MONETIZING FOOD AID
-1993-
A GUIDE FOR PVOS

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for

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Washington, DC

FAM is a Coalition of ADRA, CARE, CRS, Save the Children, and World Vision

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INTRODUCTION

In addition to the classic uses of food aid for maternal and child feeding, emergency relief and as payment for works projects, there is increasing recognition of another category of food aid; the actual sale of the food aid, referred to as "monetization," which permits any agency to translate food inputs into cash or other resources that may be necessary to support development and relief projects.

This Food Aid Management document (FAM) was developed because of the intense interest in monetization expressed in recent years by PVO staff. FAM routinely receives many probing questions about what it takes for a PVO to get involved in conducting monetizations. Interestingly, FAM has found a great deal of curiosity about monetization not only from PVOs that have never done any food aid programs but also from individuals with years of PVO experience in conducting food aid and monetizations.

This guide was written to share and circulate the large amounts of practical experience picked up by PVO staff, and to do so in as readable, contextual and accessible manner as possible. It is intended as a self-training , or auto-didactic text to introduce and provide an overview to all aspects of monetization, as well as to consolidate the lessons of the many case studies that over the years have been provided to FAM by its members. The goal also is to point the reader in the direction of other key references, such as Save the Children's 1993 Monetization Implementation Manual which provides clear step-by-step guidance on the conduct of a monetization. PVOs should also refer to AID's 1988 Monetization Field Manual, which explains the donor's perspective as well as any document.

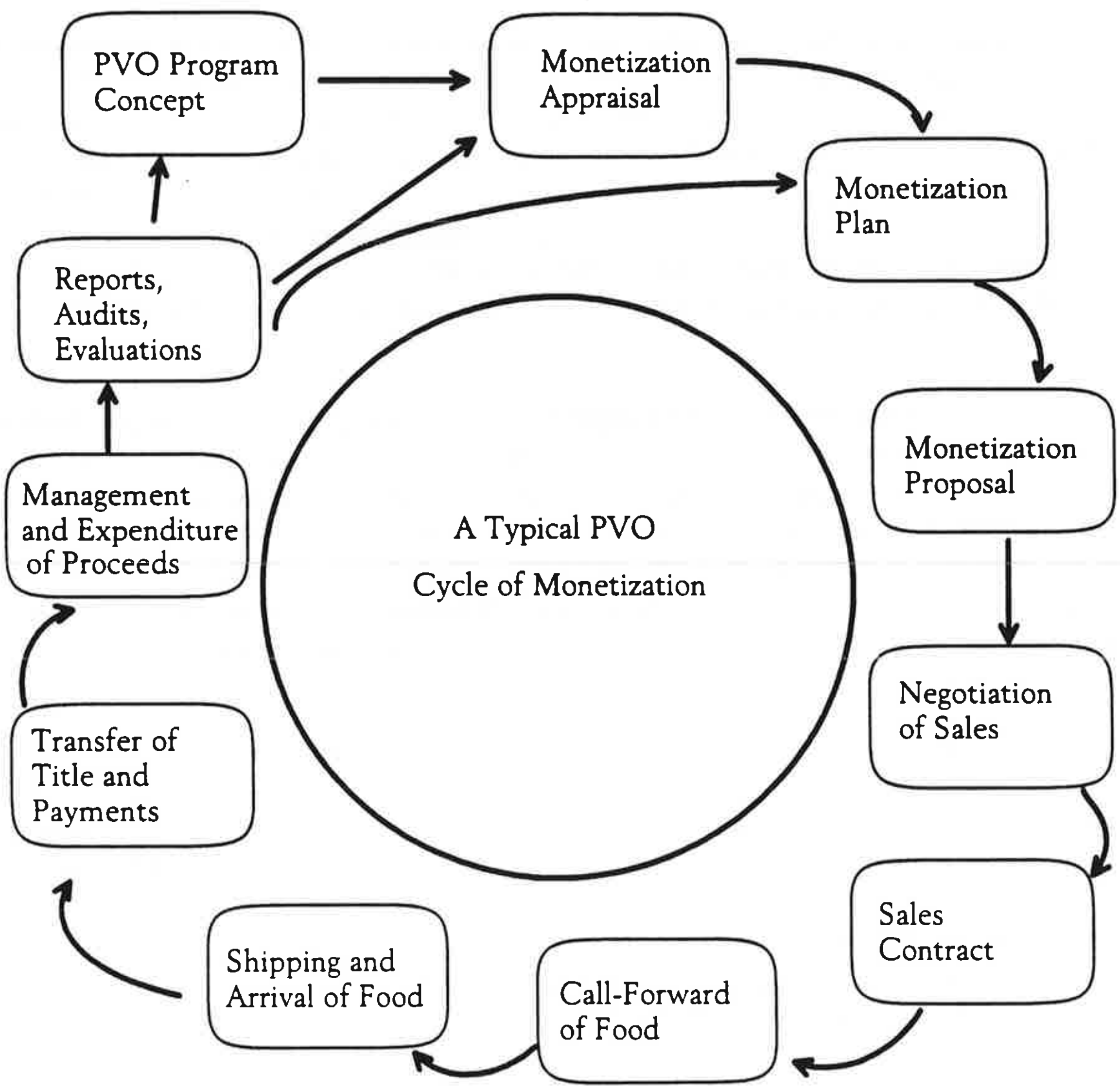
This guide is organized to match the stages of a monetization process: 1. conceptualization, 2. appraisal, 3. planning, 4. implementing, and 5. managing the proceeds. These are depicted by the "monetization cycle" diagram on the following page. Throughout this guide terms and case studies are introduced at appropriate stages to accompany the presentation of material. Most of the boxes provide further materials for the reader wishing to explore deeper on a particular subject. However, the reader can read the text straight through without needing to read any boxes, or may wish to study the boxed case studies at a later point when confronting monetization decisions and requiring reference examples.

- Chapters 1-4 discuss the background and history of monetization, who monetizes, why to monetize and why not.
- Chapters 5-11 explain the long and confusing task of beginning to determine whether a monetization is possible. This includes appraisal, assessment of potential delays, costs, returns and impacts.
- Chapters 9-13 explore the plan
- Chapters 14-19 explain how to conduct the sale, including the necessary skills in dealing with negotiating counterparts, and the format for auctions.

- Chapters 20-26 explore the follow-up to the sale. The primary importance is protecting the proceeds. To accomplish, this the PVO needs to establish, monitor, and report noncash accounts. Audits and evaluations also need to be performed.

Material for this guide derives from five sources:

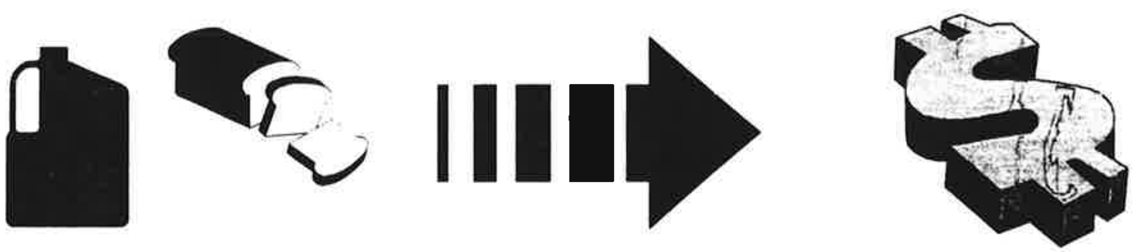
1. The Food Aid Management Monetization Seminar, held at Airlee House in November 1991;
2. Food Aid Management's briefings and field trainings (Washington, DC, Accra, Ghana, and Addis Ababa, Ethiopia);
3. Interviews and discussions with PVOs and other professionals who have conducted monetizations;
4. Published and informal literature, manuals, and reviews (cited in this document);
5. Review of technical data, food prices, reporting formats, etc. by the staff of Food Aid Management.



CHAPTER 1.
DEFINITIONS AND BACKGROUND

What is monetization?

Monetization, also referred to as "commercialization", is the sale of food aid commodities to fund development and relief activities. In the past few years, it has become a customary and substantial element of Private Voluntary Organization (PVO) programming. Groups worldwide are learning how to use agricultural commodities in more ways than mere disbursement for immediate feeding. Food monetizations are typically not projects in and of themselves. They are merely transactions by which one form of assistance (food) is converted into another (local currency), even as US dollars might undergo a foreign exchange conversion into local currency. Monetization proposals are subject to the same legislative mandates, professionalism, monitoring requirements and donor scrutiny as are regular food aid programs.



Since the early 1980s the term "monetization" has been increasingly used in common and technical parlance. In its strictest sense, it means the cashing out of goods, including labor. In foreign assistance discussions, monetization refers to the sale of commodities either by recipient governments or by PVOs. Such sales are often linked to the use of the sales proceeds for particular development projects, although some governments effectively use the proceeds as overall budget support. The term has other technical meanings as well. When economists refer to "monetization" of a region or economy they mean that there is more money circulating in it and that money transactions exceed barter transactions. Evaluation specialists "monetize" when they assign dollar values to social benefits or costs.

The World Food Programme (WFP) uses "monetization" in several manners. Both WFP and the World Bank use the term when referring to sales of commodity aid, even in the donor country, to raise cash for donations to multilateral projects. The principal type of monetization conducted by WFP is "closed circuit sales" or the purchase of imported foods at subsidized prices by cash-for-work project beneficiaries. WFP refers to commodity sales for cash in the country of origin (e.g. Canada) as "host-country monetizations." Monetization has even been used to describe sales of food by the project beneficiaries themselves.

Throughout this document, monetization will refer to the sale of foreign assistance commodities by or through PVOs, governments or other foreign aid channels. The term monetization will be used interchangeably with its plural, "monetizations", because monetization is a process. A single monetization program may include multiple sales.

What are Counterpart Funds?

Counterpart funds are the local currency or cash resources obtained from commodity sales. Government-held or donor-held accounts of local currency proceeds are usually referred to as counterpart funds. PVOs usually refer to these resources as "local currency proceeds", or "reflows."

What are the sources of food aid which a PVO can monetize?

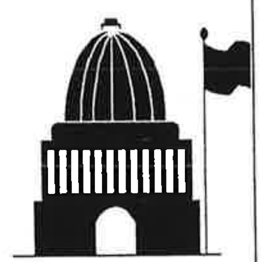
Out of a total U.S. foreign aid package exceeding $11 billion, food assistance accounted for about $1.8 billion in 1991. The US government provides food assistance under the Agricultural Trade Development and Assistance Act of 1954 as amended in the 1990 Farm Bill (see Box 1-a). Through this legislation, over $45 billion worth of food aid has been given overseas since the 1950s. Each year approximately $1.4 to $1.6 billion is appropriated by Congress under three Titles of this Act, known as "Public Law 480", or "PL 480." Title XV, Subsection A reads,

"It is the policy of the US to use its abundant agricultural productivity to promote the foreign policy of the US by enhancing the food security of the developing world through the use of agricultural commodities and local currencies accruing under this act."

This legislation has created separate categories of food aid:

Box 1-a- The legal basis for Title II food aid: excerpts from the 1990 Farm Bill

"Title II- Emergency and Private Assistance Programs



Section 201... a program... to provide agricultural commodities to foreign countries on behalf of the United States to (1) address famine or other urgent or extraordinary relief requirements; (2) combat malnutrition, especially in children and mothers (3) carry out activities that attempt to alleviate the causes of hunger, mortality and morbidity; (4) promote economic and community development (5) promote sound environmental practices; and (6) carry out feeding programs. Such program shall be implemented by the Administrator.

202...(c) Uses of Assistance.— Agricultural commodities provided under this title may be made available for direct distribution, sale, barter, or other appropriate disposition

(f) Effective Use of Commodities-- To ensure that agricultural commodities made available under this title are used effectively and in the areas of greatest need, organizations or cooperatives through which such commodities are distributed shall (1) to the extent feasible, work with indigenous institutions and employ indigenous workers; (2) assess and take into account nutritional and other needs of beneficiary groups; (3) help such beneficiary groups design and carry out mutually acceptable projects; (4) recommend to the Administrator methods of making assistance available that are the most appropriate for each local setting; (5) supervise the distribution of commodities provided and the implementation of programs carried out under this title; and (6) periodically evaluate the effectiveness of projects undertaken under this title."

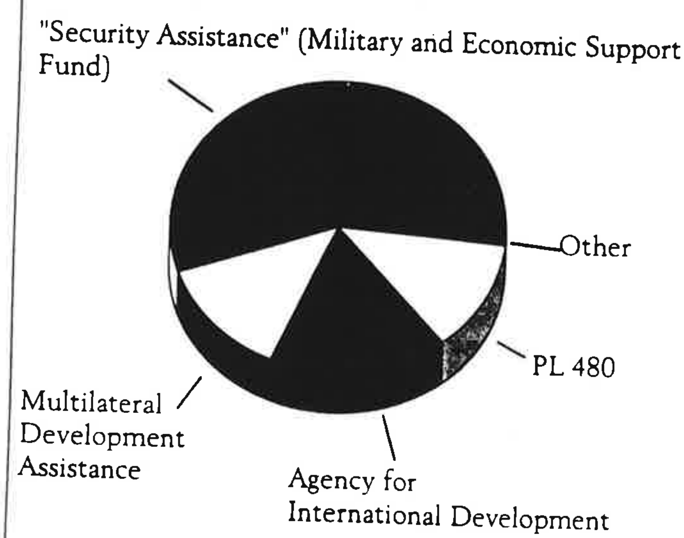
- Title I: **Sale** of agricultural commodities to developing countries on credit terms.
- Title II: **Grants** of agricultural commodities through PVOs and WFP for emergency and development purposes.
- Title III: **Grants** of agricultural commodities to governments of least developed countries.
- Title V: "Farmer to Farmer" Farming technical assistance through farmer **volunteers** .

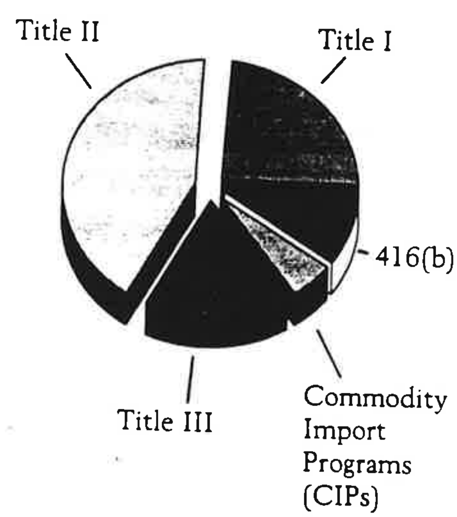
Title II food aid is for PVOs, cooperatives, and the World Food Programme. This is the principal source of food that PVOs use to support projects in the poorest countries. For this reason, this guide will refer repeatedly to procedures and regulations that refer specifically to Title II. PVO proposals to receive Title II foods for monetization must take the form of a Multi-Year Operational Plan, referred to as an "MYOP", submitted to AID.

Section 416(b), a separate account that makes use of only those foods that are currently in surplus stocks, is the next most important source of food for monetization. Section 416(b) supplies for PVOs are usually much smaller than the amount available from Title II. Because it is not a standard, appropriated amount, there is no assurance that there will be any predictable levels of commodities available from year-to-year from Section 416(b). The amounts available are often not known until midsummer each year so it is difficult to plan more than a few months in advance. Proposals to USDA for Section 416(b) commodities take the form of a Plan of Operation, or "PO."

PVOs are entitled to use Title III-generated currencies depending on their arrangements with host governments. Under Section 306(a)(5) and (b) of the new legislation, Title III food aid is available to foreign countries that are the most food insecure (have high infant mortality rates, low income, etc.). Title III food sales are monetizations conducted by governments. PVOs are permitted to assist

Box 1-b. PL 480 foreign aid comprises between 9% and 12% of US foreign assistance, varying from year to year, as shown in the pie below, left. In recent years Title II has been approximately $800,000,000, or about 44% of USG food assistance abroad, below





governments in planning their monetization as well as help determine the use of the proceeds (see Chapter 5).

The 1990 legislation emphasizes that Title III resources be directed to fostering privatization efforts in the food distribution sectors and to child survival and nutrition programs. In Fiscal Year 1991, 16 countries received a total of $293 million of Title III assistance. Some analysts feel that the value generated from the sale of Title III sales becomes primarily general budget or balance of payments support for host governments. AID finds Title III useful as a means of reimbursing foreign governments for undertaking recommended policy reforms.

Is the US the only nation that supports monetization?

No. Canadian food aid has been monetized (see chapter 2). Australian food aid policy states that it can be sold on local markets to meet nonfood project costs. In the recent relief effort for Somalia, the Government of Ireland provided a major grant to help PVOs conduct monetizations there.

Box 1-c. Legal Basis for Title II Monetization: Further Excerpts from the 1990 Farm Bill

"Title II- Emergency and Private Assistance Programs

Section 203. Generation and Use of Foreign Currencies by Private Voluntary Organizations and Cooperatives

(a) Local Sale and Barter of Commodities-- An agreement entered into between the Administrator and a private voluntary organization or cooperative to provide food assistance through such organization or cooperative under this title may provide for the sale or barter in the recipient country of the commodities to be provided under such agreement.

(b) Minimum Level of Local Sales-- In carrying out agreements of the type referred to in subsection (a), the Administrator shall permit private voluntary organizations and cooperatives to sell, in recipient countries, an amount of commodities equal to not less than 10% of the aggregate amounts of all commodities distributed under non-emergency programs under this title for each fiscal year, to generate foreign currency proceeds to be used as provided in this section.

(c) Description of Intended Uses-- A private voluntary organization or cooperative submitting a proposal to enter into a non-emergency food assistance agreement under this title shall include in such proposal a description of the intended uses of any foreign currency proceeds that may be generated through the sale, in the recipient country, of any commodities provided under an agreement entered into between the Administrator and the organization or cooperative.

(d) Use-- Foreign currencies generated from any partial or full sale or barter of commodities ...may--

(1) be used to transport, store, distribute, and otherwise enhance the effectiveness of the use of agricultural commodities...

(2) be used to implement income generating, community development, health, nutrition, cooperative development, agricultural, and other developmental activities within the recipient country; or

(3) be invested and any interest earned on such investment may be used for the purposes for which the assistance was provided to that organization, without further appropriation by Congress.

(e) Sales Assistance-- The Administrator may provide assistance to an organization or cooperative, on request, in the sale of commodities in the recipient country."

PVOs have always fed hungry people with food aid. Why would they sell it?

In the past, critics of monetization have taken the point of view that allowing food aid to be sold reduces the scale of food-supported efforts to feed hungry people. There has been some concern over the growing proportion of PVO proposals that call for sales. But recent amendments to the US Farm Bill have called for increases in monetization.

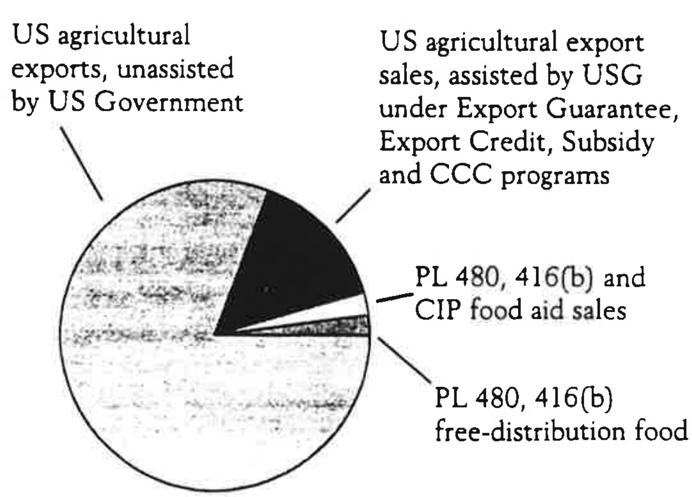
Arguments for monetization often rest on economic efficiency: the savings on internal transport, storage, handling, and administration obtained when food is sold in a convenient urban center and the cash generated used to finance projects, such as public works. Reasons for monetizating food instead of directly distributing them may be based on the following conditions:

- The cost of delivering food aid may exceed the cost of using locally available foods.
- Those commodities donated may not match local dietary habits.
- Monetization may pose fewer timing/scheduling problems associated with food arrival and distribution than direct distribution programs when their some urgency.
- In recent years it has been found that cash contributions from host governments and from beneficiaries to support feeding programs have diminished.
- The logistic costs of food distribution have been increasingly expensive, particularly in Africa.
- Monetization facilitates further food imports into a country that has little foreign exchange.

Is monetization a new way of delivering food to poor countries?

No. Referring to the chart in box 1-d, note that most US food exports are sales. Beyond that, most food-assistance programs are also sales of some sort. For many years governments have sold food donations received bilaterally. PVOs and cooperatives have been using these food sale proceeds for development projects for decades; and PVOs and cooperatives have been conducting the sales themselves for over ten years. What is new is the variety of agencies becoming involved in selling food aid. More and more PVOs, cooperatives, UN agencies, and intergovernmental organizations are exploring monetization as one among a number of mechanisms for applying food resources in varying situations.

Box 1-d. US food aid for free distribution is less than the PL-480/Section-416 food aid that is sold, and represents only 2% of all US food aid exports.



Food assistance from the United States has fallen from 30% of total grain exports in the 1960s to less than 5% today. Food aid levels have not grown as fast as US grain exports. At the same time, more and more food aid is given through PVOs and multilateral channels, while a decreasing proportion is going through foreign governments. While government monetizations have not grown, PVO monetizations have grown markedly.

Our PVO has never dealt with commodity assistance. Is monetization just for PVOs that have experience with running regular food distribution programs?

No. In fact, some PVOs that use food aid have monetized virtually all of it, without ever distributing any commodities directly to program participants. These are referred to as **"100% monetizations."**

AID tends to favor monetizations in support of conventional food distribution projects. These are referred to as **"partial monetizations,"** which continue to comprise the larger share of PVO monetizations. Monetization has been acceptable to AID and to Congress in large part because it covers the expenses of local food distribution. But monetizations do support nonfood distribution projects in a wide range of areas. The questions are: does the country under consideration warrant food aid, and is your project sound enough to justify an approved monetization proposal?

Box 1-e. One expert's views on the best uses of food aid.

"As the world's largest provider of food aid, the United States should play a leading role in addressing international problems in which food aid is an especially appropriate response. In pursuing our national interests, and the global interests that we share with others, we must adjust and adapt our programs in light of new information and changing circumstances.

"A point of agreement among experts is that food aid should be given away as little as possible.

"The simple point is that donors should provide the food commodity that yields the highest benefit in sales terms in the recipient country relative to the procurement costs. This is true whether the food is to be sold, to be exchanged, or to be used directly in projects and not marketed.

"Of course, **marketing** food, except for emergency cases, is the **most efficient** way to provide it, and one most in keeping with expanding food marketing channels. Public Law 480 should reflect this by making **monetization of all food aid the norm** and direct use of imported food aid in feeding people the exception, to be used for emergencies and other special situations. Market distortions may make commodity selection difficult, but local economists, perhaps working with host government and other donor officials, should be able to reach judgments on this issue fairly easily every three to six months.

"Selling food openly into areas with effective demand can amount to cheap, efficient and progressive taxation. Bangladesh, for example, at one time depended on food aid for a large proportion of its budget. In the mid-1970s revenues from food aid sales were equal to 75% of government development expenditures. Instead of developing a more efficient and effective taxation system, Bangladesh, some argue, was allowed to develop a dependency on earnings derived from its food sales, earnings which would disappear if either domestic or commercially imported food were used in its ration shop sales instead of food aid."

excerpted from R Hopkins 1989 "Reforming Food Aid for the 1990s" Statement before the US House of Representatives Select Committee on Hunger, June 22

But isn't the programming and sales of food too technical for PVOs without food aid experience to undertake?

Many of the necessary components of a food sale, including port surveys, claims for losses, the proposal and reporting process to the U.S. Government are the same whether the food is sold or not. It is true that PVOs with food aid experience have an advantage, but monetization involves enough technical expertise that even the large food-distributing PVOs often use specialists from brokerage or consulting firms to help them.

PVOs can help to plan and to receive benefits from monetizations without actually conducting them. Some PVOs may monetize on behalf of other PVOs. US and international PVOs have been able to use the local currency proceeds from Title III government-to-government food aid that is monetized by the recipient government. As discussed in the US Farm Bill legislation of 1990 (Box 1-c), monetization of Title II food is to be conducted by cooperating sponsors and their sub-recipients in pursuit of food security in poor nations. It is up to the PVO to determine the relative need in the countries where it works. As discussed in chapter 2, each year more and more PVOs gain experience in managing food aid, often beginning with using food in an emergency or in a monetization.

Box 1-f. Key actors/institutions

AID

Agency for International Development, the foreign assistance arm of the US Government, responsible for administering PL 480 Title II

ASCS

The Agricultural Stabilization and Conservation Service of USDA that administers the price and income support programs for major agricultural commodities.

CCC

Commodity Credit Corporation, an agent for the USDA to procure US-produced food for food aid.

FAS

Foreign Agriculture Service of USDA promotes agricultural exports, including posting agricultural attaches and trade officers overseas. This is the office that a US PVO contacts to initiate or follow-through on proposals for Section 416(b) food aid.

FFP

Food for Peace, the office within AID that directly administers PL 480 Title II.

KCCO

Kansas City Commodity Office of the USDA where the procurement, delivery to port, and shipping routes of food aid are determined.

OMB

Office of Management and Budget of the US Government which establishes annual funding ceilings for all Federal agencies, as well as procedures relating to expenditures and grants, including support to PVOs.

USDA

The United States Department of Agriculture, the federal agency which manages food aid budgets and logistics, as well as other farm support and food stamp programs. The Secretary of Agriculture is resonsible for determining the availability of surplus commodities each year.

If a PVO chooses not to monetize food aid, will the food be sold in the US instead?

No. The food aid that PVOs receive from the Federal Government is appropriated for foreign assistance by Congress on an annual basis. Each year at least 10% of non-emergency food aid must be monetized according to Section 203(b) of the Farm Bill (Refer back to box 1-b): *"commodities equal to not less than 10% of the aggregate amounts of all commodities distributed under non-emergency programs under this title for each fiscal year."*

While helping hundreds of millions of the poor overseas, US food assistance has been, in effect, a loss leader helping to introduce US food products to new countries and thereby expand future exports. But the effect of food aid overseas is small compared to other interventions by the US Government in supporting farmers and food prices in the US (see box 1-g). The amount of food that the US government provides in what are known as entitlement programs to the poor, $24 billion in food stamps alone, far exceeds the amount of food that is shipped overseas in food aid programs.

Box 1-g. USG farm support programs do not raise prices in the US market

"American consumers spend a smaller portion of their income on food than do consumers in most other countries. The portion of income spent on food indicates that US food is cheap relative to our per capita income, which is one of the highest in the world. As income goes up, consumers spend a smaller share on food."

"Is the price of US food cheaper than in other countries? The price of some foods is lower in the US than elsewhere, and the US is the world's least-cost producer of many agricultural commodities. Two elements of agricultural policy have contributed to these lower prices. First, we have been generously endowed with agricultural land, and federally funded agricultural research has increased its productivity, thus lowering food costs over the long run. It now takes fewer resources to produce farm products. Funding for agricultural research has been a major thrust of farm policy since the Civil War and it continues to account for nearly $1 billion of federal spending every year" (more than all the Title II food sent abroad).

"Second, most farm policies in the United States do not support farmers by forcing consumers to pay higher prices for food. Most government transfers to farmers are direct payments ("deficiency payments"). With a few exceptions, farm incomes have not been supported through higher consumer prices. Direct payments come about because producers of wheat, rice and feed grains are paid the difference between the market price and a target price. Thus the design of most farm programs has placed the burden of program cost on taxpayers, rather than on consumers. Because the poor spend a larger portion of their income on food and pay fewer taxes, the burden of farm program costs falls on the richer members of society. The design of US policies is in sharp contrast to policies in Europe and Japan where consumers pay higher prices in order to support farmers."

"The primary growth point for agricultural demand during the last twenty years has been export demand. For example, our domestic demand for wheat, rice and coarse grains grew at 1.4% annually from 1960 to 1989, but exports of these crops grew much faster at 4.3%. Exports have taken an increasing portion of all agricultural sales since 1970, and by 1990, trade accounted for about one quarter of agricultural output and one third of acres harvested."

from W Browne et al. 1992 Sacred Cows and Hot Potatoes Boulder, CO: Westview Press

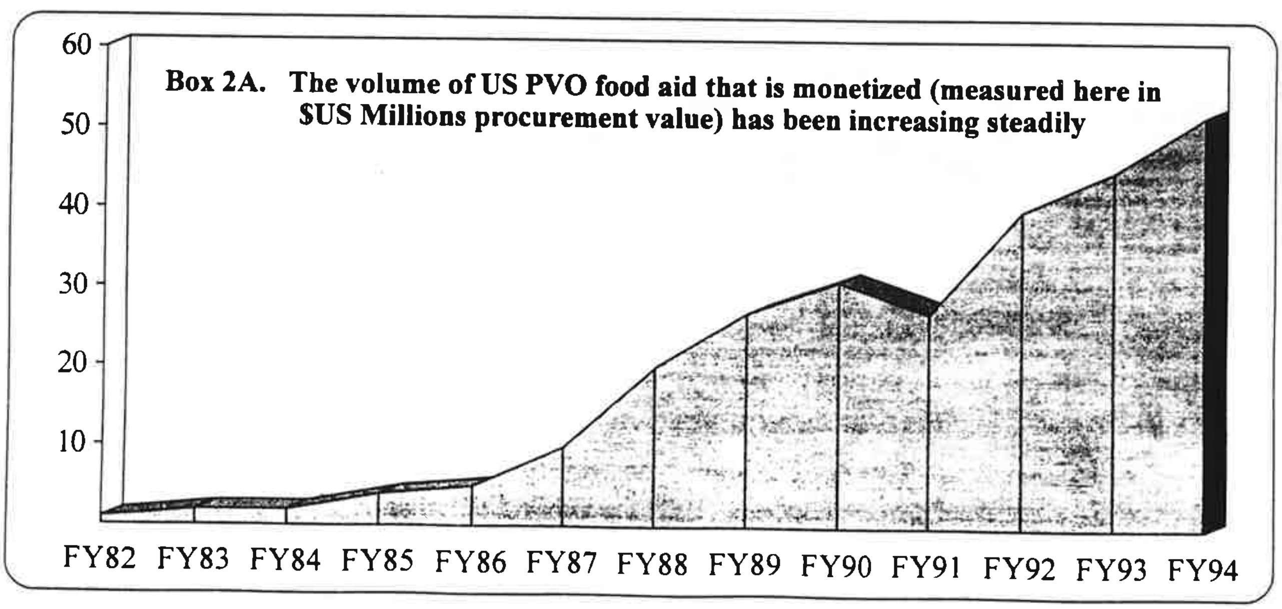
CHAPTER 2.
OVERVIEW: MONETIZATION IN PRACTICE

Are many PVOs pursuing monetizations?

Every year more US PVOs and their overseas counterparts become involved in monetization for the first time. Ten years ago only one or two cooperatives had experimented with monetization. As recently as the late 1980s, only a couple of large US PVOs had practical experience in monetization. Now many of the food-distribution PVOs conduct monetizations on a regular basis. Over 15 US PVOs have proposed or completed a monetization. Many more NGOs, local counterparts, and indigenous institutions have been the recipients of the proceeds generated from monetization abroad.

How much food aid is monetized by PVOs? Is it likely that the volume of food aid allocated for PVO monetizations will increase further?

In 1992 PVOs sold close to 150,000 MTs from Title II sources, representing about 15% of total Title II resources. In each year since 1985, when PVO monetizations were authorized, these sales have grown in volume and value, as shown in box 2-a.. The FY93 and FY94 levels cited are projected, based primarily on the trends of recent growth. Future growth in the volume of food aid monetized will depend upon PVO policies, project needs and project proposals, AID policies, and Congressional action. Due to the increasing popularity of monetization, the number of monetization proposals is expected to increase each year.. Given such assumptions, and extrapolating recent rates of growth, PVOs might monetize $100,000,000 worth of food in the year 2000.



Box 2A. The volume of US PVO food aid that is monetized (measured here in $US Millions procurement value) has been increasing steadily

Where are PVOs involved in monetization?

PVOs have used monetizations wherever they have had projects. In recent years PVOs and cooperatives conducted Title II monetizations in the following countries:

- in Asia and Middle East- Bangladesh, Indonesia;
- in Latin America and the Caribbean- Bolivia, Dominican Republic, Guatemala, Guinea Bissau, Honduras, Jamaica, Peru;
- in Africa- Burkina Faso, Ethiopia, Gambia, Ghana, Kenya, Mozambique, Sierra Leone, Sudan, Togo, Uganda.

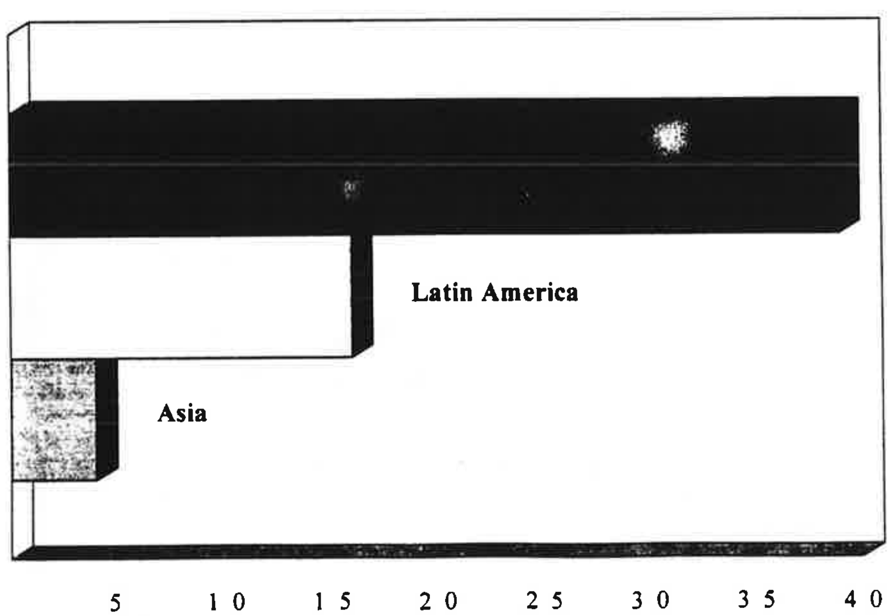
This breakdown is reflected in box 2-b below which counts each PVO annual monetization program separately. It appears that a larger number of PVO monetizations are conducted in Africa than in Asia or Latin America. This is due, in part, to the greater difficulty PVOs have in transporting food within Africa to direct distribution sites, and to the fact that more new PVO projects have been opening up in Africa than in other parts of the world.

Where can monetizations be conducted?

AID is bound by the legislative requirement that Title II food is for nations that are relatively food insecure. AID has created a "food security index" that is updated annually to contrast countries in this manner. According to this index, the following countries in addition to those listed above are considered the **least** food secure:

- in Asia and Middle East- Afghanistan, Bhutan, Cambodia, India, Laos, Pakistan, Albania, Yemen and Sri Lanka;

Box 2-b. The number of separate Title II monetizations conducted by PVOs and cooperatives in FY91 and in FY92, by continent where conducted.



Source: US AID Office of Food for Peace

- in Latin America and the Caribbean- Haiti, El Salvador, and Nicaragua;
- in Africa- Angola, Benin, Burundi, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Gambia, Guinea, Liberia, Lesotho, Madagascar, Mali, Mauritania, Namibia, Niger, Nigeria, Rwanda, Sao Tome and Principe, Senegal, Somalia, Sudan, Zaire, and Zambia.

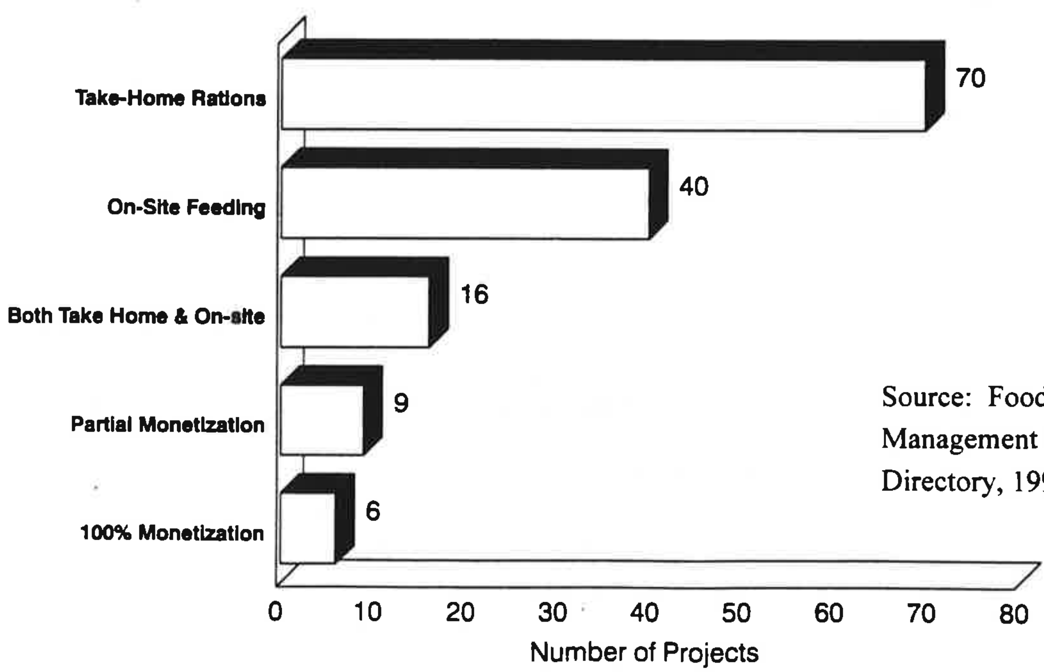
Until 1993 the Brooke Amendment prohibited food aid for development projects in countries that are in arrears in repaying debts to the US Government. Congress has now determined that all food aid and all PVO projects are exempted. This allows food aid to be monetized in support of activities in a greater range of countries, such as Sudan, Ethiopia, and Haiti.

USDA is open to discussion about the use of Section 416(b) food for almost any country where the PVO can make a case based on need at the project level and for which the food aid is not undercutting other imports from the US. For instance, although Mexico is considered too developed to receive Title II food aid, in 1989 and 1990 USDA allowed 446,000 MTs sorghum to be monetized in Mexico by PVOs such as CARE, World SHARE, Christian Outreach Appeal, International Partnership for Human Development, and Desarrollo Integral de la Familia, as well as the World Food Programme.

Is monetization more popular than other forms of food transfers?

No. PVOs still distribute most US food aid directly to target populations, either as take-home rations or through on-site feedings, as depicted in box 2-c. In the most recent year for which we have data, less than 1 in 20 PVO projects were 100% monetizations. However, a larger proportion of

Box 2-c. Numbers of food distribution methods cited among 144 PVO projects in FY92.



Source: Food Aid Management Project Directory, 1993 projects were joint monetization/food distribution where the monetization helped to finance the complementary expenses associated with regular food distribution.

At a workshop at Sussex University, England participants discussed the choice between direct distribution and monetization. They noted that the decision should depend on: (a) success in targeting the poor for a specific developmental purpose; (b) cost-effectiveness and ease of bureaucratic management in logistic arrangements, management of funds and budgetary transparency; and (c) flexibility and autonomy in the use of the resources by targeted recipients.

> *"There was a consensus at the meeting that in considering the choices, there should be a presumption in favor of monetization, defined broadly to include triangular transactions, local purchases or exchange arrangements. Direct distribution should only be considered where monetization seemed to be unfeasible-- because of difficulties of targeting, market failure or administrative barriers. ... In-kind aid transfers often conveyed a much lower income transfer to beneficiaries than the total cost involved in effecting such transfers."* (reported in S Maxwell, T Owens 1991 Commodity Aid and Counterpart Funds in Africa, IDS Discussion Paper 291, pp 16-17).

What types of project activities are these food programs helping?

As the case studies throughout this document will demonstrate, PVOs have used monetizations for the full range of activities that PVOs finance, including agricultural, public works, training, income-generating, public health, child-survival, and environmental programs. PVOs are learning how to use monetization effectively to support an ever-greater variety of projects (see chapters 3 and 22).

Who else monetizes food besides PVOs and recipient governments?

PVOs from the United States and Canada have the most experience monetizing food aid. PVOs in other continents often receive cash from donor governments with which the PVO procures food.

The Canadian Government supports monetization with food aid administered through the Canadian International Development Agency (CIDA). For example, each year approximately $1 million in food aid is sold in Bangladesh to support the work of CARE Canada.

Box 2-d. Some countries, like Ethiopia, have many forms of monetization at once.

"The level of food aid monetization (in Ethiopia) has increased, not spectacularly, but significantly. The EC is monetizing 50,000 MT a year of wheat to supply the urban rationing system; the US has signed ... a Title III agreement covering the provision of 30,000 MT of wheat and 9,000 MT of cotton in 1992, worth approximately $13 million, the value rising to $40 million in 1993 and 1994; Canada is considering a monetized food aid program; World Food Programme continues to monetize for (logistics costs); and small-scale monetization is also being practiced by NGOs. Most of these activities are still plagued by the problems... overvalued exchange rate, government tax policy, hidden wheat reserves, etc.."

from S Maxwell 1992 Next Steps in Food for Development: Report on a Visit to Ethiopia Sussex: IDS

The **Canadian Foodgrains Bank**, a group of Canadian PVOs that works with private grain donors and the government of Canada, has experimented with monetization. In the last few years it has programmed food aid through a range of creative monetizations around the world.

In 1991/92 the Canadian Foodgrains Bank sold wheat at subsidized rates to small-scale bakeries in Nicaragua as a stimulus to support these new retail outlets, to foster microenterprise in general, and to help the country with foreign exchange shortages. Other monetizations have taken place in Ethiopia and the Caribbean that are variations on the typical donor--PVO--wholesaler relationships. Because of the surplus patterns in Canada, most of the monetizations use either wheat or corn. Currently, the Canadian Foodgrains Bank has an agreement with CIDA to conduct at least 6 specifically targeted monetization programs worth a total $2 million. In this effort they will be developing staff that specialize in exploring new ways to use monetization.

The **World Food Programme** (WFP) has experimented with paying workers in cash in what are called closed circuit monetizations (see box 2-f). These workers are given the option of buying food imported by WFP from special stores at subsidized, low prices. These purchases provide cash which then recirculates as payment of their wages. In effect, the work project participants are paid partly in cash and partly through food.

WFP has tried various forms of monetization, but has been cautious about adopting any long-term strategy on using food sales. AID's Handbook 9 states: *"Sales of WFP commodities are regarded as exceptions, such decisions being based on one main question: is the sale absolutely essential to the project.... Sales of commodities are permitted only where such sales are inherent to the purpose of the project or to closed groups or designated beneficiaries. In both instances, the sales take place outside normal commercial markets"* (1981/ 12-3). Yet a recent collaborative examination of

Box 2-e. UNICEF and WFP have experimented with cash vs. food in Ethiopia

"The other type of public works in Ethiopia was the cash-for-food program. This innovative scheme assumed that in certain parts of the country it was a lack of purchasing power, rather than a lack of food, that was causing most hardship. It was therefore believed that recipients of cash in such 'pockets' of famine could tap into regional markets where food was still available at reasonable prices, thereby stimulating flows of food to distressed areas. Furthermore, it was anticipated that this would reduce intervention costs (especially compared with food-for-work), reduce delays in wage deliveries, and prevent mass migration of communities toward food distribution points, all while supporting development projects at a community level.

"...Cash-for-food recipients... had difficulty in fulfilling the program expectation of tapping distant food markets and stimulating flows of food from surplus to deficit regions. During the famine, government policies restricting grain movement between localities were enforced at road control stations and by local militia. ...In response to such problems, many households decided to stay home and try to purchase food locally. This had the effect of causing local inflation of food prices at the time of each cash distribution. More than 75% of households report that prices rose by as much as 100% around distribution times. It is not surprising, therefore, that 80% of respondents would rather have received grain at their doorstep than face the problems associated with cash payments."

From P Webb 1992 Household Responses to Famine in Ethiopia Washington DC: IFPRI food assistance by WFP and the World Bank concluded that perhaps monetization should be a more common WFP practice. It states,

"As a general principle, resources should be transferred in ways that allow the greatest flexibility and efficiency. When malnourished or food- insecure beneficiaries benefit more from local currency (from monetized food), such an approach should be considered. ...Increasing the food intake of vulnerable groups.... can make a direct contribution to the development of human resources... A target group may be more effectively assisted, however, through other measures, such as improved public health care, nutrition education, and so on, using local cash from monetization." (Food Aid in Africa: An Agenda for the 1990s)

In May, 1993, WFP hosted a conference in Rome to collect cumulative experience on monetization. Presentations at that conference demonstrated that monetizations have successfully been used to support the full range of country programs, from distribution in kind of food, through coverage of complementary costs, to market development and budgetary support for governments.

Box 2-f. WFP Experience with Monetization

During the years from 1963 to 1986 sales have been involved in 225 projects and project expansions: about 16% of the total number of WFP projects. The volume of WFP commodities approved for sale over that period has been limited, but not insignificant, amounting to 10- 15% of the total quantity of WFP food aid committed. (from WFP 1987 CFA 24/5 pg 3). Approximately one-quarter of these monetizations have been connected to projects costing over 10 million dollars. WFP has used food sales to strengthen food security through support for cereal market restructuring. But otherwise, WFP has been discourged by its governing body from using food principally as balance-of-payments or geneteral budgetary support for governments.

WFP sees all monetizations as falling within one of three categories:

Category A: projects in which the sale itself is part of the project as in support to food processing companies (dairy development), feedgrains for livestock development, and for price-stabilization through food reserves and grain banks.

Category B: projects in which WFP rations are sold to closed groups, including closed-circuit sales to workers. CFA 24/5 notes "Four types of projects have been particularly prominent in the case of Category B sales: livestock development, land development, and improvement, land settlement, and forestry projects. Sales of WFP commodities in this category have taken place in two ways. First deductions have been made from workers earnings for the WFP food received as part of their wages in cash and then allowed to purchase their entitlements of WFP commodities at subsidized prices through distribution outlets; Second, sales at subsidized prices have been made to beneficiaries through institutions of which they are members, such as cooperatives and mothers' clubs."

Category C: open market sales, including monetizations where the food is sold in the country of origin. Funds generated have been applied to the purchase of equipment, tools and materials, for skilled labor, for revolving credit funds, for shelter and water services, and for ITSH costs of regular food distribution.

Who buys commodities from the PVO? The consumer directly? Other PVOs?

Food assistance is sold to all sorts of agencies, public and private sometimes to the government or one of its agencies. PVOs can transfer foods to consumer groups that can monetize. PVOs are not permitted to monetize food directly to project beneficiaries: i.e. vulnerable groups.

PVOs do not sell to other PVOs as a matter of course. Most monetizations are designed to generate as much revenue as possible to have the largest development impact. Determining to whom food will be sold affects the price that will be offered or obtained. As a general rule, the highest prices in a country will come from the most competitive process, involving the largest number of bidders each vying for a larger share of the overall sale.

Frequently the market for a particular commodity or group of commodities will be legally controlled by marketing boards, or parastatals which are agencies set up by the government to tax, procure, store, and control prices on certain foods. Parastatals are often thought of as large corporations that are owned by the government. Marketing Boards were and are set up by many governments to control the flow of foods to encourage exports of certain foods and to facilitate the movement of certain foods to urban consumers.

Often parastatals will allow prices for a commodity to vary only within specified limits. For example, BULOG, an agency of the Indonesian Government established in 1967, makes certain that basic foods are available to consumers at all times. It is involved, therefore, in procurement of and import controls on rice, wheat, maize, soybeans, mungbeans and groundnuts. It establishes a floor price for rice and for paddy by buying from thousands of cooperatives and traders and by restricting imports

Box 2-g. Food sold in Mozambique has been donated through many sources.

At one point, there were so many agencies involved in the monetization of food aid in Mozambique that there was a great deal of confusion in identifying how much of which proceeds belonged to which accounts. Each donor intended the proceeds to be used for different projects, or for budget support for the government, to pay off debt, or to help respond to the emergency.

While Canada expected to use the price at the port of export (Canadian) for wheat sold in Mozambique, France valued its wheat sales proceeds on the wholesale price in Mozambique.

The United Kingdom provided white maize through internal purchase in Zimbabwe by the World Food Programme. They calculated the value of the donation by the wholesale price received by the parastatal, IMBEC. EEC donations are also calculated by wholesale price but based on the average prices over a year. Spain does not follow any valuation system for sales of its donated rice, leaving it up to the government of Mozambique.

The US based its value on the price of the food as procured in the United States, and used the highest legal rate of exchange available when the food arrived.

The authors of the 1990 study concluded that "A single monitoring, accounting, reporting, and auditing system, with a common framework and format, should be developed. It should cover the commodity imports as well as the local currency generated from the sale of the commodities."

B Riley, D McClelland 1990 Concept Paper: Enhancing the Effectiveness of Counterpart Funds in Mozambique (unpublished) World Bank, AID which are held off the market except in times of shortage. But BULOG operates thousands of warehouses which hold a series of buffer stocks, thus allowing rice prices to remain within a narrow range for years.

Do PVOs have to sell to these parastatals?

No. But host government policies may make it impractical or impossible to sell any other way. It is often convenient to sell to parastatals because it saves the PVO from having to examine local markets, to manage competitive sales, or to worry about price structures. Unfortunately, parastatals are rarely able to offer the best prices. They are often wealthy in inventory and real estate, but short of cash.

In other situations, where parastatals exist but the PVO is not required to sell to it, private buyers will still be influenced by the price barriers enforced by these parastatals. PVOs have found that

Box 3-h. USDA food assistance to the newly independent (former Soviet) states (NIS)

The food assistance effort, worth nearly $103 million in early 1992, included Section 416 and Food for Progress agreements. The President of the United States decided that PVOs would be used as the primary source to deliver the food aid "to reflect the spirit of the people of the US."

Food was distributed by the Adventist Development and Relief Agency, American Jewish Joint Distribution Committee, American National Red Cross, Brother's Brother Foundation, Catholic Relief Services, CARE, Citihope International, Diocese of the Armenian Church in America, Mercy Corp International, Sovereign Military Order of Malta, and World Vision Relief and Development Inc. Foods distributed included beans, Non-fat Dried Milk, Bulgur, Butter, green whole peas, butteroil, bagged rice, evaporated milk, soy-fortified bulgur wheat, infant formula, vegetable oil, lentils, and wheat flour. Wheat, rice and milk made up well over half of the total by volume.

PVOs later credited USDA for the quality of the commodity information it provided, the smooth and streamlined contract procedures, hands-on involvement in minimizing commodity losses, and flexibility in changing call forwards.

On evaluation, PVOs found that the food aid implementation had numerous indirect benefits on the transition from these areas to free-market economies, including:

- introduction of new commercial concepts to populations
- aid in development of direct carriers in country
- creation of markets for private warehouse rental
- private sector learning
- creation of private repackaging industries
- introduction of the concept of competitive bidding for PVO contracts.

Although the goal of most of the PVO programs was to increase food access for institutions, children, elderly persons and orphans, much of the food was **monetized**. For instance, Mercy Corps International's monetization of 4,000 MTs of butteroil provided proceeds that were used to support the distribution of 3,000 MTs of wheat flour in Alma Ata throughout the government ministries of Social Welfare, Health and Education. The proceeds were also used in a primary health care training program in Kazakhstan. In addition, a bilateral agreement created the Republican Fund which controlled the receipt and disbursement of monetization proceeds

taken in part from USDA 1992 USDA's Efforts to Provide Food Assistance to the Newly Independent States Washington DC: Agricultural Stabilization and Conservation Service monetization can help countries that are making the transition from markets controlled by parastatals to open markets.

PVOs have some latitude on whether to go through parastatals or not through their selection of commodities. Most parastatals and marketing boards have mandates to deal only in certain staple commodities. By selecting other commodities, such as vegetable oil, or bulgur wheat, or lentils, the PVO may be free to go directly to open market operations.

Aren't state-controlled monopolies believed to be inefficient?

Any effort to control prices to make foods affordable for the poor entails high costs. These costs are in large part responsible for the heavy debts now carried by many governments. Because of the expenses, inefficiencies, and donor pressures, the role and scope of marketing boards and parastatals has rapidly declined worldwide in recent years. This dramatically changes the nature of future PVO monetizations. More and more sales will be open-market and competitive.

So, how do PVOs determine to whom to sell food?

There are no formulas for deciding in advance to whom to sell. It depends on the results of your market appraisals and meetings with buyers and government representatives (see chapters 5-11).

To a large extent, the selection of to whom to monetize is also determined by your objectives or goals. Sometimes the PVO wants to assist small entrepreneurs and traders. In such cases, you may choose only to sell to them in small quantities that they can afford.

In other cases you may want to sell so that you can readily obtain other local foods for distribution. If you bring food in, sell it and immediately obtain other foods through local purchase you are close to conducting a "swap." A swap or barter is when you directly exchange one commodity for another. When you bring in one commodity, obtain another commodity, and use the new commodity in a different country, this is referred to as a "triangular transaction." Triangular transactions have proven to be an effective means of programming certain types of foods available in developing countries (e.g. white maize) for use in distribution programs in other food-deficit countries. "Trilateral agreements" has been a mechanism by which a donor government provides resources to a food-supplier country which in turn provides food aid to a food-recipient government. The US Government has involved PVOs in such operations to Burkina Faso and Mali (from Ghana), and to Mozambique (from Malawi and Zimbabwe). The governments of Japan, Netherlands, Switzerland, EEC, Sweden, and Italy have also used this mechanism.

➢ ***FURTHER READING:*** *For information on patterns of food aid use in projects see*

1. *Food Aid Management's Directory of Food Assisted Projects -1992;*

For levels of food monetized, see

2. *AID Food For Peace Annual Report on PL480:*
3. *G Templer et al. 1993 Monetization or Distribution in Kind? Background Material: Agency Policy and Practice. Sussex: Institute for Development Studies;*

For a history of triangular transactions see

4. *A Morton et al. 1988 Trilateral Food Aid Transactions: USG Experience in the 1980s Washington DC: Ronco Consulting Corporation*
5. *E Clay, C Benson 1992 "Triangular Transactions, Local Purchases and Exchange Arrangements in Food Aid: A Provisional Review" in E Clay and O Stokke editors Food Aid Reconsidered London: Frank Cass pg 143-190;*
6. *World Food Programme's 1987 Occasional Paper #11: A Study of Triangular Transactions and Local Purchases in Food Aid;*
7. *B Martens 1990 "The Economics of Triangular Transactions" Food Policy February: 13-24*
8. *World Bank, WFP 1991 Food Aid in Africa: An Agenda for the 1990s Washington DC*
9. *V Ruttan 1990 Why Food Aid? Surplus Disposal, Development Assistance and Basic Needs Minnesota: Center for Intl. Food and Agric. Policy*
10. *T Srinivasan 1989 "Food Aid: A cause of Development Failure or an Instrument for Success?" New Haven, CT: Yale University, Economic Growth Center Paper #417*
11. *D McClelland 1992 "Programming and Managing Counterpart Funds to Enhance Economic Development: A US Perspective" IDS Bulletin 23(2): 69-73*
12. *BIFAD, 1988 Food Aid Projections for the Decade of the 1990s Washington DC: Board on Science and Technology for International Development, National Research Council*
13. *S Chakravarty, PN Rosenstein-Rodan 1965 "Linking Food Aid with Other Aid" Rome: FAO*
14. *E Moore 1992 US Food Aid: What is It? Washington DC: AID.*

CHAPTER 3.
MONETIZATION AND FOOD SECURITY

Why do we hear of monetization related to food security?

The authorizing legislation (1990 Farm Bill) establishes "food security" as the overall goal of PL 480 food aid. AID has described food security recently as "when all people at all times have both physical and economic access to sufficient food to meet their dietary needs for a productive and healthy life." In its 1992 Policy Determination, Definition of Food Security, AID explained that,

"PL 480 ...food aid resources and AID's dollar resources can be used to complement each other and help achieve food security in ways that are consonant with AID's economic development objectives. ...Three distinct variables are central to the attainment of food security: availability, access, and utilization. It is obvious that ***many potential factors*** *may contribute to food insecurity. Food security for all is a long-term objective which will be attained mainly through sustained economic growth, -more quickly if it is equitable and broad-based."*

Do PVOs need to worry about making the connection between the sale of food aid and this general goal of food security?

Yes. However, there can be creativity in designing projects that support of food security. To ensure that your operational plan will be approved, you should clearly explain not only all the activities for which you seek support, but also the expected effects and how these relate to food security. These effects include the immediate outputs (participation levels, public works constructed, etc.). You should also explain how these outputs are expected to lead to your objectives, such as long-term increases in income, improvements in dietary habits, etc. Then discuss how these objectives are integral to efforts to achieve food security in a particular country or region. For examples see boxes 3-a and 3-b.

Few USAID Missions have identified food security, per se, as one of their strategic objectives. Nevertheless, food security can be shown to be linked with many of the existing AID priorities, including eradication of poverty, creation of social safety nets, expanding income growth, agricultural development, etc. In fact, a 1992 AID document argues-- *"For most purposes the most efficient route to food security is to monetize food aid. Even for a public food aid safety net where food aid donor support is available, it is generally more cost-effective to sell the imported food at the port city, then buy local foods in the interior to serve the nutritional needs and tastes of the local safety net recipients at lower cost"* (L Tweeten, J Pines, S Reutlinger, J Mellor 1992 Food Security Discussion Paper, AID/FHA).

Isn't PVO monetization primarily for the purpose of raising money?

Most frequently, yes, so long as the money is in support of food security. Most PVO programs have had the intermediate objective of raising revenues in local currencies. But because the monetization uses PL 480 resources, these local currencies then need to be applied to activities that promote food security. PVO proposals for monetizations having no articulated relationship to food security have been turned down by AID, even though they were important and well-planned.

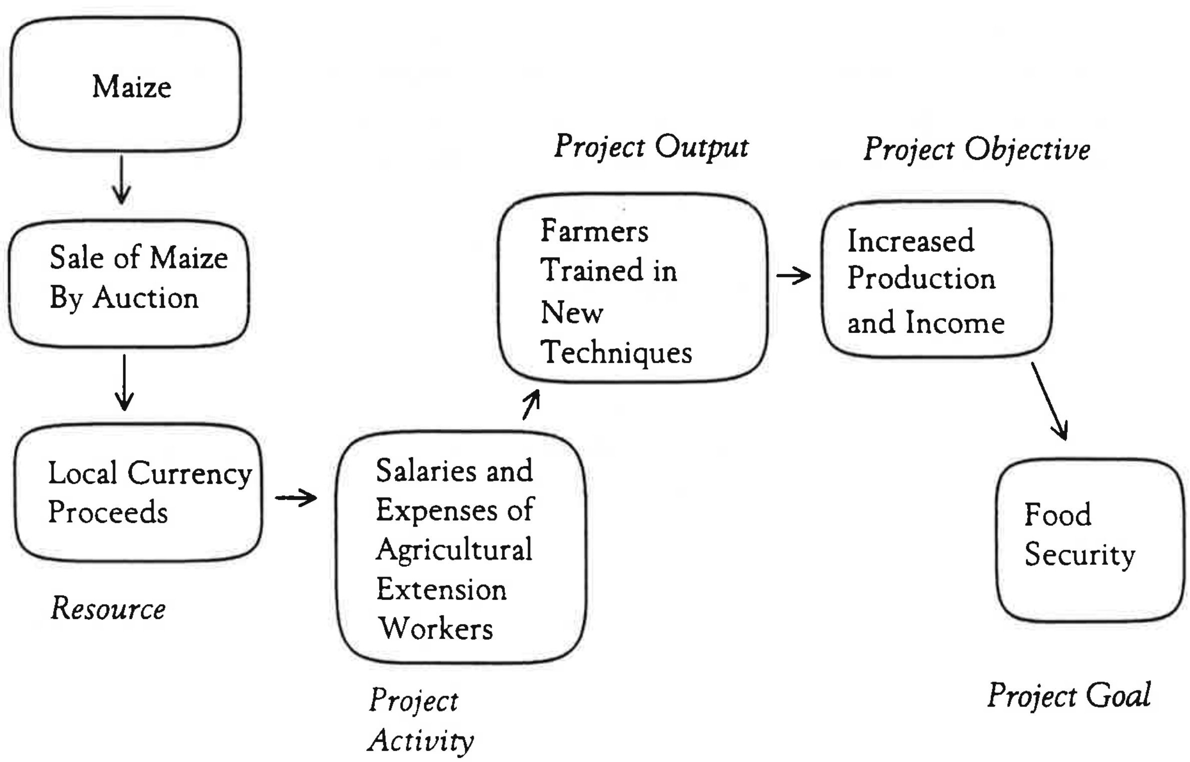
Because monetization is often a means for raising money, and not an end in itself, it can be misleading to talk about a "monetization program." Some professionals suggest that it is best to refer to the monetization as one component of an overall country program but not a program or project by itself.

Are there other possible objectives related to the sale of food itself?

Yes. Over the years PVOs, cooperatives and international NGOs have used monetizations, to accomplish a surprising array of objectives. Monetization can:

- *maximize revenue*
- *transfer income to consumers*
- *get food to local markets and to consumers*
- *stabilize or lower consumer food prices*
- *liberalize markets*

Box 3-a. An example of how sale of a commodity can be linked to food security.



- *facilitate market interchange*
- *promote private sector development*
- *reduce food losses and violent theft of food*
- *support entrepreneurs*
- *support food/farm cooperatives*
- *support struggling governments*
- *strengthen local counterpart business and accounting skills.*

When should a monetization seek to accomplish these objectives in addition to raising cash?

The objectives of the monetization are determined by you. Do not depend on the resource and its potentials to drive your PVO efforts. Often PVOs using monetization only to raise revenue find that the sales process can also have beneficial impact on the development and competitiveness of local markets. A well conceptualized monetization might have multiple objectives. As discussed in

Box 3-b. Examples of distinct activities, outputs and objectives supporting food security.

ACTIVITIES	OUTPUTS	OBJECTIVES	GOAL
* business training	skilled managers	increased crafts output	
* building village grain banks	grain silos capable of storing millet	grain carryover from year to year	
* MCH logistics expenses paid	5,000 children fed	ensure stable consumption among vulnerable	
* cash for work in agroforestry	20,000 trees planted	reduce soil erosion	
* road upgrade and maintenance	500 miles of roads in place	permit all-season access of food imports	
* pay for media programs on nutrition	200,000 hear about vitamins	dietary practices improved	
* pay unemployed cash wages	20,000 receive means to buy food	famine severity reduced	
→	→	→	Food Security

chapters 10 and 16, some of the types of sales that raise the highest revenues also help to support the smallest traders who are merely trying to break into the market.

Food assistance that is monetized is increasingly seen as a means to help entire countries make the transition from state-controlled economies to more open, efficient economies. Food aid monetization has been used in the last few years to demonstrate auction mechanisms in countries such as Mongolia, Nicaragua, and former members of the Soviet Union. In chapter 13 there is discussion of how to relate food sales, price effects, and nutritional impact.

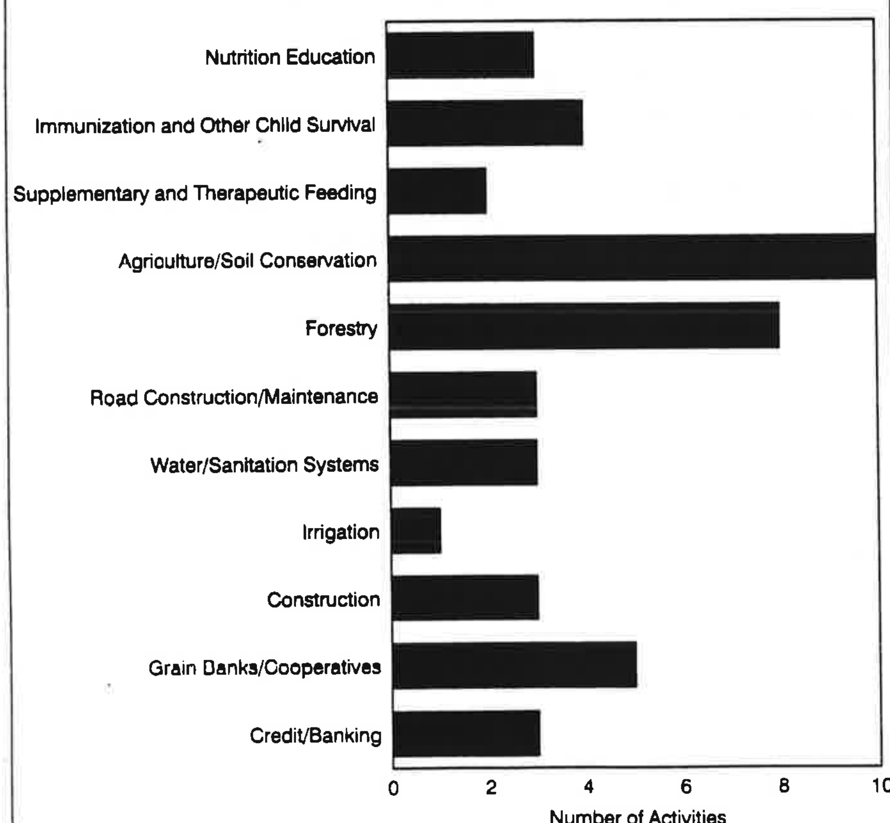
Each objective you choose entails its own cost. Be very clear in what you decide your objectives are and what they are not. Selling to cooperatives at subsidized rates, or selling specific commodities to help certain consumer groups entail costs to your program and compromises the efficiency of your monetization and reduces the revenues you raise. These costs and tradeoffs should be clearly identified in your written operational plan.

What have been the main uses of the cash from monetization sales?

A review of the applications of the local currency proceeds demonstrates that they have supported, at one time or another, almost every type of project that PVOs conduct in developing countries. As seen in box 3-c, proceeds are used more frequently to support projects involving agriculture, soil conservation, and forestry. Monetizations have also frequently helped to support the expenses associated with feeding, nutrition, and child survival programs.

In recent years monetization has been increasingly applied to innovative projects that help communities with their financial needs such as revolving credit funds to support startup expenses for small farmers, or village grain banks that allow communities to maintain

Box 3-c. US PVO activities supported by monetization in 1992.



carry-over stocks from season to season thereby help to mitigate drought and famine. Box 3-d describes a creative project supported by monetization, that uses locally purchased foods as a means of establishing local cereal storage, to help reduce year to year changes in food access. An alternate form of monetization is the donation of food directly to farmer cooperatives that store and market cereals.

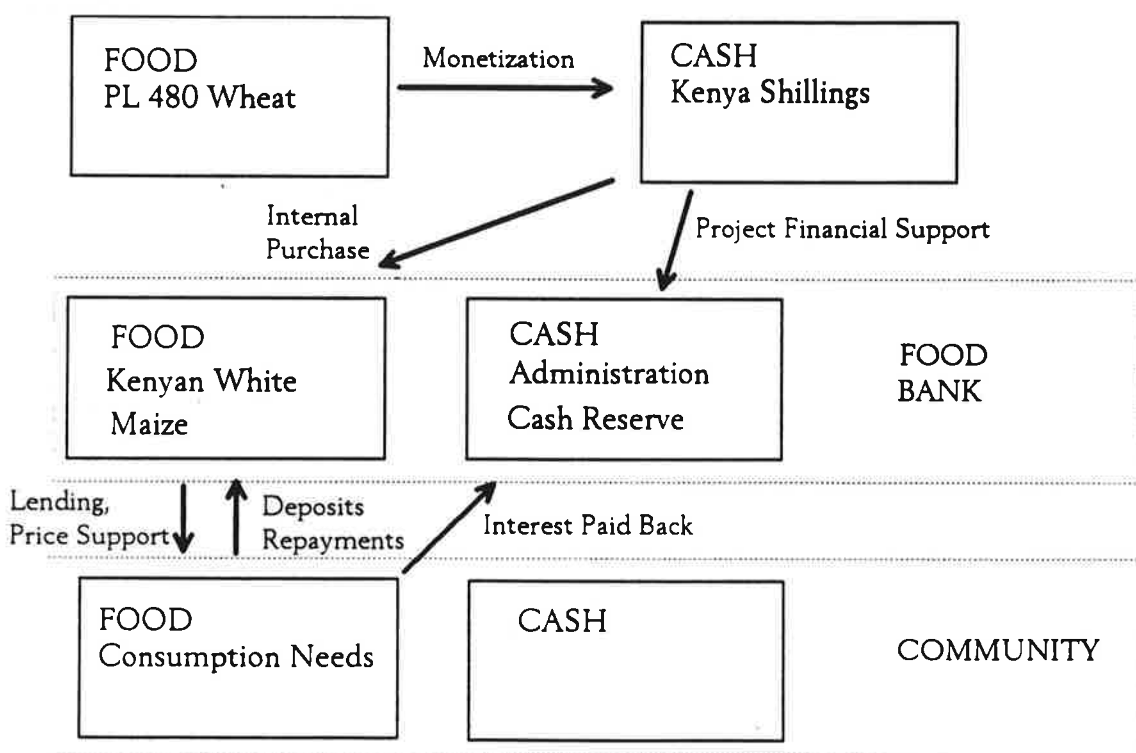
Box 3-d. One PVO's efforts in Kenya involves layered monetizations

One PVO recently proposed to address drought and fluctuations in food availability through a community food security project in the Meru and Embu districts of Kenya. Improving storage capacity and practices in drought-prone areas, through permanent grain banks would reduce food access problems both seasonally and in bad years.

The project would establish a community-managed food bank of at least 75 MTs of corn. The food bank would not include any cash accounts. Members of the community could deposit food into or borrow food. The interest paid by borrowers would be paid in food. This extra food would be sold to cover the administrative costs. After five years the project should have left permanent locally managed food banks in each village.

The US PVO would supply the original buffer stock of white maize obtained by purchasing it in Kenya with cash. This cash would be obtained through sales of PL 480 wheat in Kenya for Kenyan shillings. This mechanism of project support is schematized below:

from B Huth, H Allen, E Moore 1987 "CARE-Kenya Community Food Security Plan of Operations"



Lately there's been talk about monetization as a mechanism for disaster relief. How does it help in emergencies?

Monetization has been recommended as one means of response to slow-onset emergencies involving human conflicts, disrupted markets, and food shortages. Monetization has not been recommended for swift-onset natural disasters such as earthquakes, floods or explosions. In most of these situations markets are not seriously disrupted.

Box 3-e. US Government views on the role of monetization in a famine (Somalia)

"It is tragically clear that sometimes relief in complex emergencies, particularly where order has broken down, has been used by combatants to fuel civil strife and a civil war. ...While we know food has been used as a weapon before... we have now recently reached a new level of food diversions for the purpose of explicitly buying more weaponry.... so the traditional mechanism of just providing relief as free-food distributions may not be the right intervention, the more chaotic the conditions are. There are seven arguments which I would like to quickly present for monetization in the Somali ...and I believe perhaps even in the Yugoslavia context...

"First, we note in Somalia that the number of animals that you need to purchase a bag of grain with is so extraordinarily high now that the average nomadic herdsman can only barter a month's worth of grain for what he could have bartered with six months' worth of grain before the chaos started... So monetization, by increasing the volume of food aid to drive prices down, would increase the nutritional status of people who barter for food using their animals as their resource."

"Second, we noticed just after the United States of America and other donor countries announced a monetization in Somalia,... a sizable drop in the price of food in several cities and particularly in Mogadishu. I asked relief workers why that was and they replied that the merchants were taking all the food they had been hoarding over the last year and dumping it onto the market because they were afraid that if the price went down when the monetized food comes in, that they would not be able to make as large a profit. One of the purposes of monetization, then, is to force hoarded food onto the market...

"Third, if we monetize food with the merchants it is very clear that a lot more paying jobs will be created in the private sector, truck drivers, people to take the food off and on the trucks, retail merchants to sell the food... Monetization will... begin to get the economy moving again and restore the private market system."

"Fourth, by taking the value out of high-priced commodities like rice and wheat, in the case of Somalia, we could reduce the incentive for looting.

"Fifth is that the merchants have been advocates of looting. ...The merchants who did not get food told the looters to go out and loot more food, because it was their only source of supply. ...When the merchants have (instead) a vested interest in orderly and stable markets, they become advocates of peace and stability. Fighting hurts business when markets are functional. In one country in Asia, merchants encouraged looting during a civil war, but when a monetization program was started, they went to the guerrilla leaders and said, 'No more violence, you're interfering with our profits.'

"(sixth), The Somali merchants have ways of taking care of people who steal their food; we in donor countries and relief organizations cannot use those methods. We need to employ the traditional mechanisms by which merchants protect their property in Somalia to support the relief effort."

"Finally, the local currency would be used from the sale of this food by... the NGOs ...on labor-intensive rehabilitation projects ...at the village and the city level. This is extraordinarily important because if you move food into the market in a city and you do not increase people's incomes, they cannot afford to buy it."

excerpted from testimony by the then AID Assistant Administrator, Andrew Natsios, to the WFP 34th Committee on Food Aid in August, 1992

Monetizations however are proving an effective response for droughts, famines and civil conflicts. Governments have often monetized bilateral food aid in response to famines. For example, selling US-donated food in urban areas allowed flexible programming of cash for rural relief during severe droughts in Sudan, Mali and Chad in the mid 1980s. During the 1988 Ethiopian drought getting food aid to affected areas was very difficult because there was only a single functioning rail line. Moving cash resources to affected areas requires less time, less cost and less management.

The 1992 World Food Day: Report President's Report to Congress (Washington DC: AID) explains how the severe drought and threat of famine in southern Africa in 1992 was a problem of great concern because of its enormous scale, short lead time, and the poor infrastructure for implementing food distribution: "Governments and donors agreed upon an innovative system of moving the bulk of the emergency food donations through commercial private sector marketing channels, seeking to dramatically increase supplies available in local markets, rather than depending on traditional refugee-style feeding programs... This... strategy, focused on ...existing markets, allows the people affected by the drought, especially the poorest, to remain in their homes and continue to work to improve their lives. It eliminates the dramatic displacement into camps and the rupture of nuclear and extended families that accompanies traditional famine feeding efforts. It also allows... PVOs to focus much earlier on rehabilitation programs for the post-drought period, such as building water wells and delivering seed."

Box 3-f. A food security review of Mozambique examines food vs. cash in an ongoing crisis.

"In remote rural areas where war or drought has led to severe food shortages, and normal food marketing channels have been disrupted, there is a danger that cash for work employment programs could be highly inflationary, with the increased demand for food serving only to drive up prices... the important point is that the increased demand for food resulting from the increase in employment be backed by an increase in supply of food. In general, where a trading system is functioning, the preferred approach would be for the Government to pay workers in cash and to allocate more food aid supplies to the area, to be sold through normal channels. This avoids the need to set up an expensive parallel food distribution system which undermines existing marketing channels. The increased cash incomes may also stimulate domestic food production where the security situation permits a supply response. Food aid that is monetized in this way helps strengthen domestic marketing and production of food rather than substituting for it. However, where the trading system has been totally destroyed by the war, direct food payments to workers may be necessary.

"Food commodities must be stored, transported to the distribution sites, monitored, and distributed equitably against work completed. These activities require planning, resources and budget... in critically short supply in Mozambique today.

"In contrast, money can be moved around, stored, and distributed much more cheaply than food. In many situations, therefore, it will make more sense to sell food aid through existing marketing channels and use the proceeds to finance measures to improve food security, including employment-generating programs.

"An additional advantage of cash for work over food for work is that the former will also stimulate demand for domestically produced food, such as fruit and vegetables, which in turn will generate income and employment in peri-urban areas. Recent experience with freeing market prices for fruits and vegetables and the strong supply response that has resulted tend to support the thesis that even in the face of war-induced disruptions, farmers and transporters will find ways to increase and deliver food supplies in response to increased demand."

from Agriculture Division and Africa Unit 1989 Mozambique Food Security Study Washington DC: World Bank pg. 100

But during emergencies, don't markets sometimes fail to function properly?

Yes. Yet while being the problem markets can also be the solution. This dichotomy is why some people argue for helping to restore the market system itself. The affected populations may have abnormally low purchasing power, foreign importers are often unable to respond quickly and infrastructure may be so poor that food cannot be moved into affected regions without great expense. Yet in most cases markets can still move food out through dispersed retail networks faster than a PVO can set up comparable pipelines. No matter how massive a PVO program, most of the population of affected regions continues to depend on daily or weekly markets for food.

In conflict/famine situations, food shortages may reflect barriers to the production, transport and marketing of foods. Monetization, it is argued, can re-stimulate those markets and bring prices down. While a famine is getting worse, prices rise which encourages speculators to store food and not sell it, waiting for prices to peak. Thus monetization can quickly break the speculative spiral that often accompanies famine. In 1941 millions died in the Bay of Bengal because of a famine that was entirely a result of a speculative price spiral rather than a result of any food deficit.

Monetization can bring food to a broad consumer population without the often heavy expenses of direct distribution to every affected household. Food sales can use existing or traditional networks of merchants and transporters who know each other and have their own insurance and protection procedures. In some situations the economy is in such a recession that the merchants have nothing to trade. Some people with inventories watch prices continue to go higher and refuse to sell. Monetization, by helping to lower prices, can reverse the speculative increase in prices and the withholding of foods.

Whether because of fear, speculation, war, increased needs, interrupted production, or a decrease in marketing, any resulting food shortage threatens lives within a very short time. Food aid will almost always address the food shortage, making food more available to all, whether it is monetized or distributed freely. The key indicator to observe to identify a food shortage is whether demand has exceeded supply. When this occurs food prices increase. A food price increase of 20% or more --adjusted for inflation-- is evidence of a shortage. When cereals increase 50% to 80% the change is reason to be concerned about famine. Cereal prices can increase over 200% during a famine.

In Liberia, monetization has been one method of simply bringing food into a country still paralyzed by civil strife, occupying armies and a siege around the capital city. An Interagency Steering Committee oversees the conduct of a special form of auction whereby the sale of food is awarded by lottery. The first lottery resulted in 3000 MT of rice sold for $900,000 to local wholesalers. Lot sizes and prices were determined in advance.

What evidence is there that monetization in a famine area will depress prices enough to increase food access for the poor?

There has been not been strong evidence as to how large an effect can be expected. Food aid in general has often been known to stabilize prices, indeed to quickly reverse the gradual rise in prices that characterize famines. The Famine Early Warning Systems Project of AID has observed this effect at the local level, for instance, in Niger and Chad. But PVO monetizations of food aid have been used infrequently, in small portions, and often in conjunction with free food distributions making it difficult to determine the impact of monetization alone.

Recent emergency monetizations in Mozambique and Liberia have brought food into markets and helped to keep food prices from rising, but no studies have been conducted of the proportional increase in the actual consumption by the very poor. In Mozambique and Liberia food sales have tended to benefit urban populations. In Liberia, WFP has experimented with different sales techniques to bring large quantities of food into the markets. Markets were relied upon because there was no adequate network for free food distribution

In Somalia it has been argued that the proposed monetizations provide little guarantee that the food sold to Somali traders will be transported to those markets serving the needy. The same violence

Box 3-f. A suggested typology of how to monetize commodities at different phases of a famine.

PHASE	Primary Benefits from Monetization	Primary Difficulties	Most Appropriate Strategy	Most Appropriate Commodities
Early Warning	Stabilizes decreasing terms of trade for agricultural staples; reduces displacement of populations from farmlands.	May be unclear when or where to target sales, possible disincentives to production.	Flexible, timely sales during hungry season but using retail networks at village level. Incentive systems to support rural dry-season projects.	Staples but in moderate volume; high-value items in urban areas.
Initial Relief	Swift method of remedying food supply deficits without pre-existing direct distribution networks and without high operating costs.	Poor security situation prohibits proper auctions, safe banking, or free flow of information with buyers in target regions.	Where possible, closed-circuit sales in support of public works projects. Internal purchase, cross-border sales, large sales at port.	High-caloric density, low bulk, inexpensive cereals, perishables, edible oils.
Massive Relief	Complements free distribution by utilizing and protecting professional merchants and market channels.	Preventing re-export or hoarding during period of low domestic prices or glut of centrally- located marketed staples.	Multiple sales with limited lot sizes at border for convenience, or to farmer coops or retailers if possible.	High-value oils, pasta, sugar, milk, flour, rice that complement freely distributed foods.
Rehabili-tation	Helps transition from food relief back to normal trade routes, helps reduce potential for food aid dependence.	Disincentive effects on local production more likely and significant.	Highly competitive sales through well-publicized mixed lot-size, sealed-bid auctions to wholesalers.	Raw foods for mills processors, high income- transfer goods

that endangers regular food relief may also prevent merchants from moving food to areas of need. It is also argued that the most needy have no money, income or jobs with which to purchase food from the markets. Because emergencies are characterized by sharp changes in conditions, it may be that monetization designs should include which phase is being targeted and why. A typology of which types of monetization might be appropriate at different phases is offered in box 3-f.

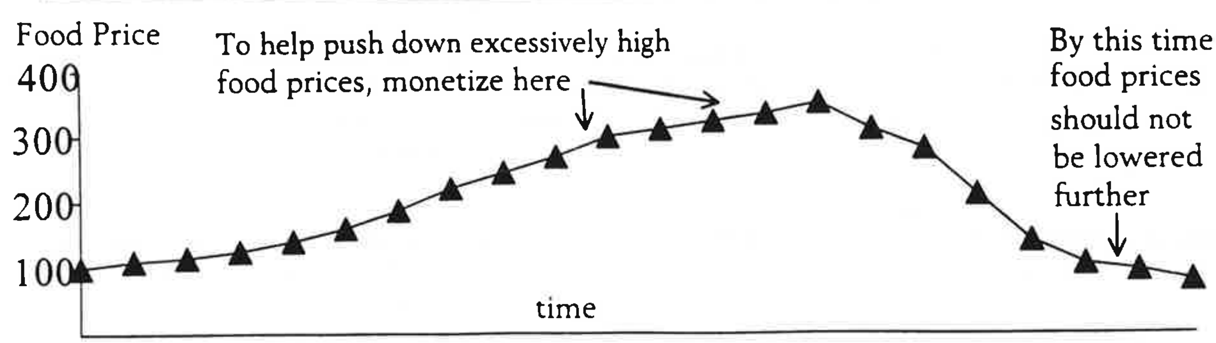
How can an international PVO with a small staff make sure that the monetized foods help the populations most in need?

The issue is how to intervene in the market so that the marketing margins of the traders including, wholesalers, don't expand, and prices are stabilized at the retail level in the intended areas. Much of the redistribution occurs naturally because households substitute one commodity for another, and merchants move food from areas of surplus to areas of deficit to take advantage of price differences.

PVOs can seek to obligate wholesalers and traders to transport and sell in specific markets through contracts and subsequent monitoring. This was the strategy used by the International Rescue Committee in 1992 to target rural markets inside Somalia by buying food in Kenya and selling to traders across the Kenya-Somalia border.

The PVO can directly move food for monetization into certain regions through its own truck fleet, by airlift or contracting transporters. At the regional level PVO sales are more likely to remain in the region or to directly reach regional retailers. The PVO can also sell directly to farmer or consumer cooperatives who have a vested interest in making the food available at the household level. This method also tends to support institution-building and domestic production. Extending this line of thought, the PVO can distribute the food directly to villages and households and let them resell the food and enjoy the income effects. Either way, there is a regional price-depressing effect.

Box 3-g. The benefits through price-effects depend critically on the timing of the sales



Famine mitigation people speak about different phases of a famine. When is the best time to monetize?

Proper timing is crucial, but timing a monetization is one of the most difficult things to do. The monetization should be timed to catch food prices when they have begun to rise and thus help bring them back down. Food should not be monetized at a point in a famine relief when food prices have already been brought back down.

Box 3-f presents some of the considerations in tailoring a monetization during different phases of a famine cycle. The early warning phase may be the most difficult to identify because so many countries seem to be in serious drought that *might* lead to famine, though few do. There are numerous early warning systems in place using satellite and ground data to attempt to predict the likelihood of a serious famine developing. During this phase, though, populations have not moved, and the economy has not been disrupted. Therefore, the goal of food assistance should be to soften the blow of the drought, by using local market distribution networks as much as possible. Depending on the circumstances, the proceeds might be programmed to village-level or district-level dry-season activities that do not in any manner discourage overall production in the subsequent years.

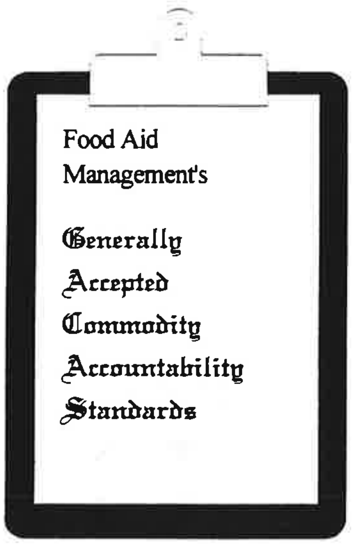
The relief phases are more easily defined by increasing mortality and social collapse, and by increasingly urgent, stepped-up efforts by humanitarian relief organizations. During these phases, the PVO may be seeking to monetize as a means of addressing a severe food supply imbalance in as short a time as possible. Mechanisms, constraints, possible disincentive effects and approvals are relatively less important than timeliness and in getting volumes of high-caloric foods into target regions.

The monetization program for the 1991-93 Somali famine was originally proposed as a means to bring food into Somalia during a period when normal food operations were meager, problematic or impossible because of violence, uncertainty, and inability to negotiate with warring factions. During this period when free food distribution was so difficult, food prices did rise several-fold. Unfortunately, no monetization was affected. During the months that monetization proposals were being prepared and agreed upon by the PVOs, large-scale food distribution had also increased, and the price of food in Somalia was falling fast. By the time monetization foods were ready to be sold, marketplaces in Somalia were well stocked with inexpensive food, thus the intent of the monetizations had to be entirely reconsidered (see box 3-g).

FURTHER READING:

1. *H Bruton, C Hill 1991 The Development Impact of Counterpart Funds: A Review of the Literature Washington DC: AID;*
2. *R Hay 1986 "Food aid and relief-development strategies," Disasters Vol. 10 #4;*
3. *S Vosti 1992 "Constraints to Improved Food security: Linkages Among Agriculture, Environment and Poverty" Washington DC: IFPRI;*
4. *S Coate 1989 "Cash versus Direct Food Relief" Journal of Development Econ 30(2): 199-224*
5. *S Hansch 1993 Food Security and Nutrition in Somalia, an Assessment Washington DC: Food Aid Management*
6. *S Maxwell, T Frankenberger 1993 Household Food Security: Concepts, Indicators, Measurements UNICEF and IFAD*
7. *J Abbott 1986 Marketing Improvement in the Developing World: What Happens and What We Have Learned Rome: Food and Agricultural Organization*
8. *W van der Geest 1991 Food Security: The Cereal Market Policy Model Oxford: Food Studies Group Working Paper #3*
9. *M Ravallion 1992 Poverty Comparisons: A Guide to Concepts and Methods Washington DC: World Bank Living Stands Measurement Study Paper No. 88*
10. *H Alderman, M Chaudry, M Garcia 1988 Household Food Security in Pakistan: The Ration Shop System Washington DC: IFPRI Working Paper #4*
11. *O Obasanjo, H d'Orville editors 1992 The Challenges of Agricultural Production and Food Security in Africa Washington: Crane Russak Pub.*
12. *P Pinstrup-Anderson 1993 The Political Economy of Food and Nutrition Policies Baltimore: Johns Hopkins University Press*
13. *B Huddleston et al. 1984 International Finance for Food Security World Bank*
14. *S Vosti 1992 Constraints to Improved Food Security: Linkages Among Agriculture, Environment and Poverty Washington DC: IFPRI*

CHAPTER 4.
EXPENSES, RISKS, CONFLICTS, STANDARDS, AND CONDUCT



The up-front costs of examining whether and how to monetize sound high. How can these be paid?

The up-front appraisal, planning, and negotiation expenses may easily exceed $100,000. The cost of conducting one particular monetization in an African country is projected at $1.4 million. In contrast, another PVO conducting regular monetizations in Central America found its monetization-related expenses to be merely $4,000 a year. A large multi-PVO monetization in South America has exceeded $300,000 in expenses. Often PVOs will apply unrestricted funds, private contributions, or AID planning or strengthening grants to the costs of developing a proposal for a monetization.

Your PVO should always be conscious of opportunities for various available sources of funding. Possible sources are AID strengthening grant funds, Farm Bill "202(e)" funds, and local USAID support. Without these types of grants, it is difficult for new or smaller PVOs to initiate a monetization. (see chapter 5).

Can these up-front costs such as appraisal and planning a monetization be paid for by the monetization itself?

Yes and no. Indirect cost recovery from monetization proceeds is now allowed (see chapter 22). If you conduct ongoing sales throughout the year, many of your expenses can be recouped. But it is not wise to plan a monetization in which the monetization proceeds pay for previously incurred costs. What if your appraisal results in a recommendation that monetization should not be pursued? One PVO avoids applying monetization proceeds to headquarters costs because its private donors might not approve of food aid paying for expenses in the US.

What's the best way to investigate permitted activities for monetization to support?

Whenever uncertain about what activities or expenses are allowable, put it in writing to AID. The PVO is not permitted to apply proceeds to activities that are not in the proposed operational plan. There have been cases of expenditures verbally authorized by AID staff only to be later disallowed following an audit by the Inspector General. Therefore, always get it in writing

Some AID regulations can be waived where a case can be made for a waiver:

"The Operational Plan submitted by a cooperating sponsor may propose, and justify, the waiver of any section of this Regulation that is not required by statute. If AID approves a waiver, the specific section or subsection waived will be identified in the Transfer Authorization signed by the cooperating sponsor and AID or in an attachment prepared by AID that is appended to the Operational Plan." (Regulation 11: 211.1(b)))

What are the most common expenses covered by monetization?

Partial monetizations are frequently used to cover the expenses associated with delivering commodities to feeding centers. These are known as internal transport, storage and handling (ITSH) expenses (see box 4-a). Partial monetizations also frequently support the staffing, review, and planning of further monetizations. 100% monetizations, in contrast, have been used to cover the local administration and implementation expenses for the range of project types discussed in chapter 3. How monetization proceeds are applied is dealt with at greater length in chapter 22.

Food distribution programs have occasionally been subject to negative publicity concerning instances of loss, theft, diversion, and the like. Wouldn't currency proceeds pose an even greater risk of theft and scandal?

To a degree. Cash may be more tempting to steal or divert for personal gain. But cash is also generally easier to protect and monitor if kept in an appropriate account. What is a greater danger to the PVO is the conduct of business itself and the types of behavior and public perception that follow.

Box 4-a. Terms about commodity costs.

FAS or f.a.s.
Free alongside ship

Transport term whereby seller is obligated to procure and deliver goods alongside the vessel, and clear them for export. The FAS price is the price of a commodity including procurement, shipment and delivery to the site of export. In the case of Title II commodities, it includes the cost to the US Government to buy the foods and have them delivered to a port such as New Orleans for shipment overseas. The procurement cost depends upon the commodity: from $140-$700.

FOB or f.o.b.
Free on board

Similar to f.a.s., except that the supplier pays for the cost of loading the food on the shipping vessel. FOB and FAS both essentially represent the procurement price.

CIF, C&F, or CFR or c.i.f.
Cost, Insurance and freight

The value of procuring, loading, shipping and covering risk on commodities to a foreign destination. The seller is obligated to cover the cost of the goods, the freight charges to the named port, the freight charges to the overseas destination, and the cost of insurance against loss. The CIF price is essentially the FAS price plus ocean shipping expenses. It depends both on the commodity and the distance to the country. Ranges typically from $250-$900

ITSH
Internal transport, storage and handling

The major complementary expenses of moving food within a foreign country from port to final distribution, as paid for out of the PL 480 account. It depends on how and where in a country the food will be used, and on the state of geography and infrastructure within a country. Per MT rates range from $50 to $500.

Lawrence Barbieri of Support Services International explains: "*Usually when a business attempts to maximize profits it is done with an awareness that greater risks are involved than in a more controlled sale. If losses occur, a business can plan to make up for these losses with the sale of other products. A business may actually choose to lose money on a given commodity ("loss leader") in order to advance market share and increase profits on other lines. A PVO does not have this alternative. Any risk taken to maximize profits that results in a loss of funds is a cost paid by the proposed beneficiaries of a project denied the expected full funding. It is a loss you can't recover and the USAID Mission probably will not be very sympathetic. You gambled and you lost.*"

Barbieri concludes that *"Monetizing commodities with a social purpose is not impossible. At first glance it requires more effort, but the end result will better reflect the PVO's fundamental purpose and goals. However, when an organization such as a PVO ignores its fundamental purpose and tries to be something else, such as a grain merchant, it must be ready to pay the price. To take the chance of being perceived by local governments and the public as profit-driven, rather than as people helping people in need, is a heavy price to pay.*" (see boxes 4-b and 4-c for further discussion)

Has involvement in monetization harmed any PVOs? Are there any risks that should be of concern?

No monetization has been the subject of a scandal, partly because PVOs have carefully approached monetization with attention to potential risks. However, people remember the things that went wrong about a program more often than they do its accomplishments and food aid is particularly visible. Although PVOs would not consider adopting policies that might encourage the breaking of any laws, the very business of conducting large sales pulls PVOs into a system in which corruption frequently plays a part. PVO emphasis on "getting things done" may conflict with local business practices. In many circumstances the everyday conduct of business may involve many solicitations for payoffs and bribes. AID instructs:

> *"The cooperating sponsor shall use commercially reasonable practices in construction activities and in purchasing goods and services with monetized proceeds or program income; maintain a code of standards of conduct regarding conflicts of interest; carry out procurement transactions in a manner to provide open and free competition to the maximum extent practicable*" (AID 1992 Regulation 11: 211.5(k)(6)(i))

Risks in the conduct of food sales include:

- Damaging organization's public reputation;
- Damaging the public perception of all PVOs and of foreign aid in general;
- Damaging the PVO's relationship with local counterparts and government;
- Damaging local perceptions of PVO's aims, intent and practices;

Box 4-b. "Images of Moral Bankruptcy" -an editorial by Lawrence Barbieri

Monetization is like a loaded gun. Care and alertness must always be used when it is present. Your PVO is the target and profit maximization could pull the trigger!

Let us start from the beginning as stated in the Agricultural Trade Development and Assistance Act of 1954, Section 2 (Amended), United States Policy. "It is the policy of the United States to use its abundant agricultural productivity to promote the foreign policy of the United States by enhancing the food security of the developing world through the use of agricultural commodities and local currencies under this act to: (1) combat world hunger and malnutrition and their causes; (2) promote broad-based, equitable, and sustainable development, including agricultural development; (3) expand international trade; (4) develop and expand export markets for United States agricultural commodities; and (5) foster and encourage the development of private enterprise and democratic participation in developing countries. These are the goals of Congress. While the law did not specify how local currencies should be generated, it is difficult to imagine support for a process which ignores these goals.

Now let us remember our own organization's fund raising. The goals of most PVOs are very clear. People coming together, donating money, goods, and services to help people worse off than they are. Malnourished children and needy people, these are the pictures seen over and over again as the call to help goes out.

Juxtapose these images with full warehouses, filled store shelves, and price tags with your PVO's name on it. Imagine trying to explain this to your individual donors, CNN, or the Congress. To them, monetizing just as a profit maximizing venture could be technically legal but morally bankrupt.

Monetization is the act of exchanging food for money. How can this act try to meet the expectations of Congress and the promises of your PVO's publicity. Let us consider some possibilities: As an example, due to a country's structural adjustment program, the price of basic commodities have dramatically increased in urban areas. Poor families who have not seen a concurrent increase in their own personal income no longer have the ability to provide an adequate diet for their families.

The PVO has commodities but needs local currency to support developmental activities in the country. The PVO has some options: 1) The PVO could sell the commodities, only looking for the best price (profit maximization) and use this money to fund developmental activities. With this type of sale the nutritional status of the poor families will not change. 2) PVOs could sell some in the above manner and distribute the balance of commodities directly to the poor. The proceeds would pay for the costs of distribution, but there wouldn't be money to fund other activities.
3) PVOs could find a way to sell the commodities and also assist needy families. For example, PVOs could arrange a procedure with private traders wherein eligible families, identified through a predetermined system, could purchase food at a subsidized rate. The PVO would also allow the merchant to purchase an additional amount of commodities which could be sold at market rate. These proceeds would be used to support other developmental activities.

PVO's would have reasonable grounds for justifying to A.I.D... a higher allocation of commodities for monetization. In this way they would have necessary funds for developmental activities (in effect maximizing their profits) and still meet the spoken and unspoken expectations of their constituency. The private merchant would have a product to sell and could make a profit. With some thought, this could be a means of providing credit to assist in the development of the nascent private sector. Lastly, the individual would have the ability to buy food with some dignity, not just receive a handout.

We have mentioned potential public perceptions or misperceptions of monetization. We have seen how monetizing with a social purpose can provide funds and help people. The last issue to be discussed is the inherent **risk** of being a business, maximizing profits, and appearing to be a moneymaking organization.

Can PVOs afford to be perceived as profit-making businesses? Many possible ways exist to monetize commodities and still achieve social goals. It will be to every PVO's advantage to seek them out and pursue them.

submitted to Food Aid Management by Lawrence Barbieri of Support Services International, 1992

- Undermining efforts of sub-recipients and counterparts in their food purchases, sales, and market activities;
- Calling into question the systems of personnel relationships and internal controls within the local PVO office;
- Damaging to long-term relationship with potential buyers;
- Involvement in criminal matters that may include court expenses, staff time, punitive findings and imprisonment;
- Exposure to liability and compensatory fines against aggrieved businessmen;
- Cessation of country program; and,
- Financial bankruptcy.

How can these dangers be avoided?

Mitigating these risks should include (1) written PVO policies and references by which a PVO thinks through its attitude toward work in difficult situations, (2) formal publication of these policies for staff, AID and for the record, (3) communication of PVO policies so field level counterparts and buyers are aware of why the PVO's staff is unable to consider certain transactions, and (4), staff training to put staff in role-playing situations so they understand how to respond to a variety of confusing choices.

The public sales arena raises the risks to PVOs one notch higher than normal operations. Because many independent buyers are watching how much you have to sell, how much you sell, and to whom you sell, any unexplained disappearance of your commodities may potentially lead to jealousy, and accusations of underhanded dealings, unfair trade, or partisanship.

For this reason, some have recommended that PVOs actively explain the purposes, methods, history, and roles of monetization to the media at all stages. It may be very important, for instance in an emergency, to be frank to the press from the very beginning why food is being sold while potential recipients are going hungry. The media are much more likely to run a negative "scandal" angle against the PVO and any food sales if they feel that they uncovered something that had the appearance of being kept quiet.

In developing its own code of conduct, a PVO might consider provisions that would address potential difficulties related to the conduct of business in different cultures, including the pressures to move commodities to meet deadlines and in emergencies. While framing its own codes and wording, each PVO may want to consider one or more provisions to address or restrict each of the following:

- the receipt of goods, services, or cash for which they do not receive written receipts;
- intentionally giving out misleading information about PVO activities;
- demonstrations of favoritism or bias against potential business associates or clients;
- willful deceit resulting in harm to another (fraud);
- earning profits by personal involvement in and knowledge of local food markets;

Box 4-c. "Monetize Aggressively, Or Not at All" -an editorial by Ron Shaw

As a means of achieving the goals set out in the legislation, one can only wonder why 100% PL480 Title II monetization was so long in coming. By providing PVOs with heretofore unavailable cash resources, monetization can combat world hunger, malnutrition and their causes, and can promote equitable, sustainable development while the process of monetization itself can foster and encourage the development of private enterprise and democratic participation in developing countries.

In considering the benefits and risks inherent in monetization one overriding fact must be kept in mind: in most sectors, PVOs can do a great deal more toward achieving their development objectives with the cash proceeds of food monetization than with food itself. The simple truth is that food as food is hard to program, hard to manage, and its output is even harder to measure in terms of lasting benefits.

It is also true that most PVO's have access to much larger quantities of food than they could ever effectively program, while, at the same time, they constantly face a shortage of cash. Monetization solves both difficulties at the same time. The argument that monetization should not be simply a "profit-maximizing venture" is understandable, but misses the point. The objective is not "profit-maximization" for its own sake, but the generation of the "maximum" amount of funds for investment in PVO relief and development programs. Monetization should, therefore, be conducted AS IF it were a profit maximizing venture.

To most PVOs, monetization has its obvious attractions (some would say temptations) but it does bring with it certain risks. One of the most obvious risks is that of (unintentionally) creating disincentive to local agricultural producers, commodity distributors and vendors (the very people PVOs set out to assist).

Profit maximization, at least in the form of price maximization, is the surest means by which a PVO can ensure its monetization activities will not have a negative effect on local production and prices. In fact, by seeking the "best" price, the PVO will contribute to the creation of market forces which encourage domestic production, distribution and marketing. Address the risk of bad press and public misperception by proactively "selling" the concept of monetization and its benefits.

In many cases, profit or price maximization will also contribute to the redistribution of wealth and structural adjustment (official or unofficial). In many countries, the rural (and urban) poverty which PVOs try to address is the result of government policies which have disproportionately benefited the urban elite at the expense of the rural peasant. Proper selection and marketing of PL480 monetization commodities will extract wealth from the urban elite (who buy expensive imports in any case) and reinvest those proceeds or "profits" in a more equitable manner.

By targeting its monetization efforts to this urban elite market, monetization will, to the extent that it displaces other imports, further benefit the host country through savings in all important foreign exchange, thus contributing to overall economic rehabilitation. While a PVO may see programs designed to stabilize prices and provide "subsidized" food to the poor as a monetization approach more compatible with their mandate, such efforts are self-defeating. Such an approach too readily opens the PVO to disincentive charges and will serve only to perpetuate the ineffective and inefficient market interventions which has so greatly contributed to the lack of food security PVO's are attempting to address in the first place.

Many PVOs also see a threat to their reputations and private donor base as they imagine headlines reading "PVO Sells U.S. Food Aid While Thousands Starve." The danger of potential public misperceptions is real enough but it is one that lies primarily in the (mistaken) belief of many PVO's that it is somehow immoral to sully themselves with commerce...and downright sinful to do so to maximize benefit.

PVO's must recognize monetization for the resource that it is and then learn to take the initiative and present monetization to the public, both in the U.S. and in the host country, as an opportunity to achieve sustainable development goals which food itself could never achieve.

prepared for FAM by Marine Overseas Services 1992

- sharing insider information with others who might directly or indirectly compete in the market ("insider information" is defined as privileged information concerning business activity that has not been made public and is therefore illegal to trade on);

Other clauses might specify procedures and internal controls to ensure clear public disclosure of PVO business activities, strategies and goals; projecting an image as to the seriousness and efficiency of the program; dated, written documentation of all transactions; and use of professional judgment in all decision-making and handling of resources. Regarding written agreements, one PVO maintains a policy that states:

What statements of procedures, guidelines, regulations or policies on behavioral standards by your PVO are available to you for either staff training or citation in public proceedings? As will be reiterated in later chapters, it is strongly recommended that the PVO segregate its monetization program from other project activities as completely as possible (even reducing communication between the staffs), and reduce the objectives of any monetization to as few as possible (see box 4-c). The PVOs participating in Food Aid Management have agreed that each PVO should establish its own manual explaining its procedures and policies (see box 4-d).

Box 4-d. The following principles on accountability from FAM's Generally Accepted Commodity Accountability Principles explain the importance of having organizational policies and the necessity of using contracts

Principle I-4 :

"Commodity management organizations (such as PVOs) should maintain a Commodity Accountability Policies and Procedures Manual describing the organization's policies and procedures regarding commodity accountability. The policies and procedures governing the operations of the organization should be published so that all staff are aware of them and guided by them in day-to-day operations."

Principle II-4:

"Commodity transactions should be recorded in a timely manner so that the organization's financial records provide the status of commodity inventory balances, issuances, and value. Written procedures should be included in the organization's commodity accountability policies and procedures manual or some similar publication of instructions.

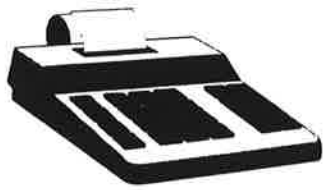
Principle III-4 :

"Commodity management organizations must ensure that accounting and accountability responsibilities and liability limits for accepting and using resources are clearly specified in agreements and contracts with donors, subrecipient organizations, transporters, and suppliers of goods or services. The agreement and contracts must be legally binding and specify the period for which they are in force. Most of the difficulties in food aid programming stem from organizations' failure to prepare realistic and sufficiently detailed contracts. More attention needs to be focused on describing the specific accountability and liability arrangmenets appropriate to individual commodity programs. In this regard, contract issues that should be addressed by PVOs and NGOs include: (1) an explanation of the roles and responsibilities of each party, (2) how accountability for the commodities is to be established and maintained, (3), the definition and extent of financial liability of each party, (4) how disputes will be arbitrated, (5) what will constitute the use of "force majeure", and (6) contract cancellation and penalty provisions."

➢ ***FURTHER READING:***

1. *Food Aid Management* *Generally Accepted Commodity Accountability Principles* *Washington DC: FAM;*
2. *PVO Behavioral Standards* *Food Aid Management;*
3. *EJ Meddaugh 1983* *Guide to Professional Accounting Standards* *New Jersey: Prentice-Hall*

CHAPTER 5.
THE APPRAISAL: PVO NEEDS AND CAPACITIES



What does an appraisal involve? How does a PVO start?

A full appraisal includes an examination of commodity markets, country port and storage facilities, and holding meetings with government and business representatives. Before taking these other steps, the PVO should first determine its needs and the extent to which it can responsibly manage a monetization. First the PVO must calculate the funding needs of the projects it believes will need local currency fund support. Steps to take:

- Calculate project needs. Do you have a description or "Operational Plan" for your program? Is it ongoing or a start-up? Clearly identify the activities to be performed, the staff size, and all categories of capital purchases and recurrent costs.
- What are your cash/capital requirements for start-up expenses, purchase requirements, or ongoing expenses? Will certain expenses be reimbursed in future years through cost recovery components of the project's activities or participant contributions? Estimate the stream of recurrent expenditures related to a project during the next two to three years.
- Calculate the total program currency needs. Which activities cannot be self-supporting or would not be covered by other contributions (e.g. government contributions)?
- Calculate the additional costs of initiating and following through on a monetization. Managing a monetization account will involve risks and direct expenses (see chapters 23-25). Include the cost of protecting the proceeds in your budget submission; it is the legitimate cost of doing business. What are the real costs of storage of goods and payment for services which will be needed later? Claim these costs as well.
- Think through how your project is related to food security and why monetization may be a particularly appropriate mechanism of support. Would your development impact be achieved through a simple cash

Chapter 5 Action Checklist

☑ ***List project activities.***

☑ ***Identify expenses related to these activities (participant support, travel, transport, fuel, vehicles, supplies, utilities, rent, construction, distribution expenses, casual labor, salaries and benefits, etc.)***

☑ ***Estimate expenses related to the sale itself, reports on the sale, financial monitoring, and to managing a local currency account.***

☑ ***Assess PVO staff capacities for conducting sales, negotiating with government entities, and managing large currency accounts.***

☑ ***Assess PVO and counterpart capacities to inspect, clear customs, store, safeguard, reconstitute and manage food supplies.***

grant, without using food aid at all (see box 5-a below)? Would that be more or less efficient than getting involved in a market sales program?

What funds can be used to support a monetization?

Monetization has been referred to by some as a last resort source of project support. Sales proceeds often complement other donor cash support in covering field expenses. Between $10 and $13 million of cash funds are offered by AID to support food programs (referred to by the part of the Farm Bill, as "202(e) funds"). These are used to support the startup of new programs and the ongoing personnel, ITSH and administrative costs. The 202(e) funds are used explicitly to support field expenses related to the conduct of food aid They will not be applicable to headquarters expenses, and they can not be spent on the project activities themselves, merely on the support of the food management. However, these funds **can** be used to help support a monetization. To appraise and propose a monetization, PVOs can seek funds from AID's Institutional Strengthening grants (ISGs), which are allocated to bolster a PVO's capacities and systems at the level of its headquarters.

For an organization like CRS, which conducted 35 sales of Title II foods between 1989 and 1992, monetization is one element in an array of funding sources that include donations from different governments as well as unrestricted private donations. PVOs often monetize because monetization, despite the burdens it carries, may be a more reliable funding source than other donor sources. PVO staff have commented that the reason they monetize instead of seeking other support is:

(1) In some circumstances, it can be easier for a PVO to get a monetization proposal approved than other proposals for more restricted grants; this is particularly if the PVO is already involved in food distribution; and,

Box 5-a. A listing of factors that might call for monetization instead of direct food distribution.

1. The objective is a general income transfer.
2. Targeting within a household is easier using cash transfers.
3. Social traditions require remuneration in cash; for instance, in a public works scheme.
4. Food is available to buy locally or is likely to become available given increasing purchasing power.
5. Government or sub-recipient bureaucratic managerial capacity is adequate for deposit/transfer/expenditure and auditing of cash funds.
6. Additionality of cash payments and their targeting of the poor assured or possible to arrange without violating labor laws, minimum wage regulations, government practices, or local customs.
7. Cash-supplementation of specific target groups is acceptable and does not lock the donor into uncomfortable phase-out or taste-dependency situation.
8. Cost-efficiency favors sale, deposit and programming of cash funds over direct distribution.

(2) It affords the PVO better control over the availability of funds. In a review conducted a few years ago by John Snow International, the authors explained how two PVOs' projects depended on local currencies made available by the local government (and AID) and how these suffered unpredictable, drawn-out delays: *"CARE is still waiting for 1.6 million Quetzals approved as an ESF grant for expanding urban food for work project to four new cities. The commodities are on the way and the money is not yet available. CARE understandably laments that it did not instead monetize Title II commodities to finance the expansion."*

Choosing between cash and food in project support involves many variables, some of which are listed in boxes 5-c and 5-d. Some of these have to do simply with what is available from the donor. Others have to do with how the resource will be used. In 1991 CARE proposed to distribute cash in a project in Nicaragua; requiring monetization to raise the cash. Save the Children has found that food aid sales fit nicely with the suppport of foodgrains banks (Burkina Faso), and Famine Early Warning systems (Ethiopia).

One PVO in Indonesia found that food was traditionally used in inter-household sharing for volunteer-based village works projects. Cash transfers to village members working on these projects would have changed the nature of the work from volunteer to employment. Conversely, one PVO recently phased out its food distribution programs in Ghana because food's symbolic value required the local leaders to ensure that it was distributed equitably to all in the region and not targeted to vulnerable groups, as elaborated in the multi-year project plan.

Is the most important part of an appraisal determining how much a PVO needs?

Equally important are the **capacities** your PVO brings to administer and support the monetization. Unless a PVO can ensure, in advance, that it can handle the logistics and management of food imports and food sales, it should reconsider monetization as a means of support. The in-country assessment should answer the following:

Box 5-b. OICI monetizes in Togo for training and microenterprise

Monetization has allowed PVOs to experiment with applying food aid to projects that have no direct involvement with food. Some PVOs that specialize in income-generating projects, for instance, have made the case that general economic development promotes purchasing power to buy food. In this manner monetization promotes food security.

OICI, a US PVO with many programs in Africa (but has no conventional food-distribution programs) has been monetizing wheat to the government of Togo since 1989. In 1989, 1991, and 1992 it conducted three separate sales to the government parastatal, SGMT, which mills flour and sells it to the population. Each sale was approximately 2,000 MT of wheat (hard, winter wheat with 13% protein content).

OICI negotiated directly with SGMT and has received approximately 41,000 CFA (the local currency) per metric ton. This is about $134 US per metric ton. Therefore, since 1989, OICI has generated approximately $800,000 through a very simple sale. This local currency has supported OICI project activities in on-site professional training and small-scale industry.

- Do you currently have staff with expertise in monetizations, sales, negotiations, contracts? Often PVOs conduct tenders for bids for services (such as truck transport of food) that are similar to conducting a food auction. What support staff can be spared?
- What is the the level of support (staffing, staff time, communications, travel) available from your PVO headquarters? Monetizations often require a higher level of feedback and timely communication between home and field offices.
- What local storage capacity do you have to hold food for a few weeks or a few months? Can you afford to rent local storage? Do your counterparts have storage facilities?
- Can your field office support a sales operation or would you need to obtain separate office space? What are the communications capacities with headquarters (e.g., telex, E-mail).

Box 5-c. Characteristics of food vs. cash as foreign assistance inputs to country programs

	Food	*Cash*
Availability:	Title II resources appropriated by Congress, stable or increasing; 416(b) variable	Dependent on PVO projects, technical assessments by AID, private donations
	Requires approval or active involvement by Mission, AID, USDA, Transshippers, taking many months to access	More variable and flexibility accessed; may be disbursed by Mission from local funds; may be given by AID or State in emergencies
	Often food surplus only available in good harvest years, when food aid not needed "pro-cyclical"	Often cash aid more restrained during world and donor recessions, also pro-cyclical
Monitoring:	Tracking, scheduling, verification, weighing, repackaging, submission of claims for losses all require organization attention and staff time	Requires equally expert attention to maintenance of books, to protection from inflation losses, but less time-consuming
	Numerous reports to AID: e.g. CSR, RSR	Fewer overall submissions to donor
Expenses:	High transport costs	Minimal cable/transport charges
	Significant storage and demurrage costs	Bank account can earn interest
	Handling, end-use checking, distribution, and administration costs substantial	Accounting, disbursement costs not as high
Expertise Required:	Experience, technical skills, trouble-shooting, and training impose an additional set of demands on PVO field staff and HQ, currently met by only a dozen PVOs	Far greater number of PVOs have institutional and staff experience managing cash inputs to support field projects
Symbolic value:	Donor governments, recipient governments, media, private supporters viscerally appreciate the high profile of food distribution	Greater tendency to want to apply cash assistance to budget and debt problems of governments, or to research
	Donations of foods from different sources often complement each other nutritionally or in taste	Cash resources from multiple donors do not carry this added incentive for commingling

derived from J Bryson, S Hansch 1993 Food and Cash for Work, Incentives and Relief in Famine Mitigation Activities Washington DC: USDA Famine Mitigation Activity

- Do you have sufficient in-country management control over your programs to ensure compliance with AID regulations, with proper codes of conduct, and to implement adequate monitoring and evaluation of program activities and effects?

Box 15-d. Characteristics of food vs. cash at the project site level

	Food	*Cash*
Project utility	More difficult, expensive to shift between sites	Easy to rotate between projects
	Longer lead-time problematic for fast-action projects	permits rapid response
Broad economic impacts:	May discourage domestic production; currency circulation multiplier effects more pronounced in the donor country	Likely to encourage domestic production, down-stream currency-use multiplier effects accrue within recipient country
	More likely to cause shift in tastes to imported goods- a drain on balance of exchange	More neutral with respect to food tastes
	Likely to cause dependency on donated food imports	Equally, if not more likely, to foster dependency on donated cash aid
Symbolic value to recipients:	Often food is perceived as a community good, and fosters cooperative or volunteer efforts within a village; more likely to be spread equitably	Cash more likely to be seen in the same light as wage payments, less likely to knit together community spirit
	More self-targeting to children and the poor	Less self-targeting to vulnerable groups
Income value to recipients:	Depends on the local retail price of comparable foods, can be high or low	Depends on exchange rate used in converting from donor to recipient country
	Income value decreased by long queue times, travel to PVO offices or work sites	Income value equally decreased by travel and waiting for cash transfers
	Physically moving food, and re-sale are costly	Cash may be more liable to taxation
	Value affected by packaging, perishability	Less urgency to protect the cash itself
	Value of food resilient to inflation or devaluation	Cash very vulnerable to inflation, devaluation
	Dampens local food prices, increases food access	Can cause local food price inflation which may render the transfer worthless to the recipients
Value to women:	Women prefer food transfers because they have a higher propensity to obtain foods for the family than other goods, and it spares them the time and effort of going to the market	More fungible, when markets are nearby, it can allow greater flexibility to obtain other needed goods. But cash is also more likely to be taken by the men in the household.
Impact on local economy:	PVO distribution may undercut role of local retailers, transporters, discourages inter-regional trade	Encourages trade in goods
	Most appropriate pre-harvest when food supply is low	Optimal season less certain

- What contacts and experience does your PVO have with local or international brokerage houses, management firms, transshippers, or consultants who specialize in commodity sales? What relationship could you draw on and at what cost?
- Is there a project already up and running, demonstrating a track record?
- Finally, consider, list and investigate alternate sources of funding. Proposals stand an improved chance of approval when the project has multiple means of support.

But how important is all this PVO capacity anyway? Isn't the food sold before it reaches the country?

When entering into the world of commodity management the PVO must accept responsibility for the proper protection of those commodities against risks. Your commodities may be rained on at port or they may suffer losses through theft and spoilage before they reach the purchaser. The purchaser may suffer bankruptcy before he can pay.

One PVO has held large quantities of donated cheese in stock for several years. It hasn't sold it because the market has not been good for sales, so the cheese has been kept in storage with other commodities.

Box 5-e. Catholic Relief Services monetizes in the Philippines

Depending on the need, monetization funds can be transferred to counterparts in the form of money, equipment, services or food. In December 1990 CRS endorsed monetization as a source of funding for local activities. Since then, CRS has supported monetization projects worldwide, including Bolivia, Burkina Faso, Ghana, Indonesia, Sierra Leone, Togo, Morocco, Gambia and Kenya. The CRS Philippines monetization was unique because the commodity was sold to the commercial traders rather than to host government food boards or agencies.

CRS Philippines monetized 14,5000 metric tons of wheat valued at $2.1 million in July 1992. The monetization proposal was first submitted to CRS and USAID in August 1990. Two consultants, four revisions, and twenty one months later, CRS Philippines received an AID cable authorizing the sale of wheat.

CRS proposed the monetization as part of a comprehensive "Food Transition Strategy" through which CRS would phase down its import of food commodities, and shift its projects to the use of local food commodities and self-sustaining small enterprise development. PL 480 commodities are converted to local foods through monetization and the internal purchase of local foods. Local commodities, such as rice, have better taste acceptability and ease of preparation. Mung beans, also, are eaten everywhere by everyone.

Monetization for the purchase of local foods also helped ensure regularity of supply, given that there are over 7,000 MCH distribution centers served. Reducing supply disruptions was found to ensure that more food was consumed in the homes. Finally, local food purchases helped to direct money into rural communities. In a number of areas, purchases are made from cooperatives associated with the same dioceses and/or families within the nutrition program.

CRS held discussions and sent preliminary tender letters to potential buyers of beans, butter oil, peas, salad oil, and wheat. The sale of wheat was found to hold the greatest opportunity in terms of sales volume. Following USDA's approval on the sale of wheat, CRS contacted the two large milling associations operating within the Philippines (PAFMIL and CHAMP) which utilize 12 mills and imported 1.4 million MTs of wheat in 1990.

based on contributions to FAM by Catholic Relief Services

More important than storage capacity is managerial capacity: the assurance that specific staff will properly monitor food, be available to take actions to protect the value of the asset (including transport, reconstitution, hiring security guards, etc.), and submit the appropriate reports to the donors, and the public to ensure accountability.

How large a role will the PVO headquarters be expected or need to play?

PVO experience on this question varies considerably. Headquarters provide information on commodity availability, recent AID policies and regulations, and on the status of pending proposals. Often headquarters staff are directly involved in negotiating with AID/Washington or USDA/Washington over access to different commodities. Some monetizations are conceived of and planned primarily from headquarters, based on field visit appraisals by headquarters staff. Other monetizations have depended upon frequent communications from the United States. Thoughout ACDI's ongoing monetization in Uganda, the headquarters maintained close, weekly support of the business needs of the sales activity.

In a review of its monetization experiences (see box 5-e), Catholic Relief Services (CRS) recently concluded:

"CRS faces a steep learning curve. CRS should develop in-house expertise that is capable of providing monetization support, coordination and review. As experienced during the Philippines monetization, information to and from Baltimore was not centralized - no single office appeared to have a clear and complete picture of what was going on. At a minimum, CRS should develop an in-house monetization team capable of offering country programs expertise in monetization, commodity nomenclature, industry practices and shipping concerns. During monetization, CRS must step out from its developmental role and seek to maximize revenue not relationships. Assuredly, our

Box 5-f. Some food-related funding sources

Institutional Support Grants, known as "ISG"s are made available annually, though in 1993 AID began approving them for 3-5 year periods. They are to strengthen the PVO's worldwide system of programming and managing food aid. This covers staff salaries at PVO headquarters, improving internal management controls, developing software systems to facilitate logistics, and providing funds to appraise and plan a monetization.

These grants are administered out of AID's Food for Peace Office. Any registered cooperating sponsor can apply for an ISG, but the pot of funds is limited. In recent years, there have been specific types of ISGs. The "Planning Assistance" grants, to help PVOs that have never conducted food aid programs were designed to explore and initiate the process. "Enhancement" and "Strengthening" grants were also recent types of ISGs. Though often referred to, none of these three grants are currently available.

"Farm Bill" grants, also referred to as "202(e) funds," are part of the PL 480 legislation and are intended to support food aid programs at the field level. This includes the costs of training in-country staff, paying for the implementation in-country of logistics and accounting systems, and covering other complementary costs that are essential for the delivery of food aid.

buyers will do the same. This point also argues for in-house expertise. Wheat buyers do not send plant managers to negotiate sales contracts. They send in their best negotiators and staff - those who possess as complete a picture as possible and those capable of getting the best deal. CRS must do likewise."

Other PVOs have found that monetizations can be managed successfully with little trouble-shooting support from headquarters. Headquarters support is required more where the need exists for strenghening business skills and techniques of the in-country staff.

What are the basic PVO requirements in requesting Title II food aid for a monetization?

The formal requirements are the same as for accessing Title II food for other types of distribution. First the PVO or cooperative must be registered with AID. The PVO will need to show that it receives voluntary contributions from the public and maintains 501(c)(3) status with the Internal Revenue Service. It should request from AID its Form 1550-2 and current annual budget chart.

Second, the PVO or cooperative needs to obtain "cooperating sponsor" status through an agreement with the office of Food for Peace. This agreement allows AID to transfer commodities to you, and you agree to accept and manage food aid in accordance with PL 480, AID regulations, and related procedures. (Refer to AID Regulation 3, 22 CFR Part 203.) Organizations applying to become registered with AID may begin by contacting the Registration Office within the Office of Private and Voluntary Cooperation at AID, Washington DC 20523-0808.

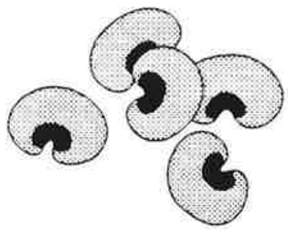
➢ ***FURTHER READING:***

1. *AID Handbook 9 Washington DC;*
2. *AID Regulation 10 (22 CFR Part 210) Available from USDA Foreign Agricultural Service*
3. *J Bryson 1991 Project Food Aid. User's Guide for Design Washington DC: AID;*
4. *World Bank 1988 Labor-Based Construction Programs: A Practical Guide Washington, D.C.*
5. *AID 1982 Recurrent Costs Problems in Less Developed Countries Washington DC:*
6. *Food Aid Management 1993 Food Aid Cost Worksheet Washington DC: FAM*
7. *A Jennings, D Shaw 1987 "Food Aid and the Recurrent Cost Problem in Developing Countries" Food Policy 12(3) August*
8. *WFP 1991 Project Colombia 2368 (Exp): Rehabilitation of small farmers within an integrated rural development programme Colombia: WFP;*
9. *Nicaragua Urban Community Development Program: Project Proposal (1990), New York: CARE;*

-- on use of food as income transfer in promoting employment in public works projects see

10. *H Ezekiel 1987 "Rural Public Works, Food Aid and Development: an Analytical Framework" IFPRI.*

CHAPTER 6.
THE APPRAISAL: MARKET ANALYSIS




What aspects of markets need to be studied?

The PVO needs to determine the potential to sell the donated foods in any of the local markets. This involves becoming familiar with the country's laws concerning imports, market prices and price structure. One should also know about commodity merchants, and the country's capacity to pay for imports. More importantly, it requires a study of what foods are sold in the country, at what prices, and why. This is the stage when potential buyers and their costs structures will also be identified. It is quite likely that in-country PVO staff will have some current knowledge of local food supplies and retail prices from which to start.

Isn't this kind of analysis theoretical and best left up to economists?

No. The market analysis is primarily performed by meeting and talking with people, asking for basic data on prices, and describing how different foods become available for sale. In some ways it resembles a drama where much of the complexity lies in understanding all the various players. In this stage of the appraisal you want to identify the major importers, wholesalers, retailers (farmers cooperatives, fair price shops, local retail cooperatives), millers, transporters, and even groups of consumers. Then you want to understand their interests and needs.

Why not wait and visit the market later, when you are about to conduct the sale?

The essence of the appraisal is to determine if US commodities can be reliably sold in the country for a reasonable price. The market analysis is the single most important part of the preparation for a monetization. The basis of decisions about commodity selection, timing, sales procedures, pricing, estimates of requirements, and food quality and grade issues are all made from the information obtained during this stage of analysis. Quite often this is when the PVO decides whether to go forward with a sale.

How long will the market analysis take?

A market survey usually requires several weeks of staff time and includes multiple interviews with

Chapter 6 Action Checklist

Have you:

☑ ***Visited local Chamber of Commerce, Ministry of Agriculture and reviewed import price data?***

☑ ***Conducted price surveys in several different retail and wholesale markets?***

☑ ***Developed a sense of where foods are brought from, by whom, and what the expenses of transport are?***

☑ ***Calculated the typical yearly variation in cereal, oil, and bean prices?***

Box 6-a. Terms about goods and prices:

Farm-gate

The stage in the chain of food distribution when the food is sold by producers to traders, cooperatives or wholesalers.

Wholesale

The stage in food distribution where food is collected into large amounts before being sold to retailers.

Retail

The final stage in the chain of distribution from manufacturer to consumer; the outlet for commodities purchased by consumers.

Border

The border stage of distribution refers to imports or exports. The "border price" is not necessarily the same as either the wholesale or retail price, but is determined more by international (world market) prices.

Spot Market

A market in which a commodity or currency is traded for immediate delivery, as distinguished from a futures or a forward market in which contracts for delivery at some future date are traded. Prices here are 'spot prices.'

Consignment

An unsold shipment of grain placed with a commission man who will offer it for sale.

Contract

The bilateral obligations of buyer and seller in a transaction. Or, the unit of the commodity being traded.

Tradable

Any good that is imported or is likely to be imported.

NTBs

Nontariff barriers that are practiced by all countries, including restrictions by individual countries on quantities of imports, and includes regulations on packaging, labeling, quality standards, etc., that are used to protect competing domestic producers.

---------Terms about market structures:

Imperfect market

One in which the following conditions, necessary for a perfect market, are not present:

(1) a homogenous product; (2) a large number of buyers and sellers; (3) there is freedom of entry and exit for buyers and sellers; (4) all buyers and sellers have perfect information and foresight with respect to the current and future array of prices; (5) in relation to the aggregate volume of transactions the sales or purchases of each market agent are insignificant; (6) there is no collusion among buyers and sellers; (7) consumers maximize total utility and sellers maximize total profits; (8) when consumer needs are not fulfilled at market it is to some degree imperfect. Markets tend to vary considerably with respect to the satisfaction of these conditions. The stock exchange and the wheat market in the US are often quoted examples of markets which come near to perfection.

Competitive market

A market in which a large number of small buyers and sellers trade independently, and ensuring that no one trader can significantly influence price.

Contestable market

A market is contestable to the degree that potential competitors can enter and/or exit the market rapidly. In other words, the threat of new players affects the pricing behavior of the current buyers/sellers. A market that is characterized by an oligopoly or monopoly may nevertheless have reasonable pricing if it is contestable. A market tends to be contestable when startup costs, or economies of scale, are not high.

Black market

System of buyers and sellers that skirts national regulations. Although parallel markets may be sanctioned, black markets are illegal by definition. They inevitably coexist with public monopoly, providing an alternative market, with higher prices, for both suppliers and consumers. The price differential includes a risk premium for covering the illegality and potential forfeiture.

wholesalers, retailers, importers, bankers, and chamber of commerce representatives. Collecting the core data on imports and major staples can be accomplished in a few days. Getting out about the country to determine the best markets for your foods may take longer. Price data collection should become an ongoing activity if you are considering or conducting monetizations in a country.

What makes price data collection so involved?

It is not that difficult. Getting the most efficient returns on your sale involves discriminating between commodities based on which one brings the best return through the sales price. Therefore, understanding prices is critical. Prices are not static, but vary from day to day, month to month, and year to year. The change in the world price of a single commodity in just one year can make the difference between a country having a large balance of payments surplus or large deficit.

There are many kinds of prices (see box 6-a). There is the price the importer pays and the price the wholesaler pays to the importer, which will be more. There is the price the semi-wholesaler pays the wholesaler, which is more still. There is the price the retailer pays the semi-wholesaler which is even higher. Then there is the price the consumer pays to the retailer which is the highest of all. There are official prices, semiofficial prices (referred to sometimes as "parallel" prices), and there are black-market prices. There are controlled, state-defined prices, and there are "open-market" prices.

Box 6-b. What determines or influences commodity prices in a country?

The following excerpt is from a review of millet, sorghum, maize and rice markets in Mali. The Government of Mali, which had been monetizing food aid and attempting to control prices learned that its intervention was often inefficient. The author summarizes many of the variables that interact to determine prices.

"The price of cereals in Mali is influenced by many factors, including the:

1) Level of production in the current and previous crop years;

2) Level of stocks on-farm and in urban warehouses; quantity and price of imported grains;

3) Quantity of food aid at present in the country, as well as the type of food aid distribution (free or priced at market price or price d at administratively-set price);

4) Costs of transport, licensing, margins, wages, and interest rates in the formal and informal sectors;

5) Expectations about the future direction of policies that might change prices (variable tariffs, import bans, changes in use of official producer and consumer prices, administrative barriers to free trade domestically, etc.);

6) Setting of certain inputs and output prices by the Government such as the price paid to rice producers in the (regional parastatals);

7. Level of effective demand domestically and in neighboring countries partially a function of wage and price policies. The level of prices in neighboring countries also undoubtedly has some influence on prices in Mali."

from W Scott 1988 Mali Cereals Marketing Restructuring Program Annual Program Evaluation Washington DC: Chemonics pg. 2-3

Which price data is the most important?

The most important prices are those paid by wholesalers and those paid to wholesalers by retailers. Even the most experienced market analysts hire local people who know the markets and who will receive more accurate responses to questions addressed to sellers about their prices, and to wholesalers about their prices and about what they have been paying over the past year.

Market survey:	Retail price quote (a)	Quote (b)	Wholesale (a)	Quote (b)
✓ Whole wheat	________	________	________	________
✓ Wheat flour	________	________	________	________
✓ Corn (white)	________	________	________	________
✓ Corn (yellow)	________	________	________	________
✓ Corn meal	________	________	________	________
✓ Sorghum	________	________	________	________
✓ Rice (20% broken)	________	________	________	________
✓ Rice (35% broken)	________	________	________	________
✓ Beans	________	________	________	________
✓ Soy oil	________	________	________	________
✓ Palm oil	________	________	________	________
✓ Cottonseed oil	________	________	________	________
✓ Peanut oil	________	________	________	________
✓ Non fat dried milk	________	________	________	________
✓ Full cream dry milk	________	________	________	________

Multiply the price per kilogram (by 1000), price per lb. (by 2,100) or other local units to convert to likely sales price per MT. This gives a basis of comparison in calculating how sales prices compare to c.i.f. prices, and gives a starting point to investigate what determines these prices. As discussed in Box 6-b, price differences may result from production cycles, rainfall patterns, or import patterns.

The final retail price quoted probably includes the following costs and markups:

- producer costs (may vary from 10% to 90% of the final retail price)
- producer profit (may vary from 1% to 20% of retail price)
- transport costs (in poor infrastructure countries, this will be high; depends on location)
- storage costs (storage costs also represent the risk the storer took in holding stocks until a season of low supply)
- taxes or subsidies (food imports, for instance, may be taxed or may sell at a premium because of a quota).

Box 6-c. A market analysis of foods in Burkina Faso: first part.

Save the Children Federation (SC) undertook an appraisal of monetization in Burkina Faso in 1992. SC was already implementing an integrated community development program in Burkina Faso with sub-project interventions in primary health care, rural water supply, child survival, agriculture, credit and savings, and literacy training that required a projected $1,500,000 of support over three years.

In late 1991, the government of Burkina Faso (GOBF) ended a long-standing program of price controls and a system of state monopolies in food-commodity trading. With the exception of wholesale price controls on rice and a monopoly on wheat and wheat flour trading held by a parastatal flour mill, all other trading in food commodities was opened to free competition through the private sector. Domestic production of most food crops in Burkina Faso is insufficient to meet national consumption. At the same time, the local diet includes several commodities available through PL 480 Title II, including rice, wheat, wheat flour, corn, corn meal, milk powder, and vegetable oil. Any of these commodities seemed suitable for monetization, but more intense investigation turned up some interesting factors. It soon became apparent that U.S. rice could not compete in price with cheap imports from Asia; and the inferior quality of U.S. PL 480 Title II wheat compared to wheat from other countries and the limited demand for wheat and wheat flour ruled out those commodities. Some market potential did, however, appear to exist for sorghum, corn, corn meal, vegetable oil, and non-fat dry milk (NFDM).

SC liked the idea of monetizing sorghum because it is the staple grain of the Burkina Bae diet and domestic production was consistently in deficit. Sorghum was also attractive because prevailing wholesale and retail prices indicated that PL 480 sorghum might bring sales prices equal to or exceeding its full CIF value. It was learned, moreover, that both private traders and officials at the GOBF parastatal Office Nationale des Cereals (OFNACER) (National Office of Cereal Grains) were familiar with PL 480 Title II sorghum from its distribution in emergency relief programs. Without exception, everyone in the Burkina Faso grain trade described U.S. sorghum as inferior in quality to domestic sorghum and incapable of commanding a strong sales price. Even when sorghum was in short supply due to poor local harvests, traders considered consumer opinion of U.S. sorghum to be so negative that they would not offer a price high enough to meet the FAS value of the sorghum. In line with these market conditions, SC dropped sorghum from consideration as a monetization commodity.

Corn and cornmeal were known to be other staples in the Burkina Bae diet. Once again, local traders were familiar with U.S. corn and cornmeal from relief programs and expressed little or no interest in PL 480 corn products. Traders explained that maize consumed in Burkina Faso is a "white" variety, produced locally or imported from Ghana with some additional imports from Europe. They described U.S. yellow corn, as "red", and insisted it would find a very limited market and low prices, as consumers demonstrated strong preference for "white" corn and "white" corn meal. Traders readily admitted that, in terms of taste, U.S. and local corn were very similar, and that, nutritionally, U.S. corn was superior. Nevertheless, they expressed little interest in purchasing U.S. corn, stressing that consumer preference was too strongly in favor of local "white" maize, because traditional dishes prepared using "white" corn "presente bien" (looked good). SC concluded, therefore, that Title II corn and corn meal offered no prospects for success as monetization commodities. In examining the market potential for PL 480 vegetable oil, it was again apparent that local tastes and consumer preference were negative on PL 480 vegetable oil. *(continued)*

submitted to FAM by Marine Overseas Services

Box 6-d. Burkina Faso appraisal for a PVO monetization (continued)

Cottonseed oil, both domestic and imported from Cote d'Ivoire, was strongly preferred over other types of cooking oil, of which several varieties were available in shops. Although much food preparation used other oils, e.g. rapeseed, sunflower, shea nut, groundnut, and palm, traders agreed that local tastes dictated that certain traditional dishes must be prepared using cottonseed oil. PL 480 soybean oil had little chance, therefore, of selling at prices commanded by cottonseed oil. Traders suggested, however, that cottonseed oil was in such short supply and was sufficiently expensive that PL 480 vegetable oil might expect to find a substantial market and command prices representing its CIF value. Although not the first choice with most consumers, PL 480 vegetable oil did generate considerable interest with commodity traders and emerged as a strong candidate for monetization.

Non-fat dry milk (NFDM) was another possibility for monetization. The production of dairy products in Burkina Faso was found to be very limited. Furthermore, the few small dairy operations in Burkina were using reconstituted powdered milk to extend fresh milk in packaging liquid milk and in the production of yogurt. As much as 95% of the milk powder available in Burkina Faso was marketed as "full cream", i.e. having a fat content of 26%. Low-fat milk powder was a rare commodity on the local market because the countries supplying the milk powder, France and Holland, produced full-cream milk powder and sold it for approximately the same price as low-fat milk powder, normally cheaper, due to EC price subsidies. The study also found that approximately 80% of the Burkina Faso milk-powder market was controlled by one importer who was the agent for the European milk producers: Bridel, Nido, and Encore. The study concluded that this de facto monopoly in milk trading, combined with high supplier prices, resulted in such a high price for milk powder that PL 480 NFDM could effectively compete. It was calculated that NFDM could sell in Burkina Faso at prices below European full-cream milk yet higher than PL 480 CIF value. Although local milk packagers, yogurt producers, and home consumers considered full-cream milk powder to be superior to Title II NFDM, it was apparent that this superiority applied only if both products sold at roughly equivalent prices. At a lower sales price, there was strong demand for low or non-fat milk powder for both industrial and domestic use, but this was also tempered somewhat by the fact PL 480 NFDM was perceived to be "too fine" or "too powdery" for ideal yogurt, which analysis indicated would constrain NFDM prices to some extent.

Using a mock tender to gather information-

The Burkina Faso Chamber of Commerce, while essentially a governmental service useful in initiating contacts with large companies and government parastatals, was of little help in making contact with private commodity traders. Contacts with buyers and collection of market intelligence was carried out through a private group, the Association Professionnelle des Petites et Moyennes Enterprise (AP-PME) (The Professional Association of Small and Medium Businesses).

An innovative method used to study market conditions and to analyze commodity sales potential was to distribute through AP-PME a questionnaire and mock tender -- soliciting non-binding bids from local traders on various PL 480 commodities. Although, as one would expect, the mock bids demonstrated some degree of collusion in fixing offers at low prices, the exercise worked well in corroborating information gathered by less formal means and provided indicators about the traders, potential buyers, and market conditions, all valuable and useful data in planning for the monetization project.

The results of the mock tender showed that bids for corn meal and sorghum were below PL 480 FAS values; bids for whole corn were slightly above FAS value; and NFDM and vegetable oil brought mock bids $185/MT and $100/MT, respectively, above the CIF values of those commodities. These were prices in line with assumptions and deductions made from interviews with the traders, but the mock tender served to corroborate the interviews and more scientifically get a handle on local commodity-market conditions.

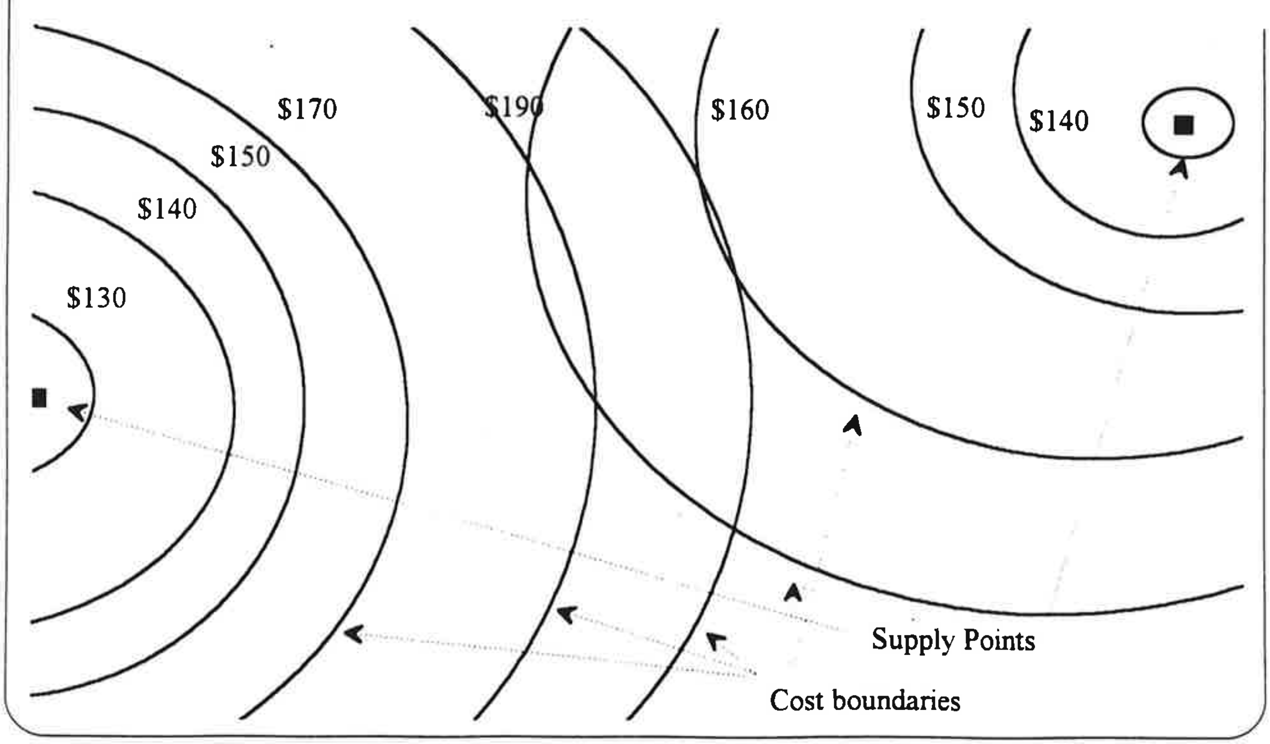
To understand the importance of the retail price, you must understand the position of the wholesalers. The difference between the local retail price and the wholesale price is how the wholesaler makes his living. He cannot offer to pay the PVO a price near to the retail price. AID's Monetization Field Manual recommends analyzing the price structure of the food chain, including the costs and profit margins as seen from the each stage: the farm, the transporter, the wholesaler, the importer and the retailer. It specifically recommends understanding the level of costs related to "internal transport and handling costs from main producing area to main consuming area," as schematized in box 6-e.

What are governments' concerns and costs concerning the interventions in food markets?

A recent study published by the World Bank found most of the countries studied were concerned with food self-sufficiency and urban food prices. This concern had a major effect on government policies on food prices and on the competitive status of imported food.

> *"All governments intervened to regulate or control private activities in agricultural pricing and distribution. Sometimes intervention was limited to imposition of price ceilings or floors, but usually other controls were also used. In many instances, legislation or regulations were put into effect that established a two-tier pricing system. In some instances, the two tiers were the controlled price and the free market price; in other instances, they were different prices at different points for the same commodity when there was no cost differential; in still other instances, there was a common price when costs indeed differed."* (see A Krueger, box 6-b)

Box 6-e. Prices across a countryside depend on the distance to nearest supply points.



Mercy Corps, a US PVO, found, when designing a sale of butter oil in Kazakistan (in the former Soviet Union), that its price was one-third lower than on the world market. This variance occured because of government interventions in the food markets to keep prices low and an artificially high rate of exchange. On the one hand the value of the Section 416 commodity was unusually low in Kazakistan. On the other hand, the same government intervention that kept the price of butter oil low also kept the price of other commodities low. IMC was able to demonstrate that its monetization program could use the currency proceeds to locally buy a other foods, fuel and services.

Box 6-f. Cereal traders in parallel markets: an appraisal in Senegal.

In virtually every country throughout sub-Saharan Africa, private grain traders continue to operate alongside public sector marketing organizations. ....Frequently, their participation in the grain trade is explicitly prohibited by law, forcing them to operate in the so-called parallel or illegal marketing channel. ...contrary to the conventional wisdom, intermediaries in parallel cereals markets frequently are able to provide a wider range of marketing services at lower cost than the state and parastatal marketing organizations which are intended to supplant them."

The official market in Senegal does include a number of public organizations, but many cereals marketing activities are handled by an extensive network of private merchants who are licensed to operate under government regulations and policies. Thus, both official and parallel markets rely largely on private sector participation. The essential difference is not whether trading is performed by public organizations or private merchants, but whether or not public and private trading is carried out in compliance with the rules of the game established by the state."

Data on the cost of credit in informal capital markets were difficult to obtain because of strict Muslim prohibitions on the charging of interest. When asked about interest payments made to local moneylenders, traders would generally claim that no such payments are made, since interest is prohibited by the Koran. Data on sales volumes handled by wholesalers were sometimes pieced together from information provided by assembly traders working upstream in the marketing channel, rather than directly from the wholesalers themselves."

Gross Costs and Revenues

Purchase price of rice paddy at farm	75
Sales of Milled rice	87
Sales of Husks and bran	12.50
Total revenues	100
(gross margin)	(25)

Expenses

Bagging fee	1.25
Bags	1.25
Transport to mill	1.25
Milling fee	9.4
Winnowing fee	.78
Rice bags	.63
Byproduct bags	.63
Transport of rice	1.25
Transport of byproduct	.3
Opportunity cost of capital (15% per year)	.58
Total costs	17.61

[all values are expressed are of French CFA per kilogram food]

The estimated costs and returns to labor and management of a parallel channel rice trader, 1985:

For this rice trader the net margin was 7.39 calculated as 100 - (75 + 17.61).

By ignoring official prices and marketing margins, traders are able to transport grain to deficit regions and to store grain into the hungry season, with the result that consumers have larger supplies and face lower prices than might otherwise have prevailed."

excerpted from M Morris, M Newman 1989 "Official and Parallel Cereals Markets in Senegal: Empirical Evidence" World Development 17(12): 1895-1906

In 1981 Robert Bates wrote, "*Besides sometimes encouraging the importation of foreign crops when domestic prices lie above world market prices, governments sometimes ban the export of food crops to prevent local prices from rising to a higher international price. In December 1974, for example, the government of the Sudan imposed an export duty of 20% on meat and meat products, thereby making it unprofitable for domestic producers to sell on the growing Mideast market and lowering the price to domestic consumers. In Kenya, both the Kenya Meat Commission and the Kenya Cooperative Creameries are compelled by government regulations to offer their products on the internal market at prices well below the world price.*" (Markets and States in Tropical Africa pg 37)

What are the ways governments control prices and markets?

Governments are primarily interested in keeping consumer prices down. In addition, they may want to control trade, particularly to reap the benefits of taxes and levies (see boxes 6-c and 6-d). Governments affect markets, prices, and imports through regulations (such as restrictions or quotas on what can be imported), licensing, price-fixing (or minimum prices), and direct involvement as a buyer and seller (through parastatals).

Governments have a difficult time controlling food supply or food prices beyond a certain point (an interesting exception is depicted in box 6-i). Large-scale commercial foods, particularly those that are transported over distances, imported,or are heavily processed, are much easier for the government to control. These include maize, wheat flour, pasteurized milk, and high quality meat. Thus price controls often exist for these commodities but not for millet or sorghum which are rarely processed in large plants. For the same reason, price controls are more effective for refined sugar and vegetable oils than for less refined products from small-scale plants. Governments have great difficulty in taxing or being a major buyer of local fresh vegetables and fruits, for example, or of foods produced in inland border regions where they can be readily sold to other countries, regardless of laws. Virtually no country attempts to control the price of fruit and vegetables because of the many marketing channels and outlets used, as well as the seasonal and short-duration aspects of their perishability and range in quality.

Do PVOs need to be concerned with black markets?

Parallel markets operate for the sale goods that are in some way controlled by the government. Since governments intervene in many food markets, you do need to be aware of the effect that unsanctioned or unlicensed trade has on your capacity to do business. You are operating in the country under an agreement with the government, and you will thus not want to conduct trade within the parallel market. However, parallel markets are important to know about because:

- Parallel market prices affect the amount of food that will be sold at official prices;
- Parallel merchants may be buying from you indirectly, in secondary markets; and
- The trends in parallel markets tend to indicate underlying supply and demand conditions more than do regulated markets.

Include parallel market traders in your examination of the current cost structure of food marketers. For an example from Senegal see box 6-f. Many of the players including visiting wholesalers, processors, local assemblers, farm processors and the like will not fall neatly into any one category (parallel, informal, etc.). Yet collectively they make up the marketing system and it is essential that you understand the roles they play.

What about consumption and who ends up eating the food?

A good market analysis does not stop at identifying the sources of foods, and the merchants moving and selling foods. It also examines trends in who consumes the foods. This step is important in identifying (a) how reliably today's "snapshot" of food markets predicts food demand in a year when your monetization is likely to occur, and (b) whether there is potential to sell donated foods that would be new to the market (perhaps dried skim milk, butter oil, certain beans, or soy-based products). Consumption analysis includes identifying changes in the population, through migration (e.g. refugees), mortality rates (e.g. AIDS), and birth rates. It also includes examination of where different foods are preferred (regional, urban/rural, ethnic patterns, proximity to ports and roads, proximity to production). It includes an understanding of how food purchases change with fluctuations in income, which can be calculated using elasticity of demand coefficients.

What do "elasticities of demand" have to do with whether a country needs food aid?

The term "elasticity" comes up in discussions about a population's levels of purchases and imports, and about impact evaluation. Elasticity refers to how much demand changes when price or

Box 6-g. The importance of analyzing trends and potential changes in prices.

This monetization project was planned in 1989, submitted in 1990, undertaken in 1991, and the proceeds were finally generated in April of 1992. During this period of waiting, delays, and re-design, the Kenya market continued to undergo changes. The original World Vision proposal was to sell wheat to the National Cereals and Produce Board (NCPB). But during the course of 1990 and 1991 the world price of wheat fell and the NCPB found itself lacking both credit and a resale market. This occured in part because of the progress of Kenya at liberalizing its internal markets. By the time the monetization was scheduled to occur, wheat was no longer a viable commodity to sell. World Vision needed to re-appraise the markets, update their information on prices for other commodities and identify if a suitable substitute existed.

AID and the US Agricultural Attaché put World Vision in touch with the Kenya Cooperative Creameries (KCC). The KCC, a parastatal, normally sells 25% of the national milk supply and almost all of the processed milk in the country. During this period of drought milk was being rationed. The Ministry of Commerce and the Central Bank of Kenya were relatively inclined to grant the KCC an import license for the milk because payment was not in foreign exchange but in Kenyan Shillings.

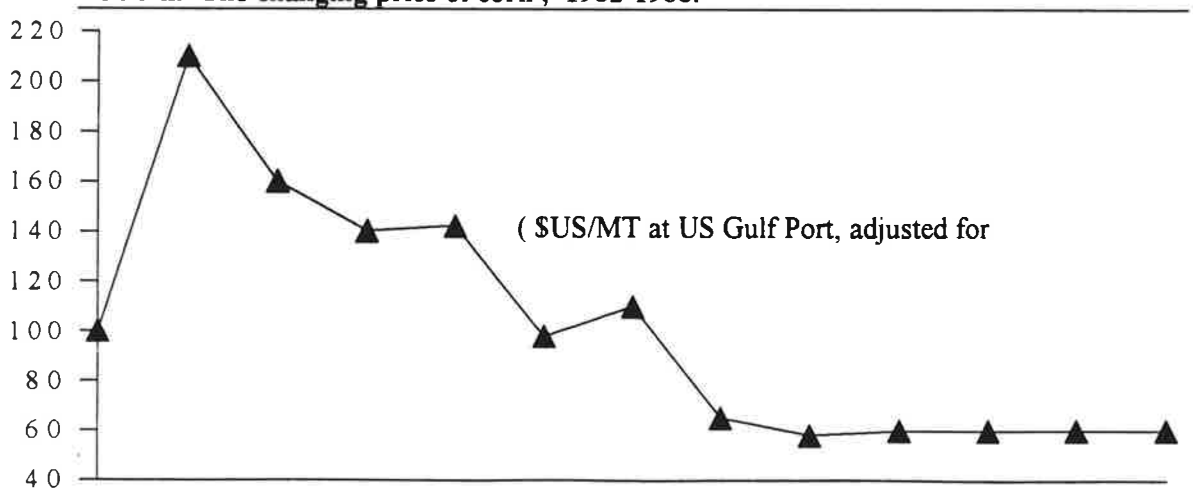
World Vision is supporting its irrigation project in Kenya through a monetization of 816 MTs of extra grade Non-fat Dried Milk to the KCC for $1,160,000. The selection of non-fat dried milk was determined because of the interest of the KCC and because of the timely shortage of milk in-country. The proceeds support resettlement work for the pastoralists of the northern, drought-prone Turkana region.

Based on materials submitted to FAM by World Vision income change occurs, in percentage terms. There are a couple types of elasticities that are referred to frequently. One is the income elasticity of demand for a given food. Knowing this can help one understand long-term trends in consumer preference. It is particularly important in countries undergoing rapid income growth as in Thailand or Botswana As household incomes increase, the proportional demand for a food may change, particularly relative to other foods. For instance, with increased incomes households may seek to consume more and more meats, wheat, sugar, and foods that tend to be more highly valued, though costing more. If the income elasticity is "inelastic," as rice is in Korea, this means that as GNP grows and families' can afford to spend more money on food, they still consume about the same amount of rice. In contrast, a high income elasticity of demand for instance for beef means that Koreans will consume more and more meat as incomes rise.

The price elasticity of demand is different. It tells us how the purchases of a food change if the price of that food changes. Some basic staples that represent the largest single expenditure of poor households have shown very large price changes in just the last decade (see box 6-h). Such price swings dramatically impact on diet patterns. Much of this change in purchases occurs because consumers switch to other foods. Since prices in some countries change a great deal even from month to month, this type of data helps you predict the likelihood that there will be a market for certain foods in the surplus.

For instance, if the demand for wheat in a country is highly price-elastic, then the amount of wheat that consumers want to buy will decrease if wheat prices increase. Wholesalers who stock up on wheat for a certain amount of sales may be caught with unsold inventories during periods of rising prices. This contingency means that the PVO may be unable to find buyers of large lot sizes regardless of the price. This is particularly the case if cereal storage in that country is in short supply.

Box 6-h. The changing price of corn , 1982-1988.

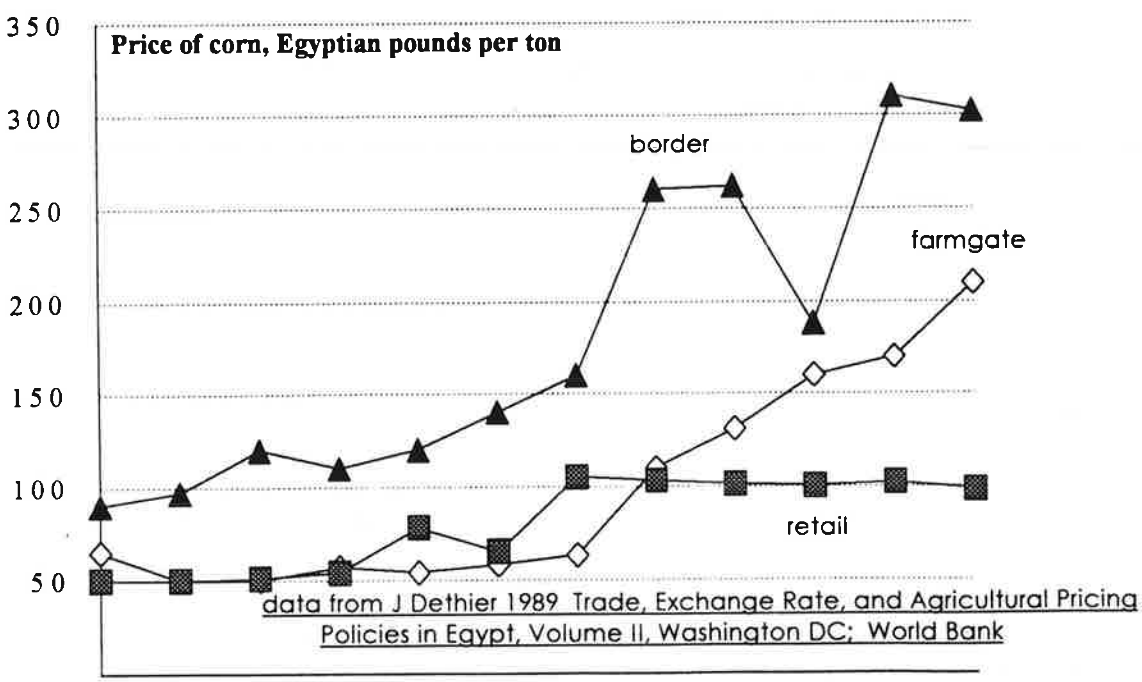


data from BOSTID 1988 Food Aid Projections for the Decade of the 1990s Washington DC: Board on Science and Technology for International Development.

➤ *FURTHER READING:*

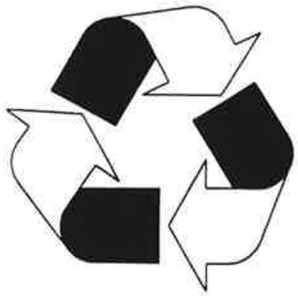
1. *P Streeten 1987 What Price Food? Ithaca NY: Cornell Univ. Press*
2. *C Peter Timmer 1986 Getting Prices Right, the Scope and Limits of Agricultural Price Policy Ithaca NY: Cornell Univ. Press*
3. *D Lindauer 1989 "Parallel, Fragmented, or Black? Defining Market Structure in Developing Economies World Development 17(12): 1871-1989*
4. *J Jenkins editor 1988 Beyond the Informal Sector: Including the Excluded in Developing Countries San Francisco: Institute for Contemporary Studies*
5. *R Bates 1981 Markets and States in Tropical Africa Berkeley: Univ. of CA Press*
6. *E Helpman, P Krugman 1991 Market Structure and Foreign Trade Cambridge, MA: MIT Press*
7. *J Strauss 1983 Socio-Economic Determinants of Food Consumption and Production in Rural Sierra Leone: Application of an Agricultural Household Model with Several Commodities, East Lansing, Michigan: Michigan State University, Paper #5;*
8. *C May 1992 Price Data in a Famine Early Warning System Arlington, VA: Famine Early Warning System Working Paper 2.6;*
9. *IRRI World Rice Statistics periodic Los Banos, Philippines: International Rice Research Institute;*
10. *B Berry 1967 The Geography of Market Centers and Retail Distribution Englewood Cliffs, NJ: Prentice Hall*
11. *N Islam 1992 Agricultural Trade Between Developing Countries: Patterns and Future Possibilities Washington DC: IFPRI.*

Box 6-i. Evolving differences between the retail, import, and farm prices for maize, due to government interventions to maintain a steady price for Egyptian consumers, 1974-19852



data from J Dethier 1989 Trade, Exchange Rate, and Agricultural Pricing Policies in Egypt, Volume II, Washington DC; World Bank

CHAPTER 7.
THE APPRAISAL: COUNTRY CAPACITIES, NEEDS, IMPACTS



What are reasons not to monetize in a particular country?

There are three key reasons for deciding against monetization: (1) your organization does not need the resources (examined in chapter 5); (2) the host country is not a good consumer market for the available commodities; and (3) the country has insufficient facilities to ensure proper management of the commodities and accountability.

Many of the strongest reasons not to monetize in any country will be discovered <u>after</u> the appraisal process. Because monetizations require approval or cooperation from the US Government, the host government, local industries, and bankers, and the PVO must compete with other competitive importers from around the world, it is difficult to determine in advance the obstacles and delays that could occur. A negative appraisal one year may be followed by a positive one the following year. Conversely, a positive appraisal may be out of date six months later. A monetization must accommodate fluctuations and evolution in the food supply, credit lines, exchange rates, government attitudes, and market structure of the recipient country.

What does the PVO need to do to determine whether a country can accommodate a monetization?

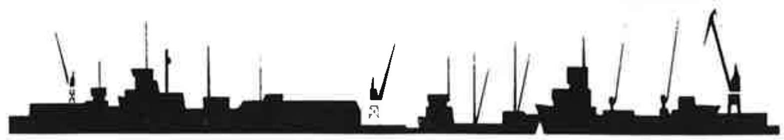
Certain elements of an appraisal are required by the US Farm Bill legislation (Section 401-403). These elements refer to possible negative economic impacts of monetization. The most important is the Bellmon analysis. The PVO should also consider examining local factor endowments and utilization, linkages between sectors of the economy, impact on the export of foods out of the recipient country, and potential gains from trade.

Chapter 7 Impact Assessment Checklist

- ☑ ***Does country have sufficient port and storage facilities and infrastructure to protect food?***
- ☑ ***Does this country suffer a shortage of aggregate food supply?***
- ☑ ***Will food substantially displace local production or imports from countries friendly to the US?***
- ☑ ***What other food aid has this country received?***
- ☑ ***Will food aid sales promote taste changes of consumers or other dependencies that the country cannot or should not afford?***
- ☑ ***Can traders in this country participate readily in auctions? How does market information flow?***

What is a "Bellmon Analysis"?

Before food aid can be given for a country program, an analysis must be conducted as required by an amendment passed by US Congress (see Title IV of the Farm Bill). Known as the Bellmon Amendment, it requires that there must be a determination that there will be no disincentive effect in the country before food aid is given. It also requires that for each purchase authorization or call forward, the adequacy of local storage and port handling facilities must be assessed as sufficient to prevent food aid losses.



What is a "disincentive effect?"

Any program is likely to have some impact on local supplies of goods, on incomes or on people's attitudes. Each of these changes influence the amount of food that will be traded or purchased, usually through changes in price. If food prices decrease, then farmers in that country will lose some incentive to continue to produce those goods and may cut back on overall food production (see box 7-a). Because monetization puts foods directly into market channels, disincentive analysis is more important than for other forms of food aid.

Many analysts believe that most poor countries should be able to produce enough food to feed their populations, but do not have the necessary experience or market structure to encourage this. US legislation does not demand that foreign aid do good in this regard (encourage farmers to expand production), but it does require that it do no harm. AID has noted that even if food aid sales are insignificant on a countrywide scale, they may still cause localized disincentive effects particularly when food sales are concentrated in a particular region. A little-appreciated aspect is that PVO sales to government agencies may cause disincentives indirectly by helping to support these sometimes

Box 7-a. Price changes affect local food output, but by how much?

To evaluate the net effect of food aid on domestic food production we need to consider its effect on the price of food and on government policies. The price effect depends on several factors: how much food aid will be provided in relation to total production; how much additional demand will be created through specific projects, programs, and monetary expansion; changes in relevant crop and input prices, and the effect of the resultant change in food prices on food production using the price elasticity of supply. It is preferable to estimate these effects through a multi -equation econometric model... On the other hand, in some circumstances a common sense approach does provide a feasible way to handle some of these problems and to allow for political and other factors difficult to include in models."

"The evidence that price is important to agricultural production, that farmers respond positively to price incentives is by now well known and convincing. Thus, any significant price declines caused by food aid must be taken seriously. We reviewed some of the data on the price and resultant production effects of food aid on food grain production in India. We found that food aid did cause a decline in relative food grain prices, but only during a fairly short part of the food aid period. The most comprehensive available study found the net loss in domestic production to be only 3% of the food aid provided."

excerpted from P Isenman, H Singer 1977 "Food Aid: Disincentive Effects and Their Policy Implications" in Economic Development and Cultural Change 25(January): 205-37 inefficient institutions. Even though a commodity is not currently being produced in a country a disincentive can still occur. Food aid may act as a disincentive on complementary crops. It may be that the imported good could be produced locally but farmers are discouraged from attempting to do so.

AID's Monetization Field Manual recommends:

"First, consider the impact the food aid commodity may have on close substitutes produced and marketed locally. For example, if wheat/wheat flour is being supplied, other common food grains such as corn, sorghum, rice, etc., which are seen by consumers as substitutes for wheat/wheat flour should be included in the analysis. The local incentives for all oilseeds must be examined if PL 480 soybean oil is to be supplied. Second, consider product differentiation. For example, certain types of US sorghum or corn may be less desirable than the local variety. Lastly, consider alternative uses the PL 480 commodity may have; e.g. for livestock feed or for industrial uses.

The analyst should calculate the percent of each PL 480 food aid commodity provided to total domestic consumption of the same or substitutable commodity for each of he past five years. If this proportion has been 2% or more over the past 4 years, have there been any unusual movements in inflation-adjusted price trends that would indicate US food aid has led to substantial declines in food prices? On the other hand, without US food aid, would domestic food prices tend to rise above normal levels suggested by the trend analysis?"

How can a PVO analyze "changes in taste?"

Even research institutes can not precisely quantify which factors cause taste changes over decades, let alone from a single field project. In most cases the PVO will not need to worry about this problem for monetization programs. In countries where a particular food aid product is unfamiliar to locals, it may be difficult to sell because there will not be sufficient demand for the product to support a good sales price. It has been recommended that PVOs consult the services of anthropologists and agricultural economists to examine whether donated foods are promoting taste changes that are undesirable or merely inevitable. Ultimately, a determination of the scale of negative impacts will be difficult for PVOs to make. After reviewing the literature on the subject E Clay and H Singer conclude:

Box 7-b. Food aid imports are predicted to increase, according to Iowa State model.

S Johnson recently circulated his estimate for the 1990s of food aid deficits in a number of countries. He ran models of the international trade of commodities:: "The individual commodity models are integrated into a larger system with other commodity components through price linkages that admit cross-country and cross-commodity interactions.

These models also predict decreasing agricultural production per capita for many of the poorest countries. For instance, "The situation that emerges, with few exceptions, for the Latin American wheat and feed grains importers when supply and use projects are analyzed in per capita terms, is one of the declining per capita consumption and declining production, but increasing per capita imports. ...The general trend emerging from the Asia analysis is for rapid growth in per capita consumption of both wheat and feed grains. In India, self-sufficiency policies have lead to growth in domestic wheat production and decreasing imports, and stable per capita wheat consumption over this period."

from SR Johnson 1991 "Global Agricultural Commodity Markets, Agricultural Policies, and Food Aid Programs" Ames, Iowa: Iowa State University

"Reviewing frequently contradictory interpretation of evidence from the same country experiences, some writers have concluded that the debate is intrinsically indeterminate. Judgments rest on the interpretation of unavoidably selective and often different evidence." (World Food Programme Occasional Paper #3)

Who needs to perform an analysis for the Bellmon Determination?

PVOs are required either to conduct an analysis of this disincentive effect or to cite the analysis which has already been performed. USAID Missions and the Agricultural Attaches of USDA's Foreign Agricultural Service have the foremost responsibility for conducting these analyses. If the country has received or is receiving other food assistance (such as Title I or Title III), USDA has often conducted a disincentive analysis. It is usually the PVO that must make sure the analysis occurs in a timely fashion.

This project involves a review of food production trends, an examination of the total scale of food aid coming into the country, and how domestic prices compare to international prices for the donated commodities. One NGO recommends estimating the caloric value of the imported food aid as a percentage of the total caloric value of foods consumed in the country in a year. If the monetization quantities exceed 5% of the total food supply (measured in calories), the potential for a disincentive effect is substantial. It also involves a listing and analysis of the structure, capacity and management of the storage facilities in the areas (port, regional) where the PVO would be bringing in the food.

A proper disincentive analysis would take into account the business environment of local farmers, their cost structure, their options, and also take into account what their options will be, given that country's comparative advantage in the world. True, food aid may displace the production of these farmers. But would cheap global imports have had this same effect eventually? In the short and medium term, to calculate the effect food aid has on local production, the analysis needs to find and use estimates of how much food production (acreage, inputs, yields) changes with changes in price (the "supply elasticity").

7-c. Disincentive effects of food aid in Ethiopia.

An example of a sophisticated disincentive analysis has been conducted by Simon Maxwell for the case of Ethiopia, where massive amounts of food aid have, during the 1980s, gradually displaced commercial imports. Maxwell finds that the country's overall dependence on food imports has not changed, only the status of those imports. Because food prices have not fallen below "normal" levels, Maxwell concludes that there has been no significant, negative effect on domestic production, or on workers' wages (through food for work). For Maxwell, the key question is whether food aid has pushed domestic food prices below the import parity price (considering wheat, maize and sorghum in the case of Ethiopia). Yet Maxwell concludes by calling for more research on both macro and micro-level disincentives.

see S Maxwell 1986 Food Aid to Ethiopia: Disincentive Effects and Commercial Displacement Brighton: IDS Discussion Paper #226

What are "Usual Marketing Requirements" and how are they related to the Bellmon Analysis?

They are both requirements that examine the broader import picture before food aid is allowed. The Usual Marketing Requirements (usually abbreviated as UMRs) are concerned whether US food aid or imports compete with the imports from nations that the US considers allies or friends. Before food aid will be permitted, the PVO or USDA must demonstrate that food aid will not significantly alter or disrupt world commodity prices or normal year trade to the recipient country. Normal year trade is typically estimated as the average of annual trade for the past 5 years. In theory, the PVO cannot bring food aid into a country unless that country has already imported or purchased the UMR (average) for that year.

To examine the profile of imports into a country, one can access MT figures for dozens of food commodities from UNCTAD's and FAO's food trade yearbooks. To compare a proposed food aid program to MTs of food aid currently being given, see the WFP reports cited below. Assessing a country's capacity should not only involve the required analyses. One should also attempt to determine the reliability of the interest of local importers and project beyond current levels of trade.

What if the country has agreements restricting trade?

Many governments do. Some governments have entered into commodity agreements with other nations that produce those same commodities in the hope of stabilizing prices by restricting trade. The intent of these agreements is not to maximize their sales, but to maximize their sales revenues. These agreements have not succeeded in reducing price variability. These commodity agreements have been for cocoa, coffee, sugar and rubber, which the PVO is unlikely to sell.

Box 7-d. Governments intervene in food markets through various intermediaries

Government control over food markets through quasi-governmental organizations take many forms. In Turkey the Turkish Tari is a cooperative sales agency for cotton, figs, raisins and olive oil. Created to serve its membership, it also makes support purchases when directed by do so by the government. Marketing Boards may be autonomous or may be part of a government ministry. Sometimes these boards or parastatals have purview over only one or over many commodities. For a PVO to sell in a country, it may have to deal with several such entities, as in the following example:

"In the Dominican Republic four autonomous government agencies formulated and implemented agricultural pricing policies. A Directorate General of Price Control (DGPC) mandated domestic food (and other consumer) prices at the retail level. The National Institute of Price Stabilization (INESPRE) then implemented these prices through its marketing, importing, storage, and transporting activities. INESPRE had exclusive rights to import basic food items and, along with another parastatal, Dominical Mills, controlled the importation of wheat and wheat products. INESPRE and Dominical Mills had to negotiate with DGPC for the prices at which they were to sell, and with the Monetary Board for foreign exchange allocations in order to import. The Monetary Board also determined the amount of credit INESPRE could have for the purchase of domestic crops."

from A Krueger 1992 The Political Economy of Agricultural Pricing Policy Volume 5: A Synthesis of the Political Economy in Developing Countries Washington DC: World Bank pg 29

Does monetization spur inflation?

No, not usually. The expenditure of the large amounts of proceeds or counterpart funds can be inflationary. But only to the degree that it offsets the deflationary effect of the generation of the proceeds. Analysts currently believe that the net effect is neither inflationary or deflationary. In the past there have been problems with large balances of proceeds sitting unspent in countries such as India and Costa Rica. These unspent funds have been more awkward politically than dangerous in economic terms.

Box 7-e. Sierra Leone: Case study of an appraisal for PVO sales (first part)

Sierra Leone is a country that is very food insecure. It has the highest infant mortality rate in the world, has little US aid, and has been wracked by food shortages and refugees from the war in Liberia. Operating from bases in border areas of Liberia, rebels made incursions into the rice-growing region of eastern Sierra Leone. The American Embassy (AMEMB) feared that the loss of control of considerable territory by the government of Sierra Leone (GOSL), and the abandonment of large areas by local farmers fleeing the violence were could result in shortages of rice, the staple of the Sierra Leonian diet. In addition to the aforementioned concern, the AMEMB wished to demonstrate good will toward the government, which was negotiating a structural adjustment agreement with the International Monetary Fund (IMF). Finding mechanisms of providing foreign aid was proving difficult as PL 480 assistance under both Titles I and III had been effectively ruled out. AMEMB and USAID/Freetown approached Catholic Relief Services (CRS) and CARE in July, 1991 concerning the possibility of mounting a Title II food monetization project, leading to this appraisal financed by CARE.

The situation in Sierra Leone was economically and socially chaotic and was not conducive to monetization programming. There was a dearth of records and those there were available were confusing, not usable due to the manner of record-keeping, or untrustworthy.

Sierra Leone, with a population of only 4.2 million, possesses fertile farmland and an excellent climate, has productive fishing grounds, and exports diamonds, gold, iron ore, bauxite, and rutile, a metallic ore used in the manufacturing of paint. Yet, by 1991, as a result of years of poor administration, corruption, and economic mismanagement, it was a net importer of food, its transport infrastructure was in ruins, local industry had collapsed, fuel was seldom available and, even in the capital of Freetown, electricity operated only sporadically and water shortages occurred frequently.

Inflation was estimated at the rate of 150% per year and was probably much higher. The local currency, the Leone, devaluing at a rate equivalent to or exceeding inflation, was effectively floating. During the 15 days during which the feasibility study was being conducted, the Leone lost 10% of its value, with the exchange rate climbing from 410 to 450 Leones to the U.S. dollar.

Commercial and banking transactions were snarled as the largest currency note in circulation was a 100 Leone bill (about 25 U.S. cents). The manager of one bank admitted that bank cashiers had stopped counting the money but tied currency into bundles and weighed them to determine their value. According to the manager of another bank, the nightmare of cash transactions would have been even worse were in not for the fact that at least 8 and perhaps 10 billion of the 11 billion Leones in circulation were confined to the parallel market and never entered the commercial banking sector.

Banks were paying interest rates between 58% on 30-day deposits and 65% on 270-day deposits while interest charges on loans were kept 10%-15% over deposit rates but were negotiable on a daily basis only. In most cases, banks could not make loans because the parallel market controlled 80%-90% of the money in circulation and they did not have any cash. There had been a 30% increase in rice prices, calculated in Leones, but a drop in price of 21%, expressed in dollars, due to a decrease in the world market price for rice. At the same time edible oil prices had jumped by nearly 26%.
(continued-)

submitted to FAM by Marine Overseas Services

S Maxwell and T Owens explain that *"The local currency counterpart funds generated by commodity aid are not an additional resource over and above the value of the commodities themselves: the resource transfer takes place when the commodities are sold into the local market. The expenditure*

Box 7-f. Sierra Leone case study (continued).

Statistics on Supply and Demand: In attempting to analyze local agricultural production of rice and edible oils, consultants found statistical information to be badly outdated, unreliable, and often simply unavailable. There was little agreement on rice requirements, domestic production, or import levels might be. For 1991, the Food and Agriculture Organization (FAO) estimated domestic production to be 286,000 MT while the GOSL claimed twice that amount, making an estimate of 544,000 MT. The FAO set rice requirements at 774,000 MT, representing a deficit of 410,000 MT, while the GOSL estimated the rice deficit at 153,000 MT. FAO's estimate of rice imports was 78,000 MT, while the PVO appraisal estimated imports were at least 200,000 MT. No reliable statistics on local demand and consumption of edible oils were available, and the data on domestic production of edible oils was from 1987.

From interviews with customs officials and traders, it became apparent that, although import duties on basic food commodities were low, they were often either waived or not collected at all. Port and customs records were either incomplete or not available; and there was a dearth of records from which information on volume and value of imports could be estimated. Essentially, no records could be located on rice imports, while the few records for edible oil imports were found to be maintained by brand name, not source or type of importation, and quantities were recorded as package units with no indication of unit volume or weight, without which data it is impossible to calculate value per ton.

The **Port** of Freetown is known as one of the most poorly managed ports on the West African coast. The worst cases of mishandling, pilferage, and theft were confined to PL 480 commodity shipments, especially **rice**. PL 480 commodity losses were found to be very high and far above acceptable minimums. Yet private imports of rice and other food commodities do not suffer comparable losses. The people of Sierra Leone regarded food aid as a gift directly to each of them. Anyone who could get near a ship or warehouse considered it their right to make off with all they could carry. Hawkers enjoyed a thriving trade on the docks selling plastic sacks for the purpose of carrying home pilfered food.

A cargo of Title I rice that landed a few months prior to the monetization study became notorious as an example of the chaos at the port. Discharge of that cargo degenerated to near-riot conditions, as security forces lost control of a large crowd which arrived by land and by canoe to "welcome" the ship. Several hundred looters swarmed over the vessel. Security personnel lost control of the situation and then themselves joined the mob in highjacking as much of the cargo as they could carry. When reinforcements arrived, shooting broke out, killing one and wounding at least two others. Losses from the cargo were extensive; the captain was forced to sail and stand the vessel off the port until order could be restored. Even a well-supervised CRS Title II cargo of bulgur wheat, discharged over a three-day period under CRS control, suffered port losses of 60 MT from a 1,400 MT consignment, a full 5%, although bulgur is less desirable than rice.

Qualification of Bidders: Regardless of the economic and security situation in the country, private traders were trading successfully in food commodities. In the course of discussions with both GOSL officials and local traders, however, it was suggested on several occasions that PL 480 monetization sales should be limited to Sierra Leonians of African descent, and that other traders, particularly those of Lebanese and Asian descent, be excluded from participation in the program.

Lessons: In spite of what was deemed a chaotic situation overall, CARE did manage to arrive at valid conclusions on market conditions, Bellmon Determination Analysis, logistics, and potential sales arrangements for a monetization project. Estimates of levels of rice and edible oil imports, accurate enough to meet USAID program design requirements, were assembled from records maintained by clearing and forwarding agents and local traders. Estimates of domestic consumption were calculated from statistics for other African countries compiled by UNICEF, while production estimates were extrapolated from old statistics and a variety of more current figures furnished by FAO.

The study concluded that rice would not bring an A.I.D.-mandated minimum sales price; it would be too risky to import through Freetown Port; and that commercial imports would probably meet shortfalls in domestic rice supplies. The study recommended that vegetable oil be selected as the commodity to be monetized because it was in high demand, would command higher prices, and could be cost-effectively containerized, circumventing serious port losses.

of counterpart funds will set in train a process of demand expansion for a varied basket of commodities. For this reason, a diversified package of commodity aid and foreign exchange is most appropriate, including access to consumer goods." (1991 The Developmental Uses of Counterpart Funds Sussex: IDS Discussion Paper 289).

As with food, currency can lose value for reasons other than pure supply shortfalls, such as speculation, leading some to argue for monetization to help stabilize local currency value. This action might be an effective intervention in cases where local currency doesn't circulate because of a decline in confidence in its value. In the recent Somalia emergency, food aid monetizations were recommended specifically to stabilize the Somali shilling.

What other impacts might monetization have?

As discussed in chapter 3, monetization frequently have any number of positive impacts, often indirect or downstream. For example competitive auction sales invariably promote the formulation of markets and the maturity of information flow. Laura Bailey explains that *"You're creating your own addition to the market information available. The price formation mechanism, supply and demand, is right in front of you and will help the traders learn what the prices are and to notice things about each other. Their information will become less asymmetrical."* To the extent that you can identify or conceptualize positive impacts, consider how they can be included in your program design, expected outputs, and justifications for your proposal to AID.

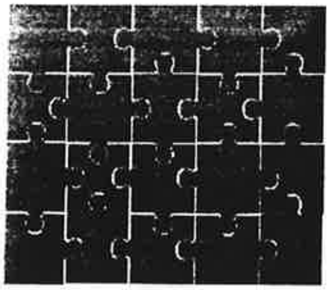
➢ ***FURTHER READING:***

1. *H Bruton, C Hill 1991 The Development Impact of Counterpart Funds Washington DC: AID.*
2. *J Fitzpatrick 1988 Food Aid and Agricultural Disincentives, New York:, CARE.*
3. *World Food Programme Annual Food Aid Review (e.g. 1992 Food Aid Review) Rome, Italy.*
4. *S Page 1990 Trade, Finance and Developing Countries NY: Harvester Wheatsheaf.*
5. *E Clay, O Stokke 1991 Food Aid Reconsidered London (in particular, the chapter on a pragmatic approach to disincentive effects by S Maxwell).*
6. *J Clement 1989 "The Macroeconomic Impacts of Counterpart Funds" Washington DC: International Monetary Fund working Paper WP/89/63.*

-- for examination of import, tariff and subsidy policies of the Philippines, Nepal, and Indonesia see

7. *T Sicular 1989 Food Price Policy in Asia: A Comparative Study.*
8. *L Dudley, R Sandilands 1975 "The Side Effects of Foreign Aid: The Case of PL 480 Wheat in Columbia" Economic Development and Cultural Change, 23(2): January.*
9. *L Hall 1980 "Evaluating the Effects of PL 480 Wheat Imports on Brazil's Grain Sector" American Journal of Agricultural Economics 62: 19-37.*
10. *C Timmer, W Falcon, S Pearson 1983 Food Policy Analysis Baltimore: Johns Hopkins Press.*
11. *1990 Agricultural Policies Markets and Trade: Monitoring and Outlook Paris: OECD.*
12. *R Ahmed, A Bernard 1989 Rice Price Fluctuation and an Approach to Price Stabilization in Bangladesh Washington DC: IFPRI.*
13. *publications from Food and Agriculture Organization's Committee on Commodity Problems.*

CHAPTER 8.
THE APPRAISAL: AGREEMENTS AND COLLABORATION



During the appraisal stage, is it important to take the time to contact many other organizations?

Absolutely. Much of the information you need already exists at different offices in-country. And identifying who the different players are in the commodity markets is a fundamental part of the appraisal. During this stage you should hold meetings.

- with the host government and appropriate ministries;
- with trade associations, customs, and Chambers of Commerce;
- with the donor government, usually the USAID Mission;
- with sub-recipients, collaborating indigenous NGOs;
- with local bankers;
- local transporters, truckers, warehouses;
- with other US PVOs that have conducted or might conduct a monetization;
- with financial intermediaries such as banks, brokerage firms, credit unions.

But aren't lengthy meetings more a part of the planning stage, not the appraisal stage?

By the time you start to draw up a detailed proposal, you should <u>already</u> have determined whether a monetization is reasonably do-able. This means you need to have appraised the degree of interest of the government, USAID, and potential buyers. Many well conceived monetizations proposals have <u>not</u> gone forward because they lacked one or two key approvals. PVOs exploring the possibility of monetization often turn to **other** PVOs for guidance. Smaller PVOs, in particular, frequently seek alliances with PVOs with more expertise in food aid with ongoing country programs. It is often fruitful for PVOs to meet at the earliest stage to discuss common concept papers which can then be taken to the local USAID mission.

Chapter 8 Action Checklist

Have you:

☑ ***Floated a concept paper to local USAID officer as well as to PVO headquarters?***

☑ ***Investigated possibility of sub-receiving local currencies from other monetizing agencies, from the Mission, from Title I, or Title III?***

☑ ***Met with Host Country representatives to secure host country agreement, and exemption from taxes and duties?***

☑ ***Drafted recipient agency agreement with all local counterparts that might be using monetization proceeds?***

☑ ***Discussed collaborative efforts with other NGOs conducting parallel programs?***

Should the PVO wait until it has conducted its initial appraisal and drafted a solid proposal before approaching USAID?

No. Most successful monetizations have involved a close working relationship between the PVO and USAID from the earliest stages of design. One of your first steps in a monetization should be to give a short concept paper to the appropriate USAID officer at the local Mission. This may be a Food for Peace officer or the USAID staffer involved in agriculture, credit or other programs. This early action is important for three reasons. First, if USAID is against the idea of monetization, you should find out as early as possible, so that you don't waste your time. Second, USAID staff have country objectives, insights into local markets and a knowledge of other monetization programs of

Box 8-a. Title III sales proceeds may be available .

Title II and Section 416(b) food aid are referred to or assumed to be the subject throughout this workbook. But recall from Chapter 1 that Title III food aid is also provided to many poor countries and that the enabling P.L. 480 legislation encourages that it be used for projects that NGOs implement.

Again, Title III is a government- to -government (bilateral) mechanism for granting food aid from the US Government to nations that are relatively food insecure. (The 1990 Farm Bill reorganized Title III to include what had previously been Section 206 aid under Title II.)

Title III food aid is now negotiated directly by USAID Missions and authorized by their respective regional Bureaus in Washington, D.C. They are often negotiated as multi-year grants and tied to large policy issues such as market reform or democratization which AID may encourage. It is up to the regional Bureaus to determine policy on how much Title III will be offered. Because Title III accounting and monitoring now devolves to USAID Missions, some Bureaus may be reluctant to emphasize Title III grants relative to their other assistance programs. Where Title III proceeds are deposited to special accounts for numerous activities, it may place great reporting demands on Mission staff. It may be in the interests of PVO field offices to talk with their Missions if they wish to encourage Title III programming. In FY91 16 countries received a total of $293 million worth of Title III assistance.

In most cases the recipient governments monetize the foods received. The sales proceeds must be used for approved project or sectoral support related to privatization, food distribution, food security, nutrition or child survival.. AID guidance on title III strongly encourages that it be used to support nutrition-oriented food aid interventions and child survival projects. Title III guidelines suggest using Title III commodity sales and local currency as "support for US private voluntary organizations and cooperatives and encouragement of the development and utilization of indigenous nongovernmental organizations.
The sales transaction may be through open bidding or direct negotiation.

AID Guidance reads "For Accountability purposes, the recipient country should establish a separate interest-bearing account for the deposit of local currency sales proceeds."

The legislation also requires that Missions shall program 10% of the proceeds into a separate account to support indigenous NGOs and cooperatives. This requirement may not have been met in many cases. The legislation encourages these governments to work with and through PVOs wherever possible.

PVOs should talk with both with USAID and with the governments to inquire about access to these monetization proceeds, and perhaps to offer to help in the programming process, for two reasons:

1). The government may have proceeds and be less clear, creative, or professional than PVOs about how to identify effective and efficient development projects;

2). In countries where Title III programs are current, USAID missions may be unwilling to to approve of additional Title II monetizations.

which you should be aware as early as possible. Third, if USAID is encouraging, and you begin to incorporate their feedback from an early stage, they have bought into your effort to a degree. They can then become an ally in your subsequent negotiations with the host government, and with other departments of the US government. Title II programs implemented by PVOs need to find links or hooks that align these projects with the focus and concentration of local USAID Missions.

If a PVO has been conducting food assistance, USAID may already be providing cash support for complementary costs through the proceeds from Title I sales. Since Title I is sold to governments, consequent sales are not always referred to as monetizations. But the sales proceeds are just as real as when a PVO monetizes. Look into what Title I proceeds are available, if the Mission likes your project.

An analyst of PVO projects, Jim Pines, has written "*Any food distribution and program activity costs that would be underwritten by monetizing Title II commodities should be important enough to the Mission and the Government to justify funding from other sources. The modest amounts of local currency that can be derived from typical Title II monetization can more easily and efficiently be managed as part of Title I and other Government sales already occuring. Challenging PVOs to persuade technical officers and the Government that PVO innovations merit support helps to assure eventual institutionalization of outstanding projects.*"

Sometimes the Mission will be the driving force behind getting a monetization started. In Uganda the USAID mission was unhappy with an ongoing direct distribution food aid program. They asked ACDI, a US agricultural cooperative, to assess the situation and make recommendations. After a year ACDI knew more about marketing in Uganda than anyone else, including some of the professional traders. ACDI brought in people with extensive experience in the trading of commodities who applied their proven skills in analyzing the market. The PVO considering monetization must be aware that it might find itself very involved in commodity marketing, which requires a completely different set of skills and knowledge from those used in the usual development projects.

Also get to know the Commercial Attache in the US Embassy, and the USDA Agricultural Attache (if there is one). The Agricultural Attache represents USDA's Foreign Agricultural Service, which monitors all food issues in-country, and has direct ties to 416(b) programming.

What other sources of proceeds should be examined?

Also inquire about **Title III programs** in the country (see Box 8-a). Title III programs offer the prospect of ready access to local currency proceeds for project support (if the government is willing to offer it) without the trouble of conducting the sale. Also, PVO Title II monetization proposals and food sales have encountered difficulties in several countries where they were seen by USAID to be competing with Title III sales. Everything else being equal, a PVO Title II proposal is more likely to be approved in a food insecure country that does <u>not</u> have other ongoing food sales. Title III programs are negotiated between AID and the recipient governments and quite often involve

100% monetizations. For instance, 46,000 MT of US wheat was donated to the government of Kenya all of which was sold, generating $10 million for rural road maintenance.

Are foreign governments usually favorable to monetization?

Frequently, but not always. third world governments will have not heard of PVO monetization, so it may simply be a matter of helping them to become comfortable with their agreeing to continue to waive import duties. Remind them that in a PVO monetization, the money stays **in** the country. Many of the poorest nations' governments conduct all food aid monetizations themselves (for example, Title III assistance). Worldwide, the bulk of bilateral food aid is sold by these recipient governments.

But even if a government agrees to allow a PVO to monetize, it may not always waive import duties. Host governments often require that the PVO abide by local trade restrictions to protect indigenous industries. Usually, the PVOs will also be required to use the official exchange rates as well. An artificially low exchange rate can make it difficult to sell imported foods at a good price. Conversely, many countries maintain overvalued exchange rates which make it difficult for PVOs to import cash at full value and thus make monetizations more useful. The host government will need a description of all your program's activities that will be supported by monetization and its proceeds. You will need to obtain a written "Host Country Agreement" between the PVO and the government, usually with AID as a third party. It should include:

- Consent to work with counterparts
- Consent for PVO to undertake all proposed activities
- Agreement that PVO may convert local funds to US dollars (when approved by AID)
- Incorporation of Regulation 11

Box 8-b. Core elements of a Host Country Agreement

1. Name of country;
2. Address of organization and ministry representing the government;
3. Statement of understanding and support of food sales;
4. Statement of government support of NGO efforts, recognition of its nonprofit status;
5. Statement of USAID's relationship with the cooperating sponsor;
6. Statement of PVO goals
7. USAID agreement to provide commodities to PVO;
8. Description of how sales proceeds will be spent;
9. Responsibilities of PVO to import, deliver, manage, and monetize commodities;
10. Government exemption of PVOs from import and port taxes, duties, consular invoices fees, or levies;
11. Government agrees not to re-export
12. Responsibilities host counterpart agency to manage program and funds;
13. Specification of commodities, expenses, and approximate sales prices;
14. Signatures
15. Dates

Host Country Agreements (see box 8-b for an illustrative outline) establish a legal basis for the transaction that is about to take place within its country. It is important for host government officials to understand the idea of monetization, the goals of the PVO, and the role of the host government. During this phase, the PVO should be able to work with the various ministries involved, be culturally sensitive, and be able to work with local authorities.

You may need to meet with representatives of multiple offices, including ministries of agriculture, trade, commerce, and treasury.

Do local counterparts ever conduct a monetization? What is their role?

There are no regulations prohibiting any organization from monetizing, including indigenous NGOs. For a foreign or indigenous NGO to access US food aid, it would need to obtain cooperating sponsor status from AID and to date few have. More typically, the local NGO will be the recipient, sub-recipient, or sub-sub-recipient of the currency proceeds. In such instances, the PVO needs to sign with the counterpart a Recipient Agency Agreement which spells out what the proceeds can and will be used for, and the counterpart's liability (repayment) for unallowed expenditures. The MYOP and Regulation 11 should be incorporated into the agreement.

Are there any advantages to PVOs sharing experiences and plans on monetization?

Yes. In fact PVOs can split up efforts or take turns performing elements of the monetization, sparing a great deal of expense, effort, and uncertainty. PVOs are increasingly submitting joint proposals and joint AERs for collaborative monetizations. This can entail one PVO taking the lead, alternating their respective functions or even setting up a separate monetization foundation or consortium, an office just for conducting monetizations.

One PVO, ADRA, chose early on to seek collaborative relationships where possible rather than duplicate the process of developing expertise in monetization. Recognizing the lack of commercial experience of most of their staff, and yet acknowledging a heavy and growing dependence on monetization proceeds, the ADRA food aid and programming planners made the decision to take advantage of the experiences of field people working on monetizations already in place, including other NGO programs, umbrella groups, and government to government Title III sales.

Box 8-c. CARE's suggested expenses for calculating the cost of monetizing on behalf of other

1. Lawyer's fees
2. Port handling fees
3. Purchase and rental of equipment
4. Coverage for losses
5. Bank charges
6. Survey costs
7. Administrative and accounting costs

from CARE 1992 Step by Step Guide to Monetization New York pg 28

If two PVOs conduct a joint monetization, do they submit one or two operational plans and separate Annual Estimates of Requirements for food?

In most situations where joint monetization has occurred, each PVO has submitted its own separate Multi Year Operational Plans (MYOPs) and Annual Estimate of Requirements (AERs). In the introduction and monetization chapter of their MYOPs, they discuss how they will collaborate on a monetization. They will annex a copy of the agreement between the two organizations to their MYOPs. AID has not imposed upon the PVOs any standardized agreement to be used between two PVOs. Each PVO retains ownership of its own food funds and accountability.

In other situations, one PVO has agreed to pass on to another PVO part of the proceeds from food that it has called forward. In this instance, the second PVO is a sub-recipient only, and does not have primary ownership of the food. The second PVO must accommodate itself to the timing and disbursement decisions of the first and must submit audit reports to the first PVO. In turn, the first PVO retains accountability responsibilities for the second PVO's activities.

Box 8-d. PVOs working in Bolivia created a widely admired consortium that efficiently sells food and manages proceeds on behalf of each of its NGO members

Beginning in 1988 the local offices in Bolivia of ADRA, CRS, Save the Children and Food for the Hungry International began planning what in 1989 became the Interagency Monetization Committee ("Directorio"). The primary goal of this collaborative effort was to sell Title II commodities and thereby provide funding for development projects. Technical assistance was provided by various ministries of the Bolivian government, by AID and by a consulting firm in the US (Planning Assistance). In 1990 a full-time manager was hired, and soon thereafter an international accounting firm retained to provide in house review of operating systems.

The Board of Directors (composed of the PVOs, AID and the ministries of agricultural and commerce meet regularly to discuss and make decisions on all activities, including: sale of commodities; purchase of local commodities; financial management; reporting/Information management; disbursements to agencies and projects; review/visits to agency projects; and monitoring.

Projects are supported by sales proceeds if funds are available, and the MYOPs are in accordance with and approved by the members of the Board (including AID). Proceeds are not disbursed to a project if it has not spent over 70% of its previous currency transfers.

The consortium is composed of different departments. The Commercialization and Commodities Department manages the food pipeline and the conduct of the sales. This department has the technical skills to prepare tenders, write contracts, keep a running register of contracts and bank guarantees and payment records. It also is responsible for the spot control and staff training for inventory management at warehouses.

The Project Department consolidates and exchanges information on the projects that are funded. This involves site visits, maintaining operational plans, reports, external evaluations, and exchange of lessons learned.

prepared for FAM by D Witkowski of Catholic Relief Services and R Hoag of Feed the Hungry Intl.

What are Monetization Coalitions?

A coalition approach to monetization is undertaken when PVOs collectively decide to establish a separate, in-country office to perform monetizations and invest the proceeds. The most well-known example is the Bolivia consortium of PVOs (see boxes 8-d and 8-e and 8-f). In Bolivia the coalition was involved not only in selling food but in helping to use the proceeds for internal purchase of appropriate foods as well. Coalitions between PVOs have operated as well in the Philippines, Ethiopia, and Burkina Faso. CARE and the National Cooperative Business Association have shared in a 100% monetization in Indonesia. A country like Ghana, with many PVOs operational, and many considering monetization, would be a logical choice for future coalitions. Coalitions can offer far greater efficiency, and a reduction in redundant PVO efforts. They also can serve as a mechanism for routing funds from other, non-food aid, sources.

Box 8-e. Some of the benefits and complications of the Bolivia PVO consortium

PROS:

- More efficient management of logistics:
- No competition for sales
- less staff time in each agency
- No need for specialization in each agency
- No duplication of effort
- Larger bulk sales and purchases (better prices)
- Single bank account - easier monitoring by AID and auditors
- Lower costs to each agency
- "Peer" review of projects promotes quality learning and sharing experiences, and reduces duplication
- Many minds review policy decisions
- "Decentralization" from AID to agencies
- One point of supervision/monitoring rather than four
- Learning/interchange between agencies to improve projects
- Technical assistance, guidance in projects, planning, etc.
- No more competition/bickering, sometimes due to religious differences.

CONS:

- Not as agile as individual management
- Time each agency director must spend in Committee meetings is sometimes overwhelming
- Agencies are judge and jury for approval of project plans and for this reason, the need for creating technical units
- Decision-making: must reach consensus or submit to majority decision
- Longer time to make decisions, changes, etc.
- Lines of authority sometimes unclear Manager sometimes unsure who has final say
- Many outside pressures facing committee on each decision AID, GOB Ministries, business groups, etc.
- Conflicting interests sometimes present difficulties:

  Sales: Who gets proceeds and when?

  Purchases: Which product first, for whom?

  Prices per commodity vs. Cash flow

  Exchange rate problems

submitted by R Hoag of Food for the Hungry Intl and D Witkowski of Catholic Relief Services

Using the coalition approach, who does what?

In some cases a single PVO takes the lead and manages the technical aspects of the monetization. In other cases, the PVOs rotate taking turns for different responsibilities. In yet other cases, independent entities are created, such as the Bolivia Consortium, that hire their own staff.

When one PVO acts as a selling agent on behalf of other PVOs, you need to determine the percentage fee retained for this service (proportional to or equivalent to the expenses of appraisal, planning, negotiating, sales and delivery) (see box 8-c). There are numerous advantages to the joint effort. Together the PVOs have a greater voice in negotiating with the government; there are economies of scale achieved in conducting market research and tracking changes in the commercial environment; and the monetization funds permit the PVOs to conduct development activities (family-level wells, greenhouses) that otherwise would not have been funded by donors.

In the case of the Bolivia Consortium, Food for the Hungry and Catholic Relief Services took turns being legally responsible for the handling of the monetization. The lead agency's legal responsibility for the conduct of the monetization ends as soon as proceeds are disbursed to member agencies. Its responsibilities include enforcing USAID regulations and decisions, acting as chair of the Board meetings, representing the consortium management to the Bolivian Government, and being the legal employer of the consortium staff. The sharing of responsibility also entails the sharing of risks, such as losses. Being the lead agency can entail involvement in macroeconomic issues. In 1993 CARE became the major importer of cereals into Somalia and a large source of currency for all agencies. One CARE staffer claimed, "CARE in Somalia is becoming a mini Ministry of Commerce, and that's testing us to the limit."

Box 8-f. Lessons learned by those involved in the Bolivia Monetization

- Investing in a few high-quality staff, especially the manager and accountant provide high returns. The manager in particular should be a adept at diplomacy and not necessarily a technical expert in marketing or monetization.

- Monetization is essentially a financing organization and thus require up-front development of good accounting systems that meet AID requirements.

- Management information systems must be timely and simple to keep pace with fast-changing markets

-To provide a guiding tool, conduct a strategic plan with all the parties as quickly as possible.

-It is essential to clarify who is in charge (PVOs?, USAID? etc.) and the role of each entity.

- Rules must be clear and be disciplined in applying rules, especially during bids with the public and treatment of member PVOs.

- Circulate periodic and professional public relation reports to the press, USAID and government.

prepared for Food Aid Management by R Hoag of Food for the Hungry International and D Witkowski of Catholic Relief Services, 1992

If PVO collaboration and coalitions are such great ideas why don't PVOs form coalitions for all monetizations? Should a small PVO just expect to plug into coalitions and not get involved in the nitty-gritty of monetization?

Much of the collaboration between PVOs is informal and involves sharing of technical experience and market information. In difficult circumstances, such as Haiti, PVOs have worked together out of necessity. In other situations, such as in the Philippines, PVOs have been encouraged to plan monetizations together by USAID.

Despite their potential, coalitions have been slow to form in most countries. The Bolivia model of a formal coalition, while allowing efficiency of sales, binds PVOs to work through an independent agency that reviews the PVO's records and is accountable for what the PVO does. This adds an extra layer of oversight, negotiation, and paperwork on an operating environment already encumbered by a great deal of regulations and red-tape. The step from working together informally to becoming responsible for each other raises enough difficulties that PVOs often shy away from them. This extra layer of responsibilities leads some lead NGOs to charge their expenses to the monetization itself (see box 8-b).

The Peru model, where a single PVO (with AID support) monetizes on behalf of others, may be less common in the future. AID has recommended that a new, separate, non-operational entity (the NGO PACT) should coordinate and conduct future monetizations for all the NGOs in Peru. This may

Box 8-g. World Vision guidelines on procurement, contracts, bidding

On many projects it has been necessary to obtain the services of local truckers, mechanics, laborers, etc. You are to treat the procurement of services exactly the same as you would the procurement of materials and supplies. When you have the time and when there are multiple suppliers on the local markets, it is always best to go out for competitive quotes. Competitive bids always get the best results fro the most realistic and reasonable prices. Of all our African relief projects, the most frequent mistake made by our field teams has been that they have been in too big of a hurry to buy; they take the first price offered by the first and only supplier solicited.

When only one supplier is used, this is called a sole source contract. Sometimes it may be justified to go sole source, particularly when the supplier has the best quality that meets our specifications. In this case, you must know what the going rate is on the locla market and be prepared to negotiate. In most cases, there is no substitute for competitive quotes. In competitive bids, the purchase order, or contract if necessary, should in principle be awarded to the lowest bidder. But it does not always work out this way. There are other factors that must be considered, namely, the quality of the product or services and the timeliness of delivery.

In Zimbabwe, when preparing to receive 10,000 MT of maize from the US through South Africa destined for Mozambique, we did not award the contract to the lowest bidder. There was only one bidder out of the five solicited who had the capability and willingness to do what had to be done: who would provide warehousing and truck haul and would haul the food commodities into hazardous areas in Mozambique. The quality of this particular company's operations was high, and their can do attitude was impressive. After World Vision made the selection to go with this partular contractor, sbusequent meetings resulted in serious and successful negotiations since some of the incremental rates were able to be reduced to our benefit.

from B Boyd 1987 Getting It There: A Logistics Handbook for Relief and Development *Monrovia, CA: World Vision International* indicate a trend be for monetizations to occur more through independent bodies, rather than the PVOs themselves.

Along these same lines, a separate "Ethiopian Food Security Foundation" has been proposed to address the multiple, piecemeal monetizations occurring in that country (discussed in chapter 2). This foundation would meet head on the sophisticated demands regarding exchange rates, market prices, and managing accounts. S Maxwell writes:

"The Foundation would act as a specialized intermediary organization between official and non-governmental food aid donors on the one hand, and operational project agencies on the other. It would not itself implement projects, but would offer expertise, standardized procedures and possible economies of scale in the monetization process."

Taken to a further extreme, an international entity might be established which would sell commodities wherever they commanded the highest returns. In this way, food sales would help dampen transitory food shortages as they occurred in one country or another, and would also achieve the highest possible revenue stream for project support. This idea requires at least partial de-linking of sales with maintaining currency in the country of sale.

➢ ***FURTHER READING:***

1. *AID guidance, USAID Mission communications to PVOs.*
2. *AID 1992* Regulation 11.
3. *CARE 1992* Step by Step Guide to Monetization *NY: CARE.*
4. *D Belshaw 1990 "The Macroeconomics of Counterpart Funds: The Case for Food for Hunger Prevention in Ethiopia" in S Maxwell and D Belshaw,* Report of Food for Development Mission *Rome: World Food Programme.*

CHAPTER 9
THE PLAN: MEETING WITH POTENTIAL BUYERS

Why meet with buyers again, after having done so in the market analysis?

The point of this chapter is that the "plan" phase of the monetization process requires an extension of the market analysis in the form of field level interaction with key players. While the written plan could be composed anywhere, there is a great deal information still required and decisions to be made that cannot merely be conducted in a US headquarters.

Regardless of whether the appraisal stage lasted 1 month or 16 months, continued monitoring of food markets will be required, up to and during the actual time of sales. As you near the point where you obtain approval and call forward your commodities, you will need to intensify your relationship with wholesalers and importers so that you properly anticipate:

- Their sources of credit and any potential weaknesses that may suddenly reduce their ability to pay; remember that your buyers have greater access to short-term credit than to long-term credit; it may be easier for them to post a bond than to complete a full payment 6 months from now. You are now at the stage of deciding **how** you will sell your commodities. Therefore you want to learn as much as possible about your customers, for instance, whether credit, solvency, and market access differ between ethnic groups. Loans available to traders may or may not be advertised, and therefore are available effectively only to large wholesalers who are tapped into the banking system.
- The relative scales of demand in-country for basic commodities, and whether there may be large shifts because of the current year's harvest, erratic rainfall, an oil price change, war, or other event.

Chapter 9 Action Checklist

☑ ***Discuss with merchants or float draft tenders to determine their needs in terms of credit, timing of payment, food quality, food grade, packaging, point of transfer, etc.***

☑ ***Study the degree of market concentration of wholesalers of each commodity; ascertain the commodities that are controlled by market forces and those commodities that can be manipulated by a few powerful traders;***

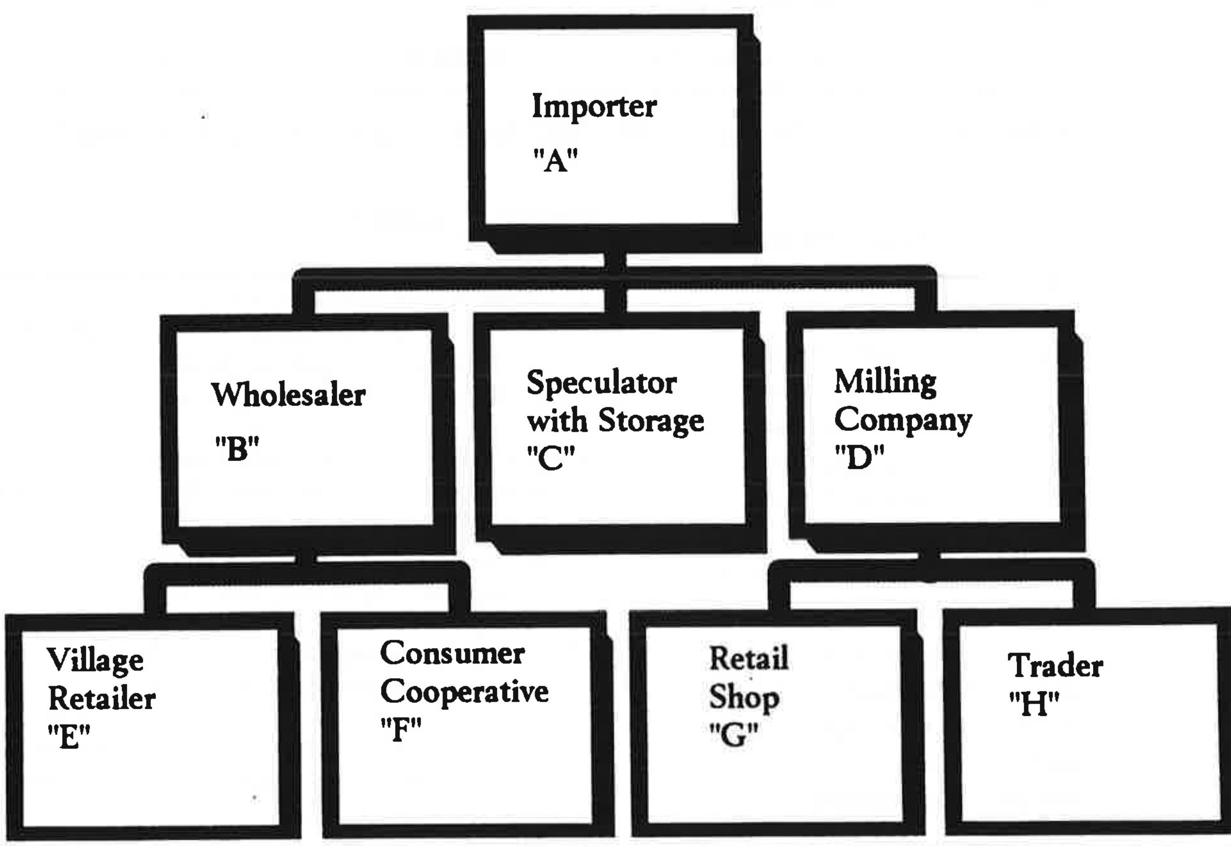
☑ ***Remember to stipulate that foods may not be transshipped or reexported;***

☑ ***Begin haggling: determine your initial asking price, given the local culture of bargaining.***

try to anticipate the effects of a $50/MT price increase or decrease in the world price of your commodity, both in terms of your buyers, and overall demand at the household level. Examine whether you have access to time series data for your country from Ministries, the World Bank, or agricultural research center. In some African countries, different famine early warning systems track prices.

- The **quality** of the commodity expected or demanded by potential buyers. The question of quality is particularly important among private merchants who may have difficulty selling US varieties of foods. Consult with local traders to best understand the grade and quality that they think they may be receiving. For instance, US red sorghum has not been popular in Chad, and yellow corn has been poorly received in many southern African, and Central American countries. When discussing cereals, ask about the minimum protein content required, the maximum moisture content. Quality issues also involve the dirt, broken grain, spoilage rate, amount of foreign material, hardness, and packaging of the food. Ask about the minimum percent damaged that is acceptable. Request from USDA a sample of the grade expected. When discussing grades with your buyers, specify the lowest-quality grade designation that is acceptable for delivery in settlement of a contract. In one monetization, Save the Children/US had great difficulty completing the sale of milled, long grain, grade #5, 20% broken rice in the Sudan when the arriving rice was not similar to the sample rice that SCF had shown to the buyer, the Gezira Trade and Services Co, Ltd, a government Parastatal. An independent lab confirmed that the rice had changed color, taste and quality, though it remained fit for human consumption. The incident was potentially ruinous, but the

Box 9-a. A generalized market hierarchy



buyer fortunately went ahead with the exchange and payment anyway. However, in subsequent years, Save the Children and the buyer had to agree in advance to minimum grade requirements.

- The preferred packaging or appropriate; whether bagged or bulk; drums, tins, etc.
- Acceptable or expected methods of treatment of the foods (DDT, insecticides, rodenticides, fungicides).
- Potential for selling **unfamiliar** foods, such as the many soy-fortified products. What is the local taste for soybeans? Have they any familiarity with corn-soy blends? Have they any familiarity with bulgur wheat?
- The preferred methods and points of delivery. Your buyers should be involved in the choice of the forwarder and stevedores, and in helping you decide the terms of your contracts (delivery after unloading, the manner in which the importers and traders would share losses and expenses incurred during the transport and unloading, etc.). More often than not, the PVO would prefer to transfer title of the commodity at port and undergo no further risks, expenses and effort.

Box 9-b. Knowing your counterparts: a description of market niches and players in Mali.

"Informal credit from buyer to seller and seller to buyer is a central feature of market operations: written contracts are virtually unknown. Only the larger and more experienced traders maintain bank accounts or use formal bank lines of credit.

"...traders strive for maximum turnover and minimal storage, in response to market volatility. Market conditions such as falling prices or a temporary glut might force them to hold grain for more than two months, but they generally prefer to buy only what they can sell in a period of one to two months. In the coarse grains market, some small wholesalers make purchases almost entirely on the basis of orders from larger wholesalers... who commit to buy a fixed amount for a fixed price with delivery in one to two weeks. Such operations make heavy use of supplier's' credit, with full payment at each level of the market chain only after the final transaction has been completed.

"In the past Malian law identified seven classifications for cereal traders, depending on their sales volume, and it imposed different requirements for each under the system of commercants agrees. This system has (now) been dismantled, and traders are distinguished only by the size of their total operation (annual sales volume), which determines the level of annual registration tax (patente) they must pay. Nevertheless, the informal distinction among wholesalers (grossistes), small wholesalers (demi-grossistes) and retailers (detaillants) continues.

"In the case of rice, the two large traders who have traditionally dominated the market continue to account for the lion's share of commercial imports, but they have been joined by a number of new entrants drawn from the ranks of general import-export traders and senior bureaucrats. The two large traders continue to retain an advantage, given their superior financial strength and their extensive distribution network. The latter includes both small wholesalers linked to the large traders by long-standing credit arrangements and their own in-house distribution system, which for at least one of the traders extends down to the retail level.

"The course grains market is much more competitive and fragmented by its very nature. Unlike the rice market, which channels an imported product to consumers concentrated in the urban centers, the coarse grains market serves to collect goods produced throughout the country and resell them to consumers who are likewise distributed throughout the country. The Bamako market is dominated by 5-10 large wholesalers, but additional large wholesalers are based in the provincial market centers. There is a very large network of small wholesalers (with estimates running up to 200 for Bamako alone). There is no generally accepted grade and standard for either rice or grain: quality premiums are low in Mali."

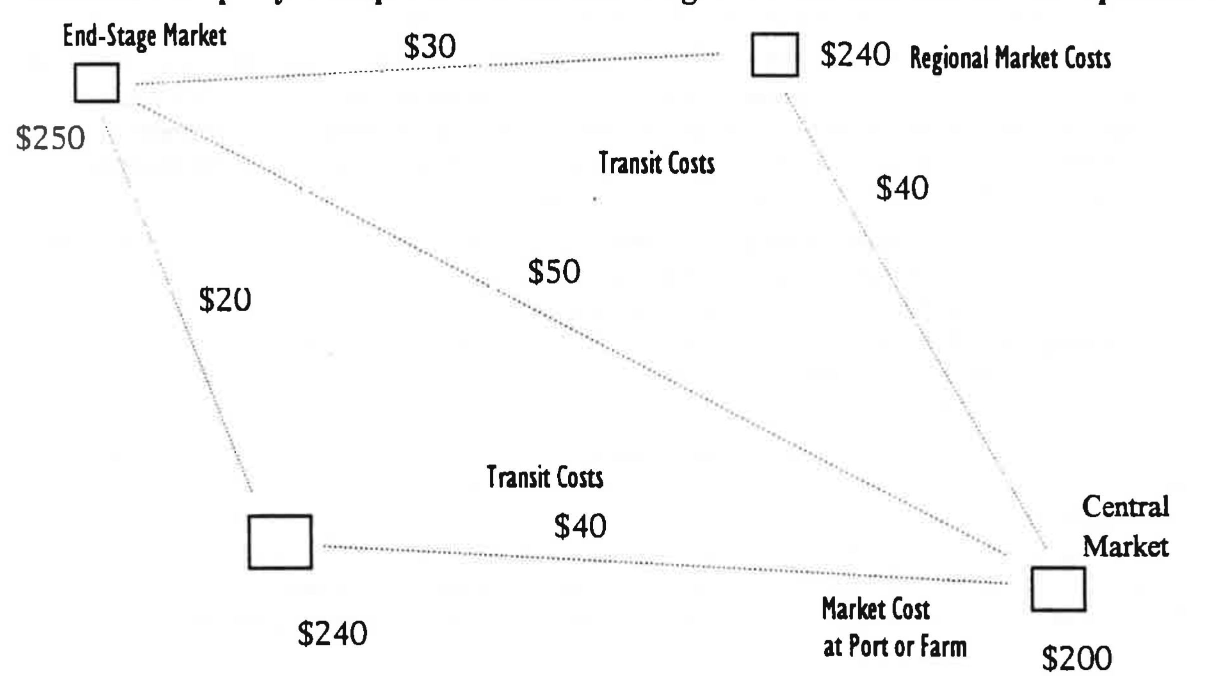
from J Bremer-Fox, L Bailey, P Lang, M Mervenne 1990. Experience with Auctions of Food Aid Commodities in Africa: Volume II Case Studies Roslyn VA: Nathan Associates, pp D2-3

- Market concentration. How many large-scale and semi wholesalers are there? Can one or a few wholesalers drive prices down suddenly if it or they choose to?
- Information that their system depends on. Are their decisions based on weekly price notifications from commission agents?
- Other potential problem areas. For example, discuss with buyers (as well as USDA) the often-reported problem that many of the PL 480 bagged foods will include the label: "Furnished by the people of the United States of America; not to be sold or exchanged."

Will the PVO monetization be affected by regional trade blocks?

Yes, because import quotas and border agreements will affect the prices of foods in the country and the competitiveness of imported goods. A form of collusion that is permitted is when governments get together and create regional trade blocks. Often these forms of regionalism merely group the separate trade-restrictions in the form of a "free trade area" (FTA), a "common market", or a "customs union." The World Bank recently wrote, *"Mexico, Chile and other Latin American countries are lining up to join a free trade area with the United States. Today regionalism is back with a vengeance. In its current incarnation, regionalism has engulfed all major players in the world economy. Division of the world into three trading blocs is being debated seriously. A move is underway to turn the Association of Southeast Asian Nations (ASEAN) into the ASEAN Free Trade Area."* (World Bank 1992 Policy Research Bulletin 3(3): July) Examples of regional trade groups are the Andean Common Market (ANCOM), the Association of Southeast Asian Nations (ASEAN), Central American Common Market (CACM), and the East AFrican Community (EAC). Because the PVO is usually bringing in much-needed

ox 9-c. Examplary costs per MT of a food at regional markets based on transport cost



see W Tomek, K Robinson 1990 Agricultural Product Prices Ithaca: Cornell U Press staple foods and is usually waived from import duties, the effects of trade agreements will appear indirectly in the price levels in country.

Where in the country should the monetization occur?

Before you finish your plan on how and where to sell your commodities, you should have a good sense of where in the market chain, you can most efficiently sell. If you are selling a very large amount of food you may have no choice but to sell to importers. But if you are selling more modest amounts, and you have the transport and storage capacity, you may sell directly to processors, assemblers, retailers, and cooperatives at regional levels. You may then obtain obtain a higher price and have more control over the final targeting. Therefore, by the end of this stage you should be able to describe the market roles and niches involved in the **secondary market channels** (see Box 9-a and 9-b). You need to know if there are there increasing numbers of independent **food assemblers** and how many traders that you might be dealing with specialize in just one commodity? Keep in mind that the market liberalization process tends to open up entry for a greater number of locals to be involved in cereals trade.

As an extension of the market analysis discussed in Chapter 6, you need to have an appreciation for where in the country food prices are the highest, and why. What are the costs of transport to those regions (see box 9-c)? Are the buyers of your foods essentially performing arbitrage (buying low in one region and selling high in another, and providing no other service)? Arbitrageurs do tend to reduce price differentials between regions. But if they are earning a large margin but not incurring large costs, it may be that the PVO can learn from them and take that next step to sell directly in that region. Are traders able to manipulate the price of goods and earn excessive margins on transport? If so, are they able to agree

Box 9-d. Why information on local prices needs to be supplemented with other cost data

"Among the most significant research results... is the critical importance of non-price factors in determining consumption patterns. The purchase price of a food on the market can be a very misleading indicator of its true cost, if the time costs of purchasing and preparing the food are not taken into account. The Mali study.... calculated that the price difference between rice and the coarse grains substantially overstated the true cost difference between the two grains, because millet and sorghum, as they are prepared in Mali, require much more time and labor in preparation than does rice. They also take more time, and thus more fuel in cooking, and they require milling, which involves either time or money, which rice does not. Rice is also considered to be more filling than millet and sorghum, so housewives purchase less rice to feed the same number of people than they would of sorghum.

"Similar reasoning underlies the consumption preference for rice observed in rural Senegal, even though the purchase price of millet was considerably lower. Because of local marketing patterns, millet was available only at large weekly markets, whereas rice could be bought close to the village every day, reducing both time and transport costs and the amount of the minimum purchase needed at one time. ...The changing value of time, particularly women's time, has been shown to be an important factor in altering how prices affect consumption."

"In Sierra Leone, households were more likely to consume cassava if they were producers of palm oil, because the processing of palm oil is a labor intensive task performed by women, and cassava required less time in preparation than millet."

see B Rogers 1989 Consumption Effects of Agricultural Policies: What Do We Know? USAID: Office of Nutrition among themselves on artificially low prices they would offer you? Are many of the apparently independent food traders actually controlled by one large owner? How much of the food that is produced is stored, or hoarded?

When conducting local market surveys, you will solicit multiple price quotes. Whenever possible, use local staff:

"Have a local national who is familiar with the local markets be a part of the procurement section. If a local store knows an expatriate is making the purchase, the price automatically goes up and there is usually no room for negotiation." B Boyd 1987 Getting It There: A Logistics Handbook for Relief and Development Monrovia, CA: World Vision International)

All this research must be conducted prior to choosing sales mechanisms (chapter 10) and selecting commodities (chapter 11). Once the commodity is in-country, it will not be possible to switch grades or varieties.

After the sale, will the buyer be permitted to repackage and relabel the commodities?

Yes. However there are two important restrictions regarding what they should not. These are:

(1) They must not re-export the foods; and,

(2) They must not sell for human consumption foods that are deemed unfit for human consumption (for example, foods that have spoiled in transit or in storage).

Box 9-e. World Vision barters food for livestock

Beginning in 1989 World Vision used Title II food assistance in a unique activity whereby food was traded directly, or bartered, to local pastoralists for their herds. The livestock were then loaned within the same region to those pastoral families that had lost their livestock and therefore deemed vulnerable by World Vision. The goal was that within three years after receipt of the animals, 50% of these households would transhumant, resuming their annual migratory patterns. During FY89, 3,555 goats, sheep, and donkeys were acquired by bartering food. These were loaned to an initial 450-500 families.

It was also projected that pastoral families receiving loan animals would double the number of female sheep and goats in their herds within three years, allowing for repayment (or reimbursement) of the loan.

The larger vision of World Vision's program in the Menaka district of northern Mali is to smooth the transition from emergency relief to long-term development and also foster community support structures, referred to as "oasis safety nets." In addition to the barter, World Vision has applied food aid to food for work (to support irrigated rice cultivation) and nutritional feeding centers. The pastoral support program is carefully designed so that the livestock loan program is complemented by income transfers that protect the herds. The 1989 MYOP notes:

"In order that the herder not be obliged to sell his recently received animals to meet immediate food needs, a supplementary food ration is provided thereby safeguarding the animal investment. In return for the food package, the herder and his family will participate in feed resource development activities."