Why Kenya's short-term fixes won't resolve its maize supply crisis

October 25 2017, by Timothy Njagi Njeru

A local miller prepares maize outside his grinding mill in Kibera, Nairobi. Credit: Thomas Mukoya

The Kenyan government recently made three policy announcements that are of great importance to maize farmers and consumers. The first was that a subsidy introduced in May 2017 to reduce consumer prices would be discontinued. Before the subsidy, prices had soared to an all-time

high on the back of dwindling supplies.

The second announcement was a significant increase in the government's budget allocation to buy maize from farmers. The third was an increase in the subsidy for fertiliser.

Earlier this year, poor domestic supply caused prices to shoot up. The government decided to allow imported maize to come in. But instead of allowing market prices to prevail, it subsidised the imports to make consumer prices cheaper, essentially subsidising consumers as well as farmers. The food subsidy reduced the price of a 2kg packet of maize flour from 140 Kenya shillings to 90, a subsidy of approximately 35%.

In ending the subsidy of imported maize, the government aims to ensure that grain millers purchase locally produced maize harvested since August 2017. The government has also signalled that it aims to purchase the entire harvest offered for sale by farmers for the strategic food reserve by allocating USD$60 million.

Increasing the subsidy for fertiliser will reduce the input costs for farmers and increase maize yields. But the overall success of these policies is likely to be mixed, especially in the short term.

The three interventions

By the time the maize subsidy was introduced in May 2017, the price for a 90kg bag of locally produced maize was about 4,500 Kenyan shillings, compared to world market prices of 1,400 Kenyan Shillings. This huge price difference is attributed to high input costs, resulting in low productivity and therefore high per unit costs.

The subsidy stabilised local consumer maize prices. But it came at a huge cost to the government, which paid out USD$67 million (6.7 billion

Kenyan shillings) between May and October 2017.

Once the subsidy ends, consumer prices are expected to increase by approximately 15% based on simulations done by Tegemeo Institute, the policy research institute of Egerton University.

Adding to the upward pressure on prices is the increase in the money the government is making available to buy maize stocks. It usually buys maize at a price higher than the market price. This has the effect of raising the market price – and undermining the objective of reducing consumer prices.

Ideally, government should intervene on either the supply side or the demand side, but not both. For example, it could intervene to keep the costs of production as low as possible so that consumers would buy food at market prices. Alternatively, it could allow producers to sell at market prices and subsidise consumers who cannot afford these prices. The consumer subsidy model has been used by India and Egypt, where households are given a cash transfer to purchase food.

It has been argued that in the Kenyan model farmers enjoy a double subsidy. They get subsidised inputs and above-market prices from government. This forces millers to offer even more attractive prices to compete with government for farmers' maize stocks. This puts inflationary pressure on consumer prices.

The USD$60 million allocated to replenish the grain reserve is significant given that for the current year the government had allocated USD$18 million (increasing the allocation by more than 400%). But it won't mop up the current harvest. Government will buy a quantity determined by the price it offers farmers. Maize farmers have a strong lobby which has influenced the price. A high price means less is purchased. Purchasing less quantities effectively leaves the government

unable to affect the price of grain by increasing supply when it falls short, a key objective of the strategic food reserve.

The government has announced that it will buy maize from farmers at Ksh.3,200 per 90kg bag. At this price, the government will buy 1.8 million bags, or only 6% of the current harvest. Monthly consumption is 3.3 million bags. The recommended quantity is three months cover. A three months cover allows the government to increase supply during when it falls short and thereby stabilise prices, while allowing time to source for more grain.

And the country will still have to import maize because it isn't producing enough. Tegemeo Institute, assessing the food situation for maize and rice production in 2017, estimates that the maize harvest will be about 20% lower than this year. Erratic rain and an army worm infestation are the main reasons.

Usually, millers are forced to offer a price higher than the government price to purchase enough quantities for milling. For example, when the government buys maize at 3,200 shillings per bag, millers will buy at 3,400 shillings, which is 6% higher. Without the subsidy that guaranteed consumers a lower price, for which millers were guaranteed a subsidised price of 2,300 shillings, it is expected that millers will pass on much of the increase in maize prices to consumers. This will amount to 40% if they buy at Sh3,200 or 48% if they buy at Sh3,400. Therefore, to keep the consumer price unchanged, government may be forced to subsidise consumer prices or offer a rebate to millers.

The third move by the government was to lower the cost of fertiliser, offered through government subsidy.

Farmers will welcome the move. Research by Tegemeo Institute found that fertiliser accounted for about 15% of the cost of production in

2017. But, as has been shown before, there is a need to investigate how the subsidy increase will affect private-sector fertiliser markets.

Longer-term solutions

To maintain stable production and prices, the government should focus on long-term interventions that will improve productivity and lower the production costs per unit.

It needs to plan better. For example, it must plan now for imports to meet the expected shortfall.

And the type of fertiliser that's subsidised should suit local conditions. Tailored fertilisers have an effect on improving maize yields.

When short-term intervention in the markets is required, it should be strategic and with a clear exit strategy. Such a response should be limited to managing shocks such as pest infestation and disease outbreaks. Currently, short term interventions seem to the only response, leading to the same challenges being repeated.

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