



## Improving incentives to expand wheat production in Ethiopia

### Main Findings and Recommendations

Government policies and inadequate access to markets have resulted in relatively low prices for wheat producers, especially between 2005 and 2007. Although price incentives improved in 2008 and 2009, they deteriorated again in 2010.

MAFAP analysis suggests that price incentives for producers could be improved by:

- ▶ addressing the overvaluation of the domestic currency;
- ▶ avoiding non-targeted distribution of grain at subsidized prices;
- ▶ developing market institutions and infrastructure;
- ▶ improving the grain value chain; and
- ▶ promoting bulk transport systems to reduce per unit transport costs.

### SUMMARY

In most of the years analysed, farmers received prices that were lower than what they would have obtained with better market access or more favourable domestic policies (Figure 1). However, farm gate prices started increasing in 2005 and price incentives (relative to international prices) improved following the global food price spikes of 2008. Farmers thus increased production based on their perception of improving prices. However, unfavourable government policies and inadequate market infrastructure are unlikely to foster a sustained increase in wheat production and yields.

### INTRODUCTION

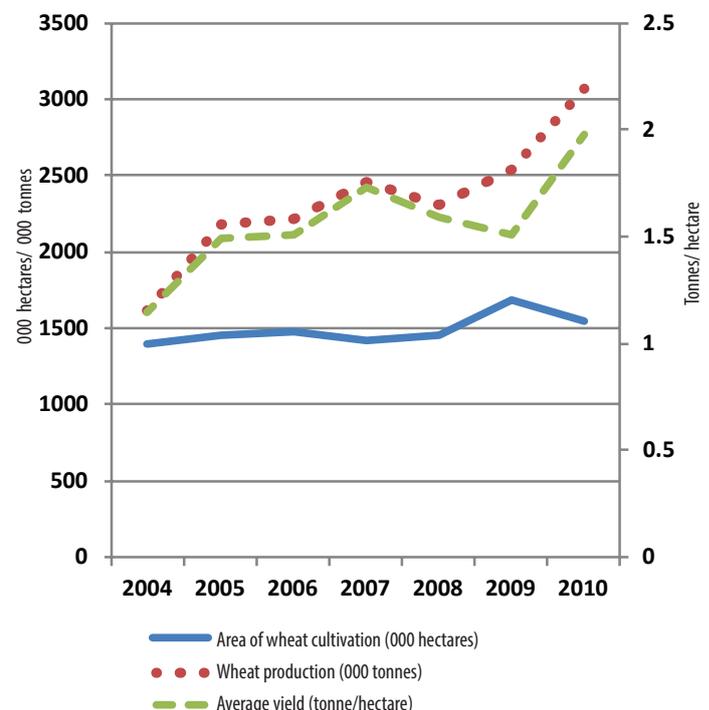
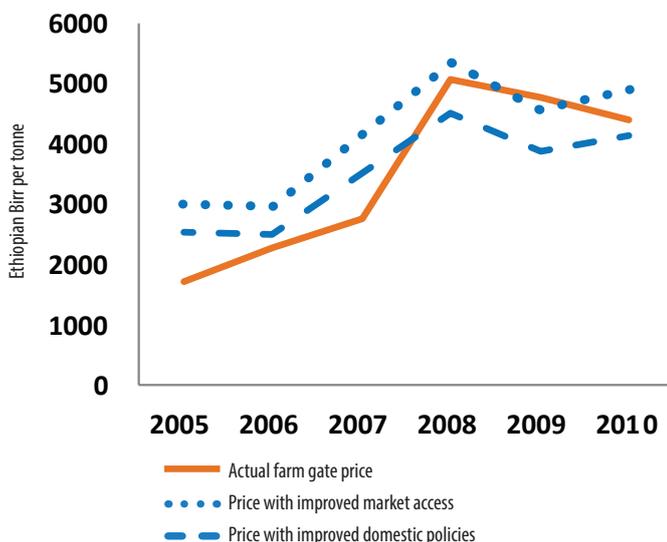
Ethiopia is the second largest wheat producer in sub-Saharan Africa, after South Africa. From 2005 to 2010, wheat production

increased significantly - mainly due to better yields (Figure 2). Nonetheless, wheat yields in Ethiopia lagged behind other major producers in Africa. From 2004 to 2011, the average yield in Ethiopia was 1.68 tons per hectare. This was about 32 and 39 per cent below the Kenyan and South African averages, respectively. Production also fell short of domestic consumption requirements and the country remained a net importer of wheat.

A marked increase in farm gate prices after 2005, improving price incentives (relative to international prices) in 2008 and 2009, expanded extension services and favourable weather

Figure 2. Wheat production and yields in Ethiopia (2004 - 2010)

Figure 1. Farm gate price of wheat in Ethiopia (2005 - 2010)



conditions all contributed to increased wheat production. Wheat's share of total cereal consumption also increased to over 20 percent in recent years, making wheat the second most important cereal consumed in Ethiopia, after maize.

## KEY ISSUES

*Consumer oriented policies have had a strong influence on producers' prices.*

Ethiopia is one of the largest recipients of food aid in Africa. It receives 27 percent of the global food aid going to sub-Saharan Africa, mostly in the form of wheat. The amount of wheat imported by the government also increased significantly in response to the 2008 high food prices. Imported wheat in the form of food aid is often distributed for free in food insecure areas while government imports are sold in urban areas at subsidized prices. While government policies aim at keeping wheat prices low for consumers, there are no policies designed to mitigate the impact of low prices on producers.

*The overvalued exchange rate keeps the price of imported wheat relatively low and makes it harder for local producers to compete with imports.*

The exchange rate in Ethiopia is characterized by 'managed floating' with strong government control. The domestic currency (Birr) was especially overvalued from 2008 to 2010. The overvaluation of the Birr was estimated at 40 percent and the government was finally forced to devalue it by 25 percent in September 2010. The high inflation rate (compared to the relatively low inflation rate among Ethiopia's trading partners) and increasing pressure on foreign exchange reserves help explain currency appreciation. Devaluing the domestic currency further would raise the price of imported wheat, making it easier for local producers to compete.

*Market institutions need to be improved.*

Grain marketing in Ethiopia is characterized by weak institutional support and inadequate infrastructure. With no effective systems in place for identifying grades and standards, existing market information systems are of limited value to farmers and other actors along the value chain. Indeed, producers and traders have difficulty making sound decisions based on price information that does not specify grades and standards. Since mixing different grades of grain compromises quality, the lack of common standards and grades has also hindered the introduction of warehouse receipt systems. Furthermore, trade associations are weak and have limited capacity to regulate themselves; establish and enforce standards; and modernize wheat marketing.

*Improving market and transport infrastructure would increase incentives for wheat farmers to market their produce.*

High transport costs severely impact farmers located far away from wholesale markets (points of competition) such as Addis Ababa. High costs are due to long distances, poor infrastructure, limited processing and the lack of bulk handling and transport systems. Indeed, grain is transported in small trucks at a high cost per unit. Lowering transaction and transportation costs would also help reduce the cost of inputs and support services, and increase farm gate prices. These would help improve incentives for producers to market their products. Currently, only about 21 percent of Ethiopia's total wheat production is marketed.

## CONCLUSIONS

Because of inadequate incentives and low technology inputs, nearly 80 percent of all the wheat produced in the country is consumed on the farm. However, with improved policies and more investment in improving wheat production, Ethiopia would be able to meet domestic demand and export to neighbouring countries. Domestic wheat would be able to compete with imported wheat if policies were more favourable for producers and other operators along the value chain. Promoting the use of more productive inputs and new technologies, reducing marketing costs, and encouraging value addition (for example with additional processing) would make domestic wheat more competitive.

### Further Reading

**MAFAP Technical Note on Wheat in Ethiopia (2012)**

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This note was prepared by the Monitoring African Food and Agricultural Policies (MAFAP) team at FAO. MAFAP is implemented by FAO in collaboration with the OECD and the financial participation of the Bill and Melinda Gates Foundation (BMGF) and USAID. MAFAP supports decision-makers at national, regional and pan-African levels by systematically monitoring and analyzing food and agricultural policies in African countries. This policy brief has received additional support from the European Union through the EU-FAO Improved Global Governance for Hunger Reduction Programme.