further processing. Larger imports may have affected the domestic dairy industry in two ways: (i) lowering the farm-gate or producer prices of raw milk, and (ii) reducing the availability of market outlets for locally produced raw milk. In fact, producer prices in real terms tended to decline between 1985 and 2002 (Figure 3) with lower prices providing a disincentive for local small-scale dairy farmers to sustain their dairy production during the period when imports of dry milk powder increased. Stakeholders claim that the depressed prices impacted negatively on the incomes of small-scale farmers who account for about 75 percent of dairy production in Kenya.

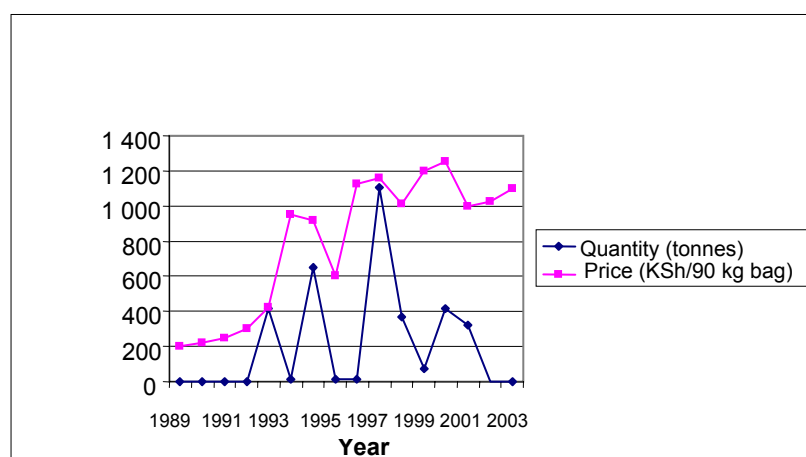
In the **sugar** sector, under the COMESA Sugar Safeguard Protocol, a quantitative restriction on imports into the Kenyan market will expire in 2008, which may facilitate higher imports, potentially causing injury to local sugar farmers. Under current arrangements, however, difficulties in the administration of import quota allocations (from COMESA) delay importation of sugar when needed. The late arrival of imported

Figure 3. Kenya real prices of milk to producers and consumers, 1985-2001



Source: Kenya Central Bureau of Statistics records

Figure 4. Maize imports and price, 1989-2004



Source: Based on National Cereals and Produce Board (NCPB) records

sugar has often caused serious domestic marketing problems in which the local sugar millers ended up with huge stockpiles of sugar with limited outlets. Due to marketing problems, millers failed to pay farmers on time, and local farmers were unable to meet their financial obligations. Meanwhile, millers were unable to make payments to suppliers. Therefore, the whole sector accumulated debts with serious injuries to the entire domestic economy.

High levels of **maize** imports in a given year, depending on the timing of imports, have normally been followed by lower producer prices in the following years. Relatively higher prices coincide with the periods when there are internal maize shortages, requiring commodity imports (Figure 4). The lagged effects of delayed imports could have a negative impact on farm incomes.

As in the case of sugar, late arrivals of imported maize created some marketing problems. Difficulties related to the approval and sanctioning of duty free maize imports for food security purposes led to delays in the placing and processing of the orders. Subsequently, marketing problems and resulting stockpiles limited outlets for local producers at harvesting time. Even when the producers could deliver their maize to the National Cereals and Produce Board (NCPB), NCPB was unable to sell to millers. This marketing problem led to a fall in producer prices. Moreover, the NCPB could not pay for the maize delivered to its depots on time, even when producer prices were relatively lower. The delayed payments to producers reduced their purchasing power to buy farm inputs, which led to poor farm yields followed by the reduction of earnings.

Causality and trade surveillance

Increased imports of dry milk power, sugar and maize are periodically required to supplement domestic production. The disruptive impacts of import surges of sugar and maize seem to be mainly associated with administrative difficulties associated with implementation of trade protocols. For all three commodities other domestic factors having an impact are poor domestic infrastructure and lack of appropriate technologies for storing and processing domestically produced products. Weakness in the import surveillance system has been exacerbated by the influx of unrecorded food products, unofficially imported into the country through porous border points.

Concluding remarks

Analysis indicates that import surges were caused more by domestic factors than by external ones. For example, in the dairy sector, management difficulties of the KCC and its collapse were the primary factors for the import surge in the late 1990s. In both the sugar and maize sectors, administrative problems for managing imports caused late arrivals, which subsequently resulted in marketing problems. The delayed arrivals had negative spiral effects on producers: some injury effects were followed by prolonged import increases. However, data limitations make it difficult to determine the real injury impact caused by the import surges. Strengthening of the national trade surveillance system is essential to obtain a better understanding of the short and longer term problems caused by surges in imports of agricultural commodities, especially for a country like Kenya that has porous border points with neighbouring countries.